

RMBS Seller/Servicers  
Australia/New Zealand  
Servicer Report

# Bluestone Servicing Pty Ltd. Bluestone Servicing NZ Ltd. Bluestone Special Servicing Pty Ltd.

## Ratings

	Current Rating
<b>Bluestone Servicing Pty Ltd.</b> Servicer Rating (Primary) for non-conforming RMBS	2-(AUS)
<b>Bluestone Servicing NZ Ltd.</b> Servicer Rating (Primary) for non-conforming RMBS	2-(NZL)
<b>Bluestone Special Servicing Pty Ltd.</b> Servicer Rating (Special) for non-conforming RMBS	2(AUS) 2(NZL)

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## Related Research

- [Rating Australian and New Zealand Sellers, Servicers and Trust Managers \(April 2006\)](#)

## Summary

Fitch Ratings has upgraded the Servicer (Primary) Rating to '2-' from '3+' of Bluestone Servicing Pty Ltd. and Bluestone Servicing NZ Ltd. for the primary servicing of non-conforming residential mortgages in Australia and New Zealand. The Servicer (Primary) Rating assesses the operational risk attributable to the company's primary servicing of non-conforming residential mortgages.

In addition, Fitch has affirmed Bluestone Special Servicing Pty Ltd.'s Servicer (Special) Rating of '2'. The rating covers the special servicing function of non-conforming residential mortgages in Australia and New Zealand.

Bluestone Servicing Pty Ltd. and Bluestone Servicing NZ Ltd. are majority owned subsidiaries of Bluestone Group Pty Limited (Group). All three servicing companies will hereafter be referred to as 'Servicing' for the purposes of this report.

The ratings reflect Servicing's experienced management team, proactive servicing and arrears management procedures and the enhancements to its servicing systems.

## Strengths

- Experienced management, loan servicing and collections teams.
- Proactive risk and arrears management policies.
- Significant investments in improving servicing systems to allow increased efficiencies and functionalities across servicing operations.
- Strong and advanced IT systems, supported by a well resourced in-house IT team.

## Areas of Concern

- Servicing is expanding its third party operations off its existing platform.
- Servicing's ability to maintain and improve operations under challenging market conditions.

## Mitigants

- Servicing has sufficient capacity and resources in place to take on additional third party servicing responsibilities and has a successful track record of converting portfolios from external systems on to its own platform.
- Servicing should be able to meet its ongoing commitments and has various strategies in place to ensure it can withstand current market conditions going forward.

## Company History and Management Experience

### Company History

Servicing was established in 2006 and commenced operations with servicing of the Bluestone Australia non-conforming residential mortgage portfolio in April 2007 (including the transition of the Group special servicing team). Servicing conducts the primary and special servicing operations of Group's warehouses and trusts and also provides servicing to third parties.

Group, a privately owned company, was established in 2000 by its founder and chairman, Alistair Jeffery. The company expanded its non-conforming mortgage business to New Zealand in 2002. This was followed by the launch of its reverse mortgage business in 2004 and, in 2007, Bluestone added the commercial mortgage business to its expanding product range.

As of December 2008, Bluestone had originated more than AUD4.8bn worth of loans, and completed a total of 17 securitisations in both countries. Servicing manages a non-conforming residential mortgage programme (Sapphire, established in 2002), a reverse mortgage programme (Emerald, established in 2006), commercial mortgage programmes, prime mortgage programmes and a motor vehicle loan portfolio.

### Management Experience

Servicing has an experienced core management team. The majority of team members have been with Bluestone Group for a number of years and have played important roles in the development and implementation of Servicing's operations.

Mike Dilworth is the Chief Executive Officer of Servicing and oversees the overall servicing operations. Prior to his role at Bluestone, he served as the CEO of AFIG's operations from 2003 to 2005. Before his role at AFIG he was responsible for the operations at the Westpac mortgage processing centre in Adelaide.

Bluestone Servicing is managed by a team of key executives with extensive third-party servicing and securitised, wholesale funding, collections and IT experience. All played dedicated roles in the establishment of Servicing as a functional business, including the evaluation, selection and implementation of its technology platform and have gone on to make up the senior operational management team of the business.

### Financial Condition

Servicing generates its revenue from servicing fee income from servicing the Group's warehouses and trusts which include the primary and special servicing fees and trust management fees and from third-party servicing fees. Servicing also generates Sundry fees which include account management fees, dishonour fees, late payment fees, discharge fees and notice of default fees.

As Servicing is defined as a small proprietary company, it is not required to prepare financial reports. However, Servicing's management accounts and cashflow projections were made available to Fitch. According to the information provided to Fitch, and under conservative assumptions, Servicing will be able to meet its financial obligations.

### Staffing and Training

Servicing is staffed by 85 people (70 in Australia and 15 in New Zealand). Many are cross-trained and are able to be interchanged across teams depending upon the demands of the business.

Servicing has extensive training programmes in place. All new employees undergo induction training upon joining the company. The training highlights the company's business model and provides inductees with an overview of each area Group's

business.

As part of their ongoing training, employees are required to successfully complete compliance training for the Uniform Consumer Credit Code (UCCC) and the Privacy Act, in addition to attending various internal and external training seminars (held by various practitioners in the industry). Employees may also be provided with external study support for approved courses.

### Primary Servicing

Phil Hurditch, the General Manager of Servicing, was previously Head of Operations at AFIG for five years prior to joining Bluestone.

The performance of the primary servicing team is monitored via key performance indicators such as: answering inbound calls within a certain period of time and actioning various loan administration tasks such as loan discharges, further advances and redraws within a strict timeframe.

### Special Servicing

Graham Horne, the General Manager of Special Servicing has more than 26 years' collections experience in residential mortgages and has been with Group and Servicing for five years.

Overall, the collections team has, on average, 10 years' experience, of which average tenure at Group and Servicing is almost three years.

The collections team undergoes extensive training. New members are assigned to the internal collections trainer then rotated amongst the various collections areas, with formal reviews conducted on a monthly basis by the team leader. Members are also required to spend time training with the primary servicing team.

It should be noted that the special servicing team is monitored by key performance indicators which include: promises made by the borrower to pay; promises kept by borrowers; amount collected from borrowers; and the number of calls handled per week. The performance of all team members is shared amongst the team on a regular basis to encourage healthy competition and improved performance.

## Risk Management and Compliance

### Risk Management Framework

Servicing has strong risk management and compliance policies in place and various committees oversee its compliance obligations. Some of these committees are:

- Compliance and Risk Committee - oversees the compliance and operational risk activities. This committee also reports non-financial information to the Group's Board Audit and Compliance Committee;
- Trust Management Committee - responsible for ensuring accurate and timely payment of distributions to noteholders and related parties by the trusts;
- Credit Committee - responsible for setting and reviewing credit/underwriting policies and arrears (from time-to-time, policy changes may be considered by relevant members of this committee as part of a project team working on a loan product initiative).

Other responsibilities of the compliance team include: conducting quarterly internal audits on Servicing's operations; and ensuring employees undergo risk management training and pass online assessments. Annual training for the Privacy Act, Anti Money Laundering and Counter Terrorism Financing Act and the UCCC for all staff is conducted via the intranet, with all procedures manuals available on the intranet. All training manuals are reviewed and signed off by legal and compliance before distribution. External legal advice from Gadens Lawyers is also used for any

legal updates where appropriate.

In addition, the Compliance officer meets with each department head on a regular basis, to identify, discuss and document the potential risks faced by their area. The risks are then listed in a matrix and graded as 'high', 'significant', 'moderate' or 'low', and responsibility for managing these risks is assigned to the department head, who will be responsible for reducing this risk to an acceptable level.

The department head has a designated timeframe to reduce or eliminate this risk, which is then reassessed at the next risk review meeting. The Compliance officer reviews the matrix on a quarterly basis with the department head, and the department head must continue to monitor such risks. The compliance team is responsible for distributing the results of the risk assessments to the managers on a regular basis.

## **Disaster Recovery, Business Continuity and Technology**

The business continuity plan for Servicing forms part of the overall plan for Bluestone Group.

Servicing established a formal business continuity plan team in 2006 to determine the recovery requirements of each business unit. A Business Continuity Plan manual is reviewed and updated on a regular basis, with the most recent review in August 2008.

Servicing utilises a multi-tiered data protection strategy. A centralised storage architecture is in place which utilises disk-based snapshot technology to facilitate replication of data between production and development environments at head office, as well as real time replication to the disaster recovery site. This disk-based protection is supported by traditional overnight tape backups that are stored offsite with a specialised data storage company.

Critical software applications, such as the BOSS loan origination and servicing system, are backed up hourly and replicated continuously to the DR site. One month's worth of replicated data is kept at the disaster recovery site. Daily tape back-ups are kept for 35 days, monthly backups are kept for one year and yearly backups are kept for 10 years. This strategy enables data recovery to be performed from either head office, the disaster recovery site or from tape, dependant on the age of the data required or the level of disaster experienced.

The offsite disaster recovery site has provision for 25 seats, with workstations and telephones. Priority is given to servicing staff. Disaster recovery tests are performed on an annual basis, with the most recent test successfully completed in February 2009.

Servicing has advanced and sophisticated IT systems in place which are supported by a suitably qualified IT group, comprising ten employees. The team is split between infrastructure/support and development, with IT contractors employed on a needs basis.

Some of the core systems include: Bluelink, an online tool that allows brokers to submit electronic loan applications; BOSS, the loan origination, settlements and servicing system developed by Axxess Consulting and customised by the Servicing IT group; and SUN, the company's finance, treasury and general ledger system.

Servicing's operations are heavily reliant upon technology and security is monitored closely by the IT department. Internet facing systems to support Bluelink, Internet Banking and the public web sites are hosted internally with three separate internet links, all with different service providers spread across the head office and disaster recovery sites to ensure constant uptime. In the event of any power failure, there are provisions in place such that a dedicated, uninterrupted power supply will

provide approximately one hour of power for each device in the server room.

The Bluestone Group's network architecture is comprised of a number of local area networks (LAN) and a wide area network (WAN). All network infrastructure is centrally located in Sydney.

Extensive security and change management systems are in place allowing real-time systems monitoring and compliance and change software (which records any server changes throughout the business and is reconciled against a control log). Furthermore, user accounts are reconciled against the Human Resources list - allowing detection of any unauthorised user accounts - and daily reports are created on firewall and web server logs.

## Primary Servicing

Group's primary servicing operations were transferred in-house to Servicing in April 2007 (for the Australian operations) and in June 2007 (for the New Zealand operations). The primary servicing operations were previously outsourced to AFIG.

The primary servicing team includes a contact centre plus variations, trust management and transactional processing teams.

The contact centre responds to incoming queries regarding the general administration of loan accounts and a customer service team processes more complex variation matters such as further loan advances, partial discharges and product switches.

The trust management team handles the collections of all income from the trusts, preparation of the interest payment determination reports, interest rate swaps and investor reports.

The transactional processing team is responsible for matching all transactions to the cash received in the bank collection accounts for each mortgage pool. The group conducts daily reconciliation processes to ensure that all transactions are coded and posted correctly, following a strict daily routine and cut-off times. Servicing has its own dedicated Westpac branch number, which allows inward direct credits and debits to be processed automatically to loan accounts.

The BOSS servicing system is a windows-based application with restricted access, dependant upon the user's authority level. Servicing staff are able to view the loan application amount, principal balance owing, amounts in arrears, type of product, approved loan-to-value ratios and current loan-to-value ratios. The servicing team is also able to calculate live payouts on loans instantaneously. Servicing's primary servicing processes are detailed in its servicing procedures manual, which is made available to all staff and accessible online.

Warehouses or trusts within the BOSS system can be tagged to a specific funder or series of funders to allow the loans to be identified easily. The system allows for each warehouse and trust to have its own separate management reporting, reconciliations, and ability to track the movement of loans within a funding pool.

Applications that interface with the BOSS servicing system include the origination processing workflow system. This system allows users to order online credit reference checks with VEDA and obtain the results of searches from ASIC. In addition, users may validate acceptable property locations, confirm property addresses, review geographic concentration risks, and issue panel solicitor instructions and settlement disbursements.

The BOSS system has allowed Servicing to develop a wide range of exception reports to continually check the integrity of data. These reports are reviewed and actioned on a daily basis. Furthermore, a summary report, listing all exception reports, is issued daily and distributed to management. A powerful feature of the

reporting system on BOSS is the ability for users to customise reports according to the user's requirements.

The BOSS servicing system is also linked directly with the company's general ledger system eliminating the need for any manual processing and ensuring the accuracy of information.

## Special Servicing

All mortgage collections from Australia and New Zealand are handled out of Servicing's headquarters in Sydney, where the team includes a manager specialising in property in possessions (PIP). Various team members are able to assist in foreclosures and PIP should the need arise. The team has approximately 7500 accounts under management.

On average, the collections team share more than 10 years' collections experience, and have on average served three years at Bluestone. The team is arranged into the following arrears buckets according to experience: 0-30 days; 31-60 days; 61-90 days; and 91 plus days. More experienced team members are assigned to manage the higher arrears categories, which will also include foreclosures. This arrangement allows staff to specialise in particular areas.

Servicing's processes for dealing with arrears are covered in its collections manual, which is issued to all staff as part of their induction training and is also available online. The overriding aim is to use legal action as a last resort. The collections manual stresses that people who fall into arrears may have fallen into hardship - such as loss of employment or divorce - and that collection processes must be both sympathetic and at all times professional.

Servicing has a firm and proactive approach to the management of its borrowers. All special servicing staff are experienced mortgage collectors, aware of the internal/external avenues of assistance that can be utilised to resolve arrears.

The collections team takes a proactive approach, with welcome calls and pre calls made to all borrowers before their first payment, and before the next three payments if their first payment is missed. SMS texts are sent to all borrowers two days before the first payment and for three months after it is cured. All borrowers must pay via direct debit. All missed payments are investigated within 24 hours and all calls are recorded.

If no phone contact is made, the field agent visits the borrower's home to rectify the account. If an arrangement is made with the borrower, then the collections team will actively monitor the account. If an arrangement with the borrower cannot be made, or the arrangement is breached, the collections team will issue a notice of demand. If the borrower ignores this notice, legal action commences to take possession of the property. In addition, Servicing also actions what it terms 'health checks' or 'home visits' in cases where it believes a more personal approach is required. The team looks at alternative solutions including: extra payment plans; accessing superannuation for financial hardship; referral programmes; or granting moratoriums.

Arrears reporting is generated from the BOSS system and can be sorted separately by warehouse and trust. The system allows the teams to analyse the arrears data in numerous ways, including: graphing arrears buckets against a benchmark index; identify trends by country, funder, or product; and tracking arrears movements under various categories.

## Default Management and Enforcement

Because of the higher level of scrutiny and maintenance required for the type of borrowers Group specialises in, the default management and enforcement process

is fairly extensive and plays a major role in Servicing's servicing activities.

It should be noted that legal action is only taken when the borrower is unable or unwilling to correct arrears after exploring all other options. However, as at the time of Fitch's review, the collections team had more than 100 properties in possession. The team conducts weekly status review meetings, with all properties tracked on the PIP reporting system. BOSS produces a PIP report that details information on all past and current properties, including the number of properties taken and discharged, the value of properties held, and tracking of historical PIPs.

Panel solicitors are instructed to obtain possession of the property with a statement of claim being served on the borrower. If the borrower does not lodge a defence, the collections team seeks both a judgment and a writ of possession from the Supreme Court and prepares an affidavit of debt. Once granted by the court, notice to vacate is served on the borrower. Once in possession, insurance over the property is arranged and valuation by a panel valuer and two market appraisals are conducted by local real estate agents are obtained. Once received, the collections team makes an assessment of the property to determine whether repairs are required to add value to the property. When this is completed, a reserve price is set and the property is listed for sale by private treaty or auction. The collections team will conduct regular property inspections to ensure the property for sale is maintained to a presentation standard. In its experience, the collections team has found it takes approximately 11.3 months from default to discharge. To date, the collections team has been able to successfully achieve property sales close to or above the valuation of the property.

### **Surveillance of Servicer Ratings**

The agency's Servicer Ratings remain current until they are updated or withdrawn. The agency aims to review the operations of the rated entity on an annual basis, or earlier if there are material changes to the entity's operations.

Information about current Servicer Ratings can be found on the agency's website at [www.fitchratings.com](http://www.fitchratings.com).

## Appendix 1

### Rating Scale

Ratings will be assigned on a scale of one to five. Additionally, + (plus) and - (minus) will be used to further granulate the scale. The rating will describe the function being rated and identify the asset class.

The servicers at level one are expected to have all areas of their company operating at top efficiency and productivity. Characteristics of a level one (1) servicer may include:

- Demonstrated expertise in servicing a diverse portfolio, i.e. loan type, property type, and geographical concentration among others.
- Highly seasoned management team with a substantial working history together.
- Stable employee base with little turnover.
- Very strong and stable financial resources.
- Very well documented and complete policies and procedures, which are readily available to all employees.
- Fully integrated, flexible systems with versatile reporting capabilities.

Characteristics of a level two (2) servicer may include:

- Effective management of a diverse portfolio.
- Seasoned management team with a history of working together.
- Stable employee base.
- Strong, stable financial resources.
- Well documented and complete policies and procedures.
- Strong systems and reporting capabilities.

Characteristics of a level three (3) servicer may include:

- Demonstrate proficiency in servicing diverse product groups.
- Adequate financial resources for its portfolio size.
- Effective internal controls.
- Proven proficiency in staffing and training.
- Established comprehensive policies and procedures.
- A master servicer must have experience and controls in place for monitoring primary servicers and other sub-servicers.
- A special servicer must demonstrate adequate workout and disposition experience.

Servicers that receive a level four (4) rating may be incompatible with the servicing criteria employed by Fitch Ratings in rating CMBS or RMBS transactions, unless additional support or structural features are incorporated. Listed below are a few situations that could cause the assignment of a level four (4) rating:

- Length of time or experience in servicing type or product type.

- Recent event that has not had time to be resolved or its effect fully assessed (i.e. merger, acquisition, change in management, or system conversion, among others).
- Specific concern or problem with the servicer.

Residential mortgage servicers that receive a level five (5) rating exhibit aspects in their operations, process, or financial condition that are incompatible with Fitch Ratings' criteria for rated RMBS transactions unless strong additional support or structural features are incorporated.

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