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*Asset-Backed Commercial Paper
Criteria Report: U.S. ABCP
Conduits – Credit and Liquidity*

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Insight beyond the rating.

AUTHOR

Matthew La Capra, CPA

CONTACT INFORMATION

Andrew Jones

Managing Director, Structured Finance
TEL +1 212 806 3250
ajones@dbrs.com

Matthew La Capra, CPA

Senior Vice President, Structured Finance
TEL +1 212 806 3259
mlacapra@dbrs.com

R. Dorothy Poli

Senior Vice President, Structured Finance
TEL +1 212 806 3261
dpoli@dbrs.com

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Asset-Backed Commercial Paper Criteria Report: U.S. ABCP Conduits – Credit and Liquidity

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The DBRS U.S. Asset-Backed Commercial Paper Conduit Rating

PRIMARY RISKS OF ABCP

U.S. asset-backed commercial paper (ABCP) is a short-term debt instrument issued by a conduit and backed by a variety of individual asset-backed transactions. In order to issue a short-term rating on commercial paper (CP) issued by an ABCP conduit, DBRS analyzes the comprehensive risk profile of the conduit, focusing on the four primary risk areas, two of which, credit risk and liquidity risk, will be examined closely in this report:

- Credit risk.
- Liquidity risk.
- Legal risk.
- Operational risk.

This report generally does not cover legal and operational risks with respect to ABCP conduits.

DBRS SHORT-TERM RATING

General

Regardless of the debt instrument the conduit issues, DBRS rates to the CP investor being paid in whole and on time. Payments that are not timely or complete constitute a default.

The chart below illustrates how DBRS's short-term ratings approximately correlate with other rating agencies' short-term ratings.

More Gradations

With more short-term rating gradations than other rating scales, DBRS offers CP investors more information and transparency. DBRS's ratings of R-1 (high), R-1 (middle) and R-1 (low) on an ABCP conduit range from a AAA to an A (low) risk profile. DBRS believes that investors can better understand risks inherent in ABCP portfolios through more granular short-term ratings.

Short-Term Ratings Scales Comparison

DBRS	S & P	Moody's	Fitch Ratings
R-1 (high)	A-1+	P-1	F1+
R-1 (middle)	A-1	P-1	F1
R-1 (low)	A-1	P-1	F1
R-2 (high)	A-2	P-2	F2
R-2 (middle)	A-2	P-2	F2
R-2 (low)	A-2	P-2	F2
R-3	A-3	P-3	F3
All ratings below R-3	All ratings below A-3	All ratings below P-3	All ratings below F3



Commercial Paper Fundamentals

An ABCP conduit is a special-purpose vehicle that is structured to be bankruptcy remote and legally separate from its sponsor. The conduit acquires assets via an asset purchase or a secured lending transaction. Some common assets or asset interests that ABCP conduits finance are trade receivables, auto and equipment loans and leases, credit-card receivables, mortgages and collateralized debt obligations (CDOs). ABCP is generally limited to a 270-day tenor and is issued on either a discount or interest-bearing basis.

BASIC MECHANICS OF ABCP STRUCTURES

ABCP Conduit Revolving Phase

An ABCP conduit is a vehicle that is usually intended to last until a program wind-down occurs. CP is issued against transactions that have been accumulated over time. During the revolving phase, an ABCP conduit typically acquires and retires transactions at the same time as it issues and retires CP.

- **Payment of Interest on Commercial Paper and Conduit Fees:** Although interest is typically covered transaction by transaction by the liquidity facilities, the conduit's sponsor and/or administrator designs the program to cover interest and CP conduit fees in one of two ways:
 - **Interest-Bearing Assets:** For transactions that have underlying interest-bearing assets, typically interest collected on the assets pays the interest on the CP and the conduit fees.
 - **Non-Interest-Bearing Assets:** For transactions that have non-interest-bearing assets, typically additional reserves in the form of overcollateralization are established to cover interest and conduit fees.
- **Payment of Principal on Commercial Paper:** During the revolving phase, the conduit will issue new CP in order to retire maturing CP in a process called "rolling the CP." CP can only be rolled against performing transactions. Rolling the CP typically repays 100% of the principal component of maturing CP.

ABCP Conduit Wind-Down Phase

- **Voluntary Wind-Down:** For various reasons, program sponsors may choose to wind down a CP conduit. In this case, the portfolio of transactions may naturally amortize. During the natural amortization of the transactions within the conduit's portfolio, maturing CP is typically paid by both collections from the assets and from issuing new CP. This will recur until the conduit's transactions are completely amortized. Alternatively, banks may choose to fund some or all of the transactions with a liquidity facility, thereby immediately removing any or all of the transactions from the conduit.
- **Involuntary Wind-Down:** An involuntary conduit wind-down may occur if the conduit breaches specific program triggers that are set out at the conduit's inception. The "Program-Level Structural Features" on page 16 outlines some of the material triggers that would invoke an involuntary conduit wind-down.

CONDUIT CLASSIFICATIONS

Several features distinguish conduits from one another:

- **Conduit Type:** Key conduit types are multi-seller, single-seller, arbitrage programs, hybrids and structured investment vehicles (SIVs).
- **Conduit Liabilities:** The general types of debt issued are CP, extendible CP and medium-term notes (MTNs).
- **Conduit Credit Variations:** All conduits are either fully or partially supported.
- **Conduit Liquidity Variations:** The liquidity facilities provided to conduits are either full or partial/alternative.

The criteria and methodologies described in this publication generally relate to partially supported multi-seller programs, which are the most prevalent type of conduit in the U.S. ABCP market.



Conduit Types

• Multi-Seller Conduit

- **General:** A multi-seller conduit is a limited-purpose, bankruptcy-remote vehicle that provides funding to a multitude of unaffiliated originators/sellers in exchange for asset interests.¹ Individual sellers' assets are acquired transaction by transaction, typically accumulating into a diversified portfolio across asset types and industries to support the CP issued by the program.
- **Credit:** Each transaction that is added to the conduit's portfolio must be structured and/or credit enhanced so that the resulting risk profile of the CP conduit is commensurate with its CP rating. Program-wide credit enhancement (PWCE) is available as a fungible layer of credit enhancement across all transactions (see "Program-Wide Credit Enhancement" beginning on page 15 for more details). An integral part of assessing the CP risk profile of a conduit is the size of its PWCE relative to the size and composition of its portfolio of transactions.
- **Liquidity:** A liquidity bank, typically the conduit's bank sponsor, provides a liquidity facility for each transaction to address timing mismatches between the payment streams of the assets and the CP maturity dates or to repay CP investors in the event that CP cannot be rolled, including a market disruption.² Liquidity facilities typically do not fund for defaulted assets. Sponsor banks providing liquidity may use the facility to transfer the transaction out of the conduit for any reason. As an alternative to traditional liquidity facilities, multi-seller conduits may have an extendible CP feature. Please see "Extendible Commercial Paper" on page 10 for more details on extendibles.

• Single-Seller Conduit

- **General:** A single-seller conduit is a limited-purpose, bankruptcy-remote vehicle that provides funding to a single seller in exchange for interests in its pool of receivables. Single-

seller programs are popular among large credit-card issuers, major auto manufacturers and mortgage originators.

- **Credit:** As is the case for multi-seller conduits, single-seller conduits acquire transactions that are structured and/or credit enhanced so that the resulting risk profile of the CP conduit is commensurate with its CP rating. Credit enhancement addresses historical and projected asset deterioration at a particular rating level commensurate with the risk to the CP investors.
- **Liquidity:** As in the case of multi-sellers, the liquidity provider(s) address timing mismatches between the payment streams of the assets and the CP maturity dates or issues that arise when CP cannot be rolled, including a market disruption. If the seller's short-term rating is high enough, it may serve as the liquidity provider. If not, one bank or a syndicate of liquidity banks may serve as the liquidity provider(s). As an alternative to traditional liquidity facilities, single-seller conduits may have an extendible CP feature. Please see "Extendible Commercial Paper" on page 10 for more details on extendibles.

• Arbitrage Conduit

- **General:** An arbitrage conduit is a limited-purpose, bankruptcy-remote program that invests specifically in explicitly rated securities. Generally, the primary impetus for forming these vehicles is an arbitrage motive. Arbitrage conduits typically buy high-yield or longer-term securities or both. They fund these securities with lower costing and shorter-term CP and collect the resulting spread.
- **Credit:** Arbitrage programs are primarily composed of explicitly, highly rated transactions. Each transaction that is added to the conduit's portfolio must be rated appropriately such that the resulting risk profile of the CP conduit is commensurate with the rating on the CP issued. An explicit rating addresses the timely payment of periodic interest and ultimate payment of principal on the legal final date.

¹ The conduit's portfolio consists of transactions collateralized by underlying assets. Such underlying assets are referred to herein as "underlying assets," "assets" or "collateral." The conduit's interest in these transactions is referred to herein as "asset interests."

² Market disruption in the CP market results in investors ceasing to purchase CP.



PWCE is required as needed depending on the mix of the ratings of the transactions within the conduit's portfolio.

- **Liquidity:** Traditionally, liquidity would fund for the principal and interest on the CP unless the security's or, if applicable, the third-party enhancer's³ rating migrated downward to near default status. However, regulatory changes have spurred liquidity, in some programs, to cover only investment-grade assets. The latter necessitates additional credit enhancement or structural features in those particular transactions. Similar to the multi- and single-seller programs, as an alternative to traditional liquidity facilities, arbitrage conduits may have an extendible CP feature.

• Hybrid Conduits

- **General:** A conduit that has more than one feature can be characterized as a hybrid. A common hybrid is the multi-seller arbitrage conduit, which both provides financing for a multitude of sellers and also purchases explicitly rated securities. As a result, a hybrid conduit has similarities to both arbitrage and multi-seller conduits.
- **Credit:** The transactions that hybrid conduits acquire must be structured and/or credit enhanced so that the resulting risk profile of the CP conduit is commensurate with its CP rating. For sellers, the credit enhancement can be in the form of overcollateralization, subordination, excess spread, third-party guarantees, lines of credit (LOCs) and other types. As is the case for both multi-sellers and arbitrage conduits, PWCE is available as a fungible layer of enhancement across all transactions, although some explicitly, very highly rated⁴ transactions may not be required to post PWCE but typically can still benefit from this extra layer of enhancement.
- **Liquidity:** The liquidity funding formula can vary transaction by transaction depending on the transaction's characteristics as well as the type of collateral that underlies the transaction.

• Structured Investment Vehicles

- **General:** An SIV is a specialized type of conduit that invests in highly rated securities but has less than full liquidity support because of the expected liquidation value of the highly rated securities. SIVs are designed to be bankruptcy remote, with characteristics of both structured finance and operating companies. As such, there is an active reliance on the managers of the SIVs. They generally invest in a diversified portfolio of highly rated, typically AAA, longer-term securities that collectively have a greater yield than the cost of the liabilities they issue. Liabilities typically comprise CP, MTNs and subordinated capital notes.
- **Credit:** Credit enhancement is typically in the form of subordinated capital notes. The required credit enhancement is sized via a simulation-based capital model or an appropriately vetted capital charge matrix. The model or the matrix sizes the credit enhancement considering the period required to liquidate the underlying portfolio. At all times, the liquidation proceeds plus the credit enhancement must be sufficient to pay the rated liabilities issued by the vehicle.
- **Liquidity:** SIVs have an innovative liquidity structure. In general, their liquidity needs can be covered by the inherent liquidity in the SIV structure. The inherent liquidity in the SIV structure typically includes but is not limited to available unencumbered cash on hand, liquidity eligible assets (LEAs)⁵ and standard liquidity loan facilities. The manager of an SIV has some or all of these tools at its disposal to ensure that the vehicle can meet its cash outflows (fees, maturing CP and MTNs, as well as swap payments, if any).

Typically, during the revolving phase, cash inflows from the underlying securities and any available inherent liquidity in the SIV structure must be sufficient to retire maturing liabilities and all other cash outflows over specific periods of time. Because the liquidity loan facility is one component of the inherent liquidity in the SIV structure, it is typically a fraction of the size that is required for traditional CP conduits.

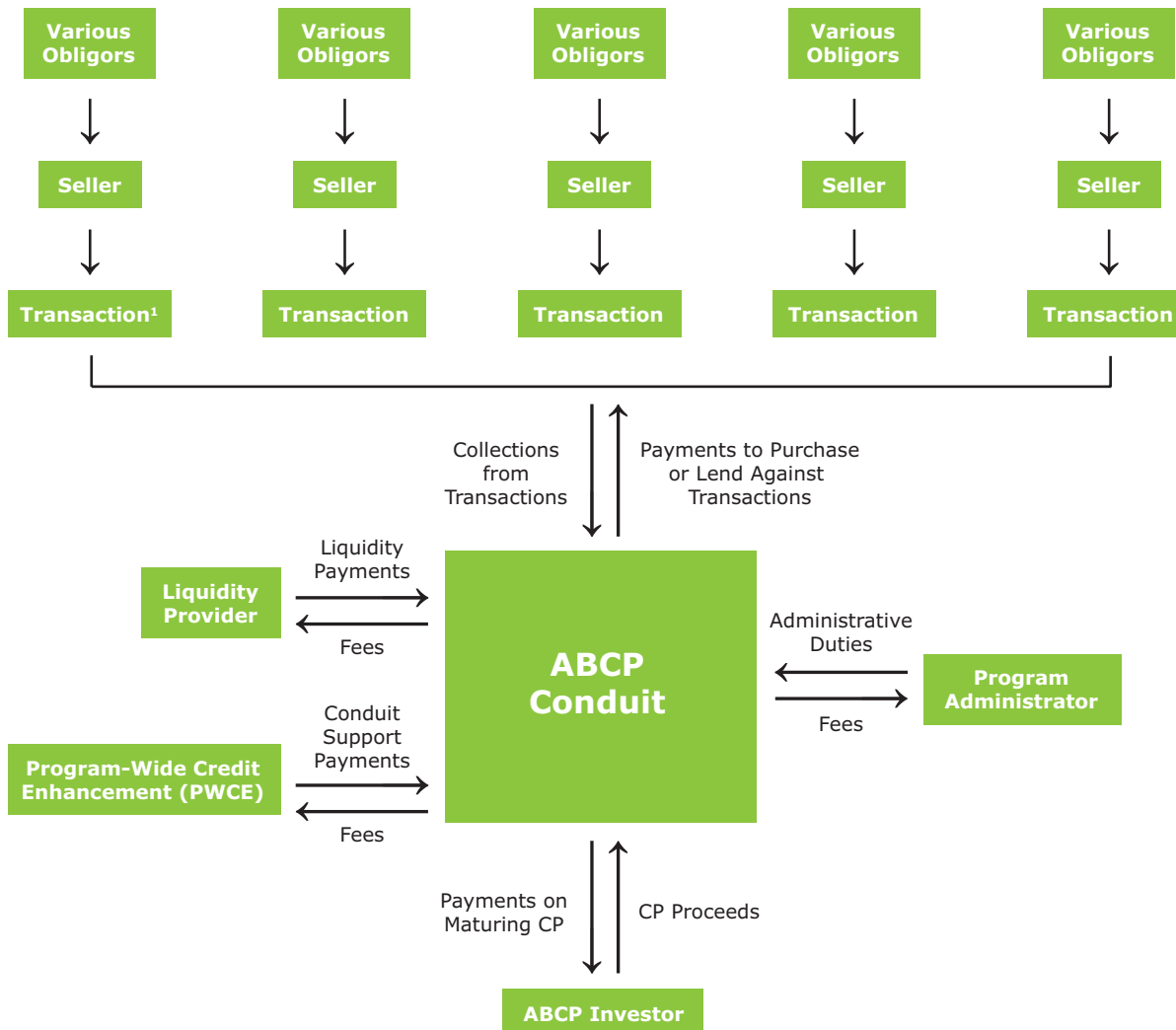
³ A third-party enhancer is typically a highly rated guarantor affiliated with the transaction participants or a monoline insurer rated AA or higher.

⁴ Those explicitly rated transactions that are rated higher than the CP issued from the conduit may not be required to post PWCE.

⁵ Liquidity eligible assets (LEAs) are eligible assets that are highly liquid.



Typical Partially Enhanced Multi-Seller ABCP Conduit Structure



¹ The transactions that the ABCP conduit acquires represent the special purpose vehicles (SPVs) that the sellers typically set up to facilitate the conduit's acquisition of the transaction.

An uncured breach of any cash outflow coverage tests will cause a cease issuance of all liabilities, resulting in the defeasance of the SIV and consequently the liquidation of the underlying portfolio. During the defeasance stage, all inherent SIV liquidity and future cash proceeds from the liquidation of assets should be sufficient to retire the liabilities in full and on time over the liquidation period until the SIV vehicle winds down completely.

Conduit Liabilities

- **Commercial Paper**

ABCP is generally structured to comply with Rule 2a-7 of the *Investment Company Act of 1940*. It is generally 270-day⁶ short-term debt and issued on a discount or interest-bearing basis. The most common form of conduit issuance is fixed-rate CP, issued at a discount with the face value due at maturity.

⁶ CP issued in the United States typically has a term of no longer than 270 days. In the case of CP extendible programs, the tenor could be as long as 397 days.



- **Discounted CP:** The investor purchases discounted CP for a price that is less than the face amount due at maturity. The interest is imputed from the difference between the purchase price and the face value. It cannot be prepaid by the issuer or redeemed by the investor prior to maturity.
- **Interest-Bearing CP:** Interest-bearing CP accrues interest on the amount of the investor's purchase price paid for the CP. The investor will collect all interest and principal at the maturity of the CP. It also cannot be prepaid by the issuer or redeemed by the investor prior to maturity.
- **Extendible Commercial Paper**
Extendible CP is characterized by having both an expected maturity date and a later final maturity date. If CP does not roll on the expected maturity date, the program is designed such that the conduit's administrator has the option of extending the payment on the CP until the legal final maturity date. During the extension period, the conduit either relies on the cash flows from the amortization of the assets (e.g., credit cards or trade receivables) or the cash flows from the sale of the assets (e.g., mortgages) in order to pay the CP. Although the extension of the CP is very unlikely, DBRS assumes extension and thus rates to the legal final maturity date.
- **Medium-Term Notes**
MTNs have tenors ranging from 270 days to 30 years but are typically issued with maturities ranging from one to ten years. MTNs are rated with long-term ratings. They can be issued at a fixed rate but are typically floating-rate instruments that make periodic interest payments. They do not qualify as an eligible investment for money market funds under Rule 2a-7 unless their maturities are less than one year. They are not especially common among typical ABCP conduits but are issued extensively out of SIV structures. SIVs may use MTNs as a tool to manage liquidity requirements.

Conduit Credit Variations

- **Fully Supported:** Fully supported ABCP conduits are distinguished from partially supported programs because they are 100% credit enhanced by an appropriately rated entity. For these conduits, the analysis is not focused on the underlying collateral, but rather on the party providing the credit enhancement. The risk to the CP investor is that the credit enhancer itself becomes insolvent. The documents must dictate that the enhancer will irrevocably and unconditionally pay the liabilities in full and on time. The enhancer is often the sponsor or a financial guarantor.
- **Partially Supported:** Partially supported programs are far more prevalent in the ABCP market than fully supported programs. They are characterized by having less than 100% credit enhancement. The analysis for partially supported conduits focuses on the transactions within the conduit and on the PWCE available.
 - **Transaction-Level:** The transaction analysis focuses on the credit quality of the underlying collateral, the liquidity-funding formula, the transaction-level credit enhancement and the structural and legal protections. Credit enhancement at the transaction level represents the first-loss protection to the CP investor.⁷
 - **Program-Level:** The program-level analysis focuses on the size of the PWCE relative to the overall composition of the conduit's portfolio of transactions as well as program structural and legal features. PWCE is generally regarded as second-loss protection to the CP investors.

Conduit Liquidity Variations

- **Full Liquidity:** Full-liquidity programs are far more prevalent than partial-liquidity programs. Full-liquidity programs typically provide 102% liquidity support to the transactions within the CP conduit. Typically, these facilities will not fund for defaulted receivables. The surplus 2% liquidity support is used to mitigate interest rate risk, but it is not relied on by DBRS. Please see "Is 102% Enough to Cover Interest?" on page 17 for more details.



- **Partial/Alternative Liquidity:** Partial-liquidity programs have less than 100% liquidity support. These programs leverage the inherent liquidity from the underlying assets to pay the CP. Therefore, the liquidity facilities may not be necessary or the size may be decreased relative to traditional facilities depending on the extent of the inherent liquidity available. For example, extendible CP programs may have partial or no liquidity support.

The ABCP market is developing alternatives to traditional full-liquidity programs. As a testament to this, there is a notable trend toward establishing SIV and extendible CP conduits. With changing regulatory rules and Basel II pending, much of the market is searching for alternatives to traditional liquidity facilities. DBRS believes this trend toward partial- or alternative-liquidity structures will continue and is prepared to analyze innovative alternatives.

Credit Risk

In order to protect the CP investor, conduit sponsors typically structure their vehicles to employ credit enhancement on two levels: the transaction-specific level and the program-wide level. Thus, for the CP investor to actually take a loss, the asset deterioration must be greater than the credit enhancement provided on the transaction level *and* it must deplete the entire program-wide credit enhancement that is available across all transactions.

TRANSACTION-SPECIFIC CREDIT ENHANCEMENT

Transaction-specific credit enhancement is first-loss protection used to absorb any deterioration of the collateral on specific transactions within the conduit's portfolio. Each transaction in the conduit must be structured and/or credit enhanced so that the resulting risk profile of the CP conduit is commensurate with its CP rating. Common forms of transaction-specific credit enhancement are overcollateralization, subordination, excess spread, seller recourse, cash reserves, third-party guarantees, structured liquidity and total return swaps. Transaction-level credit enhancement is specific to each transaction and cannot be applied to other conduit transactions.

Types of Analysis at the Transaction Level

In order to rate ABCP, DBRS formulates a credit opinion on each underlying transaction. At the transaction level, DBRS's analysis can take the form of an internal assessment or an explicit rating.

- **Internal Assessment:** Many transactions acquired by a conduit do not carry explicit ratings. For these transactions, DBRS performs a credit evaluation that is called an internal assessment. These assessments are used by DBRS as part of the analysis of the CP. An internal assessment is similar to the analysis of explicitly rated transactions, with some exceptions. For internally assessed transactions, DBRS relies on the conduit's administrator to perform an in-depth review of the seller's operations. Further, an internal assessment relies on many protections offered by the liquidity facility. For example, dilution and commingling risks are often covered by the liquidity facilities. DBRS, therefore, relies on the rating of the liquidity provider for many risks in internally assessed transactions. Detailed explanations of what the liquidity facility typically covers with respect to the above risks, as well as other risks, can be found in the "Other Risks" section beginning on page 17.

- **Explicit Ratings:** Explicitly rated transactions are analyzed on a "stand-alone," or "term," basis.⁸ However, the payments from the explicitly rated transaction to the conduit often do not match the payments from the conduit on the CP. Thus, there is a need for traditional liquidity support to mitigate cash flow timing mismatches, as well as any market disruption risk.

Transaction Characteristics

- **Revolving Transactions:** A revolving transaction continually finances its receivables through the conduit until the date at which it terminates. New collateral enters the transaction and pays down on an ongoing basis. Transactions of this

⁸ "Stand alone," or "term," transactions are rated such that the internal cash flows must be adequate to pay periodic interest and ultimate payment of principal at the legal final date.



nature can theoretically finance their receivables indefinitely. The assets in revolving transactions typically must conform to eligibility criteria that is reviewed by DBRS.

Generally, revolving transactions are characterized by having amortization triggers that are typically checked monthly. These triggers are generally in place to ensure that the transaction has the proper credit enhancement on an ongoing monthly (reporting period⁹) basis. If breached and left uncured, an amortization of the transaction will occur. (Please see “Revolving Transactions – Sizing Transaction-Level Credit Enhancement” below for more details on the credit aspects of revolving transactions.) Many explicitly rated transactions initially revolve and subsequently, at a predetermined date, amortize.

- **Amortizing Transactions:** An amortizing transaction is characterized by assets that typically amortize from the transaction’s inception until the assets completely wind down. Amortizing transactions often have a “static” asset pool. That is, the asset pool composition is set from inception. (Please see “Amortizing Transactions – Sizing Transaction-Level Credit Enhancement” on page 13 for more details on the credit aspects of amortizing transactions.) Some explicitly rated transactions can be classified as amortizing.

Transaction-Level Credit Enhancement

The transaction-level credit enhancement is sized according to DBRS’s rating methodology, which takes into account both (1) methodologies used to rate a term, or stand-alone, transaction as well as (2) risks covered by the liquidity facilities for that particular transaction. The major factors that are considered include, but are not limited to, the following:

- Eligibility criteria or static pool¹⁰ characteristics.
- The history of delinquencies.
- The historical payment characteristics (e.g., seasonality).

- The historical timing of losses on vintage pools.
- Customer concentrations.
- The originator’s risk profile.
- The quality of the servicer.
- Underwriting procedures and policies and recent changes therein.
- The quality of the data.
- Idiosyncratic factors specific to the particular asset type.
- Industry/asset-type comparables.

The type of analysis of underlying transactions will vary based on the asset sector (e.g., mortgages versus auto loans versus trade receivables). The type of analysis will also vary depending on whether the transaction is a revolving transaction or an amortizing transaction.

• **Revolving Transactions – Sizing Transaction-Level Credit Enhancement**

– Topping up the Reserve in Revolving

Transactions: For revolving transactions, the proper credit enhancement must be in place and fully intact at the start of each reporting period. This is often accomplished via monthly (reporting period) credit triggers tied to a CP issuance test.

Generally, the most prevalent monthly credit trigger in a revolving transaction is known as the borrowing base test. This test ensures that the assets and the required credit enhancement are fully intact on a go-forward basis. Any depletion of the required credit enhancement resulting from asset deterioration is typically cured by the seller in the form of contributing more receivables to the transaction. This ensures that after each monthly (reporting period) report, the transaction’s required credit enhancement is fully intact. This procedure of restoring the credit enhancement required each

⁹ The reporting period is usually conducted on a monthly basis but may be shorter. It represents the frequency of reports on which key asset performance tests often rely.

¹⁰ A static pool is a transaction that is characterized by having a fixed pool of specific assets that amortize from the transaction’s inception to the point at which they wind down.



month (reporting period) is called “topping up” the reserve. If the reserve is not topped up, the transaction will wind down and amortization begins.

- **Ascertaining the Exposure Horizon in Revolving Transactions:** The key to accurately sizing the transaction-level credit enhancement requirement focuses on the exposure horizon, which is the time during which the transaction’s collateral can experience losses.

For revolving transactions, as noted above, the credit enhancement is typically topped up on a monthly basis. Therefore, revolving pools in effect have a fresh start each month (reporting period) because the credit enhancement is restored to its requisite level. If the credit enhancement is not topped up, the conduit is precluded from issuing CP supported by that transaction. Therefore, the transaction cannot purchase additional assets, thus causing the transaction to amortize.

The maximum time during which the collateral can experience losses, the exposure horizon, is typically calculated by adding the time it takes for the assets to naturally amortize to the length of the reporting period.

- **Amortizing Transactions – Sizing Transaction-Level Credit Enhancement**
 - **Ascertaining the Exposure Horizon in Amortizing Transactions:** As is the case for revolving transactions, the key to accurately sizing the transaction-level credit enhancement requirement for amortizing transactions is the exposure horizon, which is the time during which the transaction’s underlying assets can experience losses. Calculating the exposure horizon for amortizing transactions is simpler than for revolving transactions. Generally, the exposure horizon is the time it takes for the assets to amortize. Hence, the sizing of credit enhancement is based on the amortization period.

- **Revolving and Amortizing Transactions – Shortening the Exposure Horizon Via Structural Features:** Most revolving or amortizing, non-explicitly rated transactions that are in a conduit’s portfolio are sized as per their exposure horizon. However, there are structural features that may shorten the exposure horizon. For example, an appropriately rated takeout provider may promise to purchase a transaction at a particular time or a transaction may be short-tailed as detailed in the “Short-Tail Exposure” summary on page 22. The sale shortens the exposure horizon for that transaction.

- **Explicitly Rated Transactions:** Explicitly rated transactions can be characterized as either revolving or amortizing.

Explicitly rated revolving transactions typically have a set revolving period followed by an amortization period, the end of which is the legal final date. During the revolving stage, these transactions typically have amortization triggers that ensure that the transaction has the proper credit enhancement on a go-forward basis. These various triggers can be checked daily, weekly or monthly, depending on the type of trigger. If breached and left uncured, an early amortization of the transaction will occur. This occurrence, along with greater-than-anticipated asset deterioration, could lead to the downgrade of the explicitly rated transaction.

Similarly, for explicitly rated amortizing transactions, among other factors, poor asset performance beyond the expected defaults could lead to a downgrade of the explicitly rated transaction. In both cases, the focus for ABCP is the downgrade itself.

If the explicitly rated transaction deteriorates more than anticipated and a ratings downgrade occurs, a conduit’s program and/or transaction documents will set forth a course of action. Areas addressed by the documents may include, but are not limited to, the following:



- The action that the rating downgrade will compel the conduit’s administrator to perform (e.g., sell the asset, fund the asset with liquidity).
- The timing by which the liquidity facility must fund upon certain events (e.g., a downgrade to a particular level).
- Any events that can enable the liquidity facility not to fund the liquidity funding formula (i.e., if the rating falls below investment grade).
- The additional credit enhancement that may be provided upon a downgrade.

In any event, DBRS must be confident that the documents detail the conduit’s course of action and that action sufficiently mitigates the risk to the CP investor upon downgrade of the transaction’s rating to a rating level commensurate with the rating of the CP issued by the conduit.

Transaction-Level Triggers

DBRS typically relies on structural triggers for many transactions. These triggers often necessitate remedies that ensure that the transaction has the proper credit enhancement on a go-forward basis or, if not, cause an amortization of that transaction. However, while certain triggers are integral to many transactions, such as the borrowing base test for revolving transactions, they are not necessarily required. For example, the sponsor bank may elect to 100% credit enhance or “wrap” a particular transaction with a liquidity facility (liquidity will fund for the principal and interest on the CP). In this case, DBRS will rely on the liquidity bank’s rating. The “Liquidity Covering Credit Risks” section on page 21 addresses the possible varying magnitudes of credit coverage by liquidity facilities.

Because some triggers are more vital than others, the remedies for the breach of structural triggers vary according to their importance. Some triggers may not result in a particular transaction winding down but rather may invoke another action. For example, a credit deterioration trigger may invoke the trapping of excess spread from the assets to bolster the transaction’s credit enhancement. Some common triggers are explained below.

- **Borrowing Base Test:** The borrowing base test (see “Revolving Transactions – Sizing Transaction-Level Credit Enhancement” on page 12 for details) ensures that the transaction has the requisite credit enhancement each time the test is calculated. The frequency of its calculation can be monthly, twice a month, weekly or daily.
- **Performance Triggers:** Additionally, many transactions contain performance triggers that address underperforming collateral. Varying asset types command different quantitative triggers. Common performance tests include excess spread, delinquency and dilution triggers.
- **Seller Triggers:** Qualitative seller triggers on the transaction level include, but are not limited to, the following:
 - A seller/servicer insolvency.
 - A seller/servicer downgrade.
 - A material decline in the servicer’s ability to perform its duties.
 - A breach of material representations and warranties.
 - The cross-default of the seller with respect to other debt obligations.
- **Conditions Precedent to Issuing CP:** The conditions by which CP can be issued are an important part of revolving transactions. The breach of these conditions will preclude the conduit from issuing CP until cured. Thus, they ensure that some key elements on which the transaction’s rating was based are fully intact each time the conduit issues CP. For example, the borrowing base test is a key condition precedent to issuing CP as it ensures that upon each CP issuance, the proper credit reserves are in place.
- **Transaction Wind-Down:** Uncured breaches of transaction-specific triggers may invoke certain remedies, including a cease issuance of CP and/or no new purchases of assets. If such a breach is left uncured, remedies such as this will effectively amortize the transaction.



PROGRAM-WIDE CREDIT ENHANCEMENT

Program-wide credit enhancement (PWCE) is a fungible layer of protection generally available to all transactions within a conduit's portfolio. PWCE is typically drawn after a transaction's liquidity facilities have funded for the good assets (non-defaulted). If, after the liquidity facility funds, a particular transaction's credit enhancement is insufficient to cover the deterioration of such a transaction, PWCE then absorbs the excess loss. Thus, the transaction-specific credit enhancement acts as a first-loss enhancement and the PWCE is typically regarded as second-loss enhancement.

DBRS views PWCE as an additional layer of protection much like a subordinated tranche of a CDO. The size of the PWCE relative to the risks inherent within the conduit's portfolio of transactions is vitally important to the overall risk profile of the conduit.

PWCE can take many forms but is typically an LOC, a surety bond, a third-party guarantee, a credit asset purchase agreement or an irrevocable loan facility. The entities providing the PWCE instrument are required to provide an irrevocable commitment, have an appropriate rating and possess the capability of providing same-day funding. If same-day funding presents a problem, a facility with an appropriate short-term rating must contractually agree to front the necessary funds for the program enhancer.

PWCE Rationale

PWCE is primarily required for the following reasons:

- First, for transactions that are internally assessed, DBRS relies on the sponsor's review of each seller and the related assets. This includes the sponsor bank's ongoing reviews of such seller. PWCE provides protection for the variation, if any, between the bank's evaluation of a seller and what DBRS's opinion is or may have been had it reviewed the seller.

- The second reason, substantially more complex, addresses how the growth of a CP conduit affects its risk profile. As the number of transactions increases within the conduit and the conduit grows in size, there are factors that counterbalance one another (see "Risk Factors," "Risk-Mitigating Factors" and "Net Effects" below) and thus affect the risk profile of the conduit.

Risk Factors

As the number of transactions within a conduit increases, the probability that any one or more of those transactions will default also increases. Further, there is a correlation between the transactions within a conduit's portfolio, increasing the likelihood that if one transaction defaults, so will another. DBRS considers the effect of these risk factors when analyzing the risk profile of a CP conduit.

Risk-Mitigating Factors

In contrast, increasing the number of transactions will likely increase the size of the PWCE. Increasing the size of the PWCE has positive effects on a conduit's risk profile. These positive effects counter the aforementioned corrosive factors. First, as the size of the PWCE increases, the smaller each transaction becomes relative to the PWCE available to it. Therefore, the probability of any one transaction having a negative impact on a CP investor is decreased. Thus, as the PWCE grows with the CP conduit, more transactions will have to default simultaneously to reach the threshold that would affect the CP investor negatively. Also, to the extent that the number of transactions increases the diversity across asset and industry lines, default correlation among such transactions decreases the risk to the CP investor.

Net Effects

The overall net effect of the counterbalancing factors on the conduit's risk profile will vary depending on the composition of the portfolio and the relative size of the PWCE. Nevertheless, PWCE is in place to absorb the potential net negative effects, if any, of increasing the number of transactions within a conduit's portfolio.



Sizing PWCE

As described on the previous page, PWCE is the fungible layer typically available to all transactions within the conduit's portfolio when first-loss protection has been exhausted. DBRS determines the minimum amount of PWCE considering the projected composition of transactions within a conduit's portfolio such that the total risk profile of the conduit is commensurate with the rating on the CP.

Excess PWCE

DBRS believes that the size of the PWCE relative to the composition of the portfolio of transactions within a CP conduit is a vital factor in assessing the overall risk profile to the CP investor. For example, the difference between a CP program that has 5% PWCE and 10% PWCE is material and should be reflected in the rating of the CP, all else being equal. For example, if a conduit's portfolio comprised "A," AA and AAA transactions and had 5% PWCE, that conduit may command a rating of R-1 (low). However, if that conduit had the same portfolio with 10% PWCE, an R-1 (middle) or R-1 (high) may be more accurate (depending on the rating level of the liquidity support). DBRS believes ratings that more accurately reflect the overall risk profile of a CP program will provide CP investors with more information and more transparency.

PROGRAM-LEVEL STRUCTURAL FEATURES

Key CP Cease Issuance/Asset Purchase Tests

Key tests at the program level include, but are not limited to, the following:

- **Program Asset Test:** The principal of the non-defaulted assets of all the transactions within the conduit's portfolio should be greater than or equal to the principal of all of the conduit's liabilities at any time.
- **Program Liquidity Test:** The total available liquidity commitments must exceed the principal and interest of all outstanding CP at any time.

- **Remedies for Breach of Key Program Tests:** Any failure to satisfy these tests typically prohibits the conduit from issuing CP and purchasing additional asset interests, until cured. If left uncured for a specified period of time (usually a very short time frame), the cease issuance may become permanent or a Program Termination Event will be officially invoked. Either way, the program will wind down if breach is left uncured.

Minimum PWCE Test

Required PWCE may be reduced if the program size decreases. Nonetheless, erosion of the PWCE below a particular level as a result of defaulted assets may invoke a CP cease-issuance trigger or, if severe enough, may cause the program to wind down. If a program wind-down occurs, PWCE typically is subject to a fixed floor amount to mitigate the potential for losses resulting from adverse selection¹¹ from within the conduit's portfolio of transactions.

Other General Program-Level Structural Features

The key material triggers that will wind down a conduit if left uncured for a short period of time include, but are not limited to, the following:

- The program documents cease to be in full force and effect.
- A breach of any material representation or warranty by the conduit as per the program documents.
- A breach of the minimum net worth covenant within the program documents.

¹¹ Adverse selection may occur when the conduit's portfolio is negatively affected because as shorter-term transactions pay off, the conduit may be left with a longer-dated, less-diversified portfolio of transactions. Generally, the longer a portfolio of transactions is exposed to losses, the lower the credit quality of such a portfolio, all else being equal.



Other Risks

The following are various other conduit risks and their respective mitigants. They are present at both the transaction and program level. Liquidity facilities play a large role in covering many of these risks.

INTEREST RATE RISK

Interest rate risk arises when the interest collected from the conduit's underlying assets may be insufficient to pay the conduit's cost of funds timely. The transactions in the conduit's portfolio are made up of fixed, floating and non-interest-bearing assets. CP interest rates, although typically fixed for the term of the CP, fluctuate as new CP is issued. Therefore, the potential for variability in the conduit's transactions as well as in CP rates over time represents interest rate risk.

Interest Rate Mitigant – Transaction-Level

- **Liquidity Facility:** Generally, DBRS relies on the transaction liquidity banks to fund the interest accrued at the time of funding and the interest that will accrue to the maturity of the CP. Thus, the risk to the CP investor reflects the rating on the transaction liquidity provider. Typically, the sponsor bank provides the liquidity facility for each transaction.

Additional Interest Rate Mitigant – Transaction-Level

- **Reserve Account:** DBRS typically relies on the liquidity provider to cover interest rate risk. However, conduits have incentive to properly address interest rate risk because in cases where

the sponsor bank is also the liquidity provider, the bank does not want to take a loss if liquidity funds and the reserve is sized improperly. If liquidity is drawn, cash will be available from the interest rate reserve to reimburse the liquidity provider. If liquidity does not fund, which is unlikely, cash is available from the reserve fund to pay CP.

- **Additional Safeguards:** Other safeguards to the CP investors include the following:
 - Typically, the conduit assets are structured to pay, at a minimum, the conduit's cost of funds.
 - The conduit's floating-rate assets are generally hedged. That is, the conduit will typically swap out the asset's yield and receive the conduit's cost of funds.

Rather than rely on the above safeguards, DBRS typically relies on the liquidity support to cover interest rate risk on the transaction level.

Interest Rate Mitigants – Program-Level

- **PWCE:** Any losses on the transaction level (namely, a liquidity bank not funding) will be covered to the extent there is available program-wide credit enhancement.
- **Program Liquidity Tests:** DBRS relies on program-level tests that are designed so that the liquidity will always be sufficient to pay the principal and interest on the outstanding

Is 102% Enough to Cover Interest?

Typically, liquidity facilities are sized at 102% of the transaction limit. The extra 2% is designed to cover the interest component of ABCP. Is this enough? In a high-interest economic cycle and/or CP issued with longer maturities, interest due on the CP may be more than 2%. Therefore, DBRS does not rely on the actual size of the liquidity facility, but rather on the program-level liquidity test. This test prohibits the conduit from issuing any ABCP if, after such issuance, the available liquidity amount cannot cover the principal and interest on all of the outstanding CP. Therefore, DBRS relies on the program liquidity test and thus the liquidity facilities to cover interest rate risk. For those few programs that issue floating-rate CP, a transaction-by-transaction analysis is required to assess interest rate risk.



CP in full. As described under “Key CP Cease Issuance/Asset Purchase Tests” on page 16, there is a liquidity program test that will prohibit any CP from being issued if, after considering such issuance, the available liquidity is less than the principal and interest on the then outstanding CP. Please see “Is 102% Enough to Cover Interest?” on page 17.

FOREIGN EXCHANGE RISK

Foreign exchange risk arises when a conduit has assets that pay in a currency other than the currency in which the CP is issued. If the asset’s currency were to weaken relative to the CP currency, the cash flow from those assets would lose value and could be insufficient to pay the CP.

Foreign Exchange Mitigants – Transaction-Level

Foreign exchange risk is typically addressed at the transaction level, although the program documents will set forth the general approach that will be taken. There are three primary ways to mitigate this risk on the transaction level: hedging, liquidity support and reserve account. For the first two, the goal of the administrator is to transfer the foreign exchange risk to an appropriately rated entity. The third mitigant is a reserve, based on an evaluation of the foreign exchange risk. The following are summaries of these common mitigants.

- **Hedging:** A conduit’s administrator may hedge foreign currency exchange (FX) risk by entering into a FX rate swap with an acceptably rated counterparty. The risk reflects the rating of the hedge counterparty for payment.

A conduit’s administrator may hedge FX risk by matching spot and forward contracts. Matching the spot and forward contracts will shore up full payment when the CP matures.

- **Liquidity Support:** Sometimes liquidity will fund in the currency of the CP and thus liquidity will take the foreign exchange risk. The risk reflects the rating of the liquidity bank for payment. Behind the scenes, and irrelevant to the CP investor, the liquidity bank will most likely hedge the risk for its own internal risk management.

- **Reserve Account:** The third mitigant is a reserve account based on the evaluation of the possible foreign exchange movement between the currencies, the exposure period to such movement and the environment of the applicable currency’s sovereign location.

Foreign Exchange Mitigant – Program-Level

Any losses on the transaction level in excess of the transaction-specific enhancement will be covered to the extent there is available program-wide credit enhancement.

COMMINGLING RISK

Commingling risk arises in the event that the seller, acting as the servicer on a transaction, becomes bankrupt and the collections due to the conduit are commingled with its general funds. In this situation, the amounts due to the conduit are at risk.

Commingling Mitigant – Transaction-Level

- **Liquidity Facility:** Commingling risk is typically covered by the transaction’s liquidity facility. The liquidity funding formula, via document language, will include funds due from the seller that have not been received. Typically, liquidity funding formulas only reduce for defaults. The definition of “defaults” generally does not include these funds due from the seller. Therefore, liquidity banks typically take commingling risk. Thus, the risk to the CP investor reflects the rating of the liquidity bank.

Additional Commingling Mitigant – Transaction-Level

- **Lockboxes:** Lockboxes are segregated accounts specifically set up to separate the seller’s funds from those due to the conduit. Setting up accounts in the name of the conduit is a typical safeguard used to mitigate commingling risk.

Conduits have incentive to properly address commingling risk because in cases where the sponsor bank is also the liquidity provider, the bank does not want to take a loss if liquidity funds and commingling risk is not properly addressed. Although DBRS relies on the liquid-



ity facility, the use of lockboxes is an additional safeguard to the CP investor.

Commingling Mitigant – Program-Level

Any losses on the transaction level (namely, a liquidity bank not funding) will be covered to the extent there is available program-wide credit enhancement.

DILUTION RISK

Primarily relevant in trade receivable and credit-card transactions, dilutions are non-cash adjustments to the receivables. These include, but are not limited to, discount incentives for early payment to customers, errors in invoice amounts and returned goods. Dilutions are a normal recourse item back to the seller. If the seller becomes bankrupt, these amounts owed to the conduit by the seller are in jeopardy. When dilutions occur, they reduce the amount of receivables and thus can leave the conduit short of funds.

Dilution Mitigant – Transaction-Level

- **Liquidity Facility:** Similar to commingling risk, dilution risk is also typically covered by the conduit's liquidity facility. The liquidity funding formula, via document language, will include funds due from the seller that have not been received. Liquidity funding formulas typically only reduce for defaults. The definition of "defaults" typically excludes any diluted items.

Therefore, liquidity will take dilution risk. Thus, the risk to the CP investor reflects the rating of the liquidity bank.

Additional Dilution Mitigant – Transaction-Level

- **Reserve Account:** DBRS typically relies on the liquidity provider to cover dilution risk. However, a conduit has an incentive to properly address dilution risk because in cases where the bank sponsor is also the liquidity provider, it does not want to take a loss if liquidity funds and the reserve is sized improperly. If liquidity is drawn, cash will be available from the dilution reserve to reimburse the liquidity provider. If liquidity does not fund, which is unlikely, cash is available from the reserve fund to pay the CP investors. In rare cases, some transactions may not cover this risk via liquidity. In these cases, DBRS would size the reserve at a standard commensurate with the internal assessment of the transaction.

Dilution Risk Mitigant – Program-Level

Any losses on the transaction level (namely, a liquidity bank not funding) will be covered to the extent there is available program-wide credit enhancement.

Liquidity Risk

GENERAL

Liquidity support is vital to an ABCP conduit. Most CP conduits do not match the maturity of their assets to the maturity of their liabilities. Therefore, there may be mismatches between the cash flow from the assets and the requirements to pay CP in whole and on time. This is the main reason for liquidity support in U.S. ABCP programs. In addition, although a market disruption is very unlikely, liquidity is available to pay CP during such an event.

Liquidity agreements are typically an integral part of each transaction. They generally fund for the good assets (non-defaulted) before PWCE is drawn. PWCE is designed to cover the defaults in excess of the transaction's first-loss credit enhancement.

Liquidity support is typically a facility provided by liquidity banks, predominantly sponsor banks, that support transactions within the ABCP program. They are typically sized up to 102% of the transaction. Liquidity risk is one of the primary areas of focus when analyzing ABCP transactions.

FORMS OF LIQUIDITY AGREEMENTS

Liquidity support can take many forms and is typically provided on the transaction level for ABCP programs. The following are common forms:

- **Liquidity Asset Purchase Agreement:** The most prevalent form of liquidity facility is the Liquidity Asset Purchase Agreement (LAPA). LAPA banks purchase the entire asset interest and thus take the transaction out of the conduit and onto its own balance sheet. The LAPA bank will fund for the funding formula, which is reviewed by DBRS for inclusion of the transaction into the conduit. Assuming the credit is sized properly, the funding formula will be adequate to retire CP in whole and on time. This is because the liquidity funding formulas typically cover everything but defaults. If credit enhancement is adequate to cover defaults, then the amount the LAPA bank funds should be ample.
- **Liquidity Loan Agreement:** A Liquidity Loan Agreement (LLA) differs from a LAPA in that the provider agrees to lend to the conduit in the amount of the funding formula. The conduit must pay the liquidity bank back for this loan. Any outstanding liquidity loans should be properly counted as a liability of the conduit for both the program asset test and the program liquidity test.
- **Other Liquidity Facilities:** Total return swaps and repurchase agreements are examples of other forms of liquidity facilities that can support transactions within a CP conduit. The counterparties providing these facilities must be appropriately rated or internally assessed to a standard commensurate with the risk profile of the CP conduit.

SAME-DAY FUNDING

Liquidity facilities are required to fund on a same-day basis and thus must have an adequate short-term rating. (See the "Rating Requirements for Liquidity Support" section on page 21.) Same-day funding mitigates any timing mismatches and market disruption risk.

LIQUIDITY FUNDING FORMULA

The liquidity funding formula describes the amount that a liquidity provider will fund when asked to do so. Typically, liquidity funding formulas exclude defaulted assets. This formula is analyzed by DBRS to understand how the funding formula works in concert with the required credit enhancement for that particular transaction.

There are three prevalent types of funding formulas: asset-based, capital-based and liquidity-event. The first two are commonly used in internally assessed transactions; the last is often used in explicitly rated transactions.

- **Asset-Based Liquidity Funding Formula:** Asset-based formulas typically provide for the funding of the good (non-defaulted) asset balance. Defaults are usually accumulated from the last



good borrowing base test. The initial balance as of each good borrowing base test report includes the requisite reserves appropriate to the rating level commensurate with the CP issued.

- **Capital-Based Liquidity Funding Formula:** Capital-based formulas typically provide for the funding of the capital that is equivalent to the principal and the interest on the CP minus the defaults that are in excess of the credit enhancement required for that specific transaction.
- **Liquidity-Event Liquidity Funding Formula:** Liquidity-event formulas are commonly used with explicitly rated transactions. Such formulas typically provide for the funding of the principal and interest on the CP. However, they are sometimes appropriately referred to as liquidity cliff formulas because, if an explicitly rated security or related third-party enhancer's rating migrates downward to a particular level, the liquidity facility may no longer be obligated to fund. Thus, the likelihood of such migration occurring within a specific time period is the key risk. Please refer to "Explicitly Rated Transactions" on page 13, which explains some of the more common considerations from DBRS's perspective.

RATING REQUIREMENTS FOR LIQUIDITY SUPPORT

- **Liquidity Rating Requirements for R-1 (low) CP Programs:** DBRS requires that for R-1 (low) ABCP programs, liquidity support is R-1 (low) or higher.
- **Liquidity Rating Requirements for R-1 (middle) CP Programs:** DBRS requires that for R-1 (middle) ABCP programs, liquidity support is R-1 (middle) or higher. On an exception basis, R-1 (low)/A (middle) banks may support R-1 (middle) programs under certain conditions. DBRS will require special structural features that will limit the risk of downward migration of the rating of the bank. Such features may include downgrade triggers resulting in a replacement of the bank or a draw on liquidity within a specified time period acceptable to DBRS.
- **Liquidity Rating Requirements for R-1 (high) CP Programs:** DBRS generally requires that for R-1

(high) ABCP programs, liquidity support is R-1 (middle) or higher. A downward rating migration of an R-1 (middle) liquidity provider will necessitate further assessment and an action from the administrator and/or the affected liquidity bank acceptable to DBRS.

LIQUIDITY COVERING OTHER RISKS

In many transactions, particularly non-explicitly rated transactions, external-liquidity support covers more than market disruption risk and timing mismatches. These risks are detailed in the "Other Risks" section beginning on page 21.

LIQUIDITY COVERING CREDIT RISKS

In addition to covering market disruptions, timing mismatches and other risks, liquidity is sometimes used to cover credit risks. The degrees to which liquidity will cover credit risk can vary. In some instances, the liquidity facility may elect to cover some of the credit risk, as detailed in "Short-Tail Exposure" highlight on the following page. In other instances, liquidity will cover the entire credit risk by wrapping the transaction. In this case, liquidity will fund for the principal and interest on the outstanding CP under all circumstances except for the acceptable "Exceptions to Liquidity Funding" listed below.

EXCEPTIONS TO LIQUIDITY FUNDING

Liquidity facilities are committed and obligated to fund upon request except under remote circumstances. Generally, the acceptable exceptions to liquidity funding are as follows:

- The bankruptcy of the conduit.
- A highly rated third party's insolvency. Typically, the AAA monoline insurer that is a party to the transaction.
- A rapid downward migration of a security to non-investment-grade status. Given the changing regulatory environment for an increasing number of conduits, liquidity may only support investment-grade assets. There are varying ways via credit enhancement and/or structural features to cover the risk of liquidity not funding the



transactions that are less than investment grade. DBRS requires that such a transaction be credit enhanced or structured to an acceptable standard such that the risk profile of the conduit is commensurate with its CP rating.

- Other exceptional circumstances acceptable to DBRS that will not negatively affect the rating of the CP issued from the conduit.

Short-Tail Exposure

Whether transactions are revolving or amortizing, the exposure horizon is the maximum time the collateral pool can be subject to losses. However, the exposure horizon can be shortened by the use of liquidity facilities. This is explained and illustrated below.

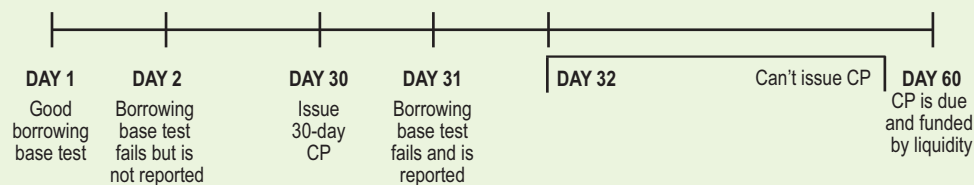
A transaction's structural features may shorten the time period during which the underlying assets are subject to losses. This is referred to as short-tailing the exposure horizon. A common way to short-tail the exposure horizon is via a funding mechanism within the Liquidity Asset Purchase Agreement (LAPA). For example, if a revolving transaction* were to amortize in five months and had a monthly reporting period (borrowing base test) then the exposure horizon would be 180 days (equal to the underlying assets' amortization plus the reporting period). If, however, the CP tenor were limited to 30 days and had a liquidity funding mechanism tied to a monthly borrowing base test, then the exposure would be shortened to approximately two months. This is so because upon a borrowing base breach, CP could no longer be issued and liquidity would be invoked. The example below illustrates this concept.

Structural Features of Short-Tail Example

Without the following structural features, the exposure to losses on this collateral pool would have been 180 days.

- CP tenor will be limited to 30 days.
- A borrowing base breach will invoke a cease-issuance trigger on the CP.
- Liquidity will fund the CP (excluding defaults) upon maturity.

Worst Case Scenario Timeline



Exposure to losses is from day 2 to day 60.

The exposure to losses on the transaction in this example has been reduced from 180 days to approximately 60 days because of the short-tail feature. It is important to note that there are various ways to short-tail exposure. The above example is among the more common ways used.

* Assuming that the tenor of the CP can be up to 150 days or more.



Rating Process and Documentation Review

RATING PROCESS INITIATION

The initial review of a new conduit usually begins with a proposal phase. The proposal phase is useful in order to uncover any unusual or complex issues with respect to any credit, liquidity, legal or operational risks. Thereafter, documentation is prepared and DBRS conducts its initial operational review of the prospective sponsor bank.

CONDUIT RATING – PROGRAM ANALYSIS

After the proposal phase, the administrator, typically the sponsor bank, delivers the program documents. These are the documents to which the administrator of a conduit must adhere. DBRS analyzes these documents in order to issue a rating on the CP program. Typical program documents include, but are not limited to, the following:

- Administration Agreement.
- The conduit's corporate documents.
- Management Agreement.
- Depositary or Issuing and Paying Agency Agreement.
- Placement Agency Agreement.
- Any insurance or LOC agreement.
- Security Agreement.
- Definitions (summary of terms).
- Investment Policy.

CONDUIT CONFIRMATIONS – TRANSACTION ANALYSIS

After reviewing the conduit program documents, DBRS will review the operative documents for each transaction that the conduit acquires. Specifically, DBRS will analyze the documents that govern each level of asset transfer as well as the liquidity agreement and any other documents that are salient to the transaction rating. Upon the satisfactory completion of the document review together with the credit analysis of the transaction, a formal credit committee is conducted. If the credit committee votes to agree with the proposed rating, a rating letter will be issued. The rating letter will confirm that the addition of the transaction to the conduit's portfolio will not change the current rating of the CP issued by the conduit.

Asset Transfer Agreement/Receivable Purchase Agreement

The document that governs the transfer of asset interests from the seller (or special-purpose vehicle (SPV)) to the conduit will be reviewed. Key factors analyzed include, but are not limited to, the following:

- Transaction-level conditions precedent to issuing CP (e.g., borrowing base test).
- Eligible receivables.
- Credit enhancement.
- Key definitions.
- Legal aspects of the transaction.



Liquidity Agreement

The other essential document on the transaction level is the liquidity agreement, which can take many forms. Total return swaps and repurchase agreements provided by appropriately rated counterparties are examples of acceptable liquidity facilities. However, the most prevalent forms of liquidity agreements are the Liquidity Loan Agreement (LLA) and the Liquidity Asset Purchase Agreement (LAPA). Key factors analyzed include, but are not limited to, the following:

- Circumstances by which the liquidity bank will fund.
- The liquidity funding formula.
- Circumstances by which liquidity is not obligated to fund.
- Timing of payment in order to retire the CP timely.
- The other risks covered by the liquidity provider (see the “Other Risks” section on page 17).
- Legal aspects of the document.

Surveillance

MONTHLY REVIEW

DBRS monitors each conduit on a monthly basis, based on reports submitted by the respective conduit administrators. The key elements of the monthly report are designed to identify any weaknesses within a conduit’s portfolio in order to ascertain whether any rating action is required. These elements include, but are not limited to, the following:

- Each transaction’s name and rating.
- Conduit liabilities outstanding.
- Seller concentrations.
- Portfolio mix, including concentrations.
- Required and actual transaction-specific credit enhancement.
- Required and actual program-wide credit enhancement.
- Liquidity bank commitments and ratings.
- Any changes to support facilities.
- The ratings on support counterparties, if applicable.
- Portfolio performance as related to deal-specific amortization triggers.
- Conduit performance as related to program amortization triggers.

ANNUAL REVIEW

Annual operational reviews, along with monthly surveillance, are essential to support the ongoing rating of the ABCP conduit.

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www.dbrs.com

Toronto

DBRS Tower
181 University Avenue
Suite 700
Toronto, ON M5H 3M7
TEL +1 416 593 5577

London

1st Floor
25 Copthall Avenue
London EC2R 7BP
TEL +44 (0)20 7562 5600

New York

140 Broadway
35th Floor
New York, NY 10005
TEL +1 212 806 3277

Paris

27, avenue de l'Opéra
75001 Paris
TEL +33 (0)1 7038 5214

Chicago

101 North Wacker Drive
Suite 100
Chicago, IL 60606
TEL +1 312 332 3429

Frankfurt

Trianon Tower
Mainzer Landstrasse 16
60325 Frankfurt
TEL +49 (0)69 9716 8144