



Methodology
Rating U.S. ABS CDO Restructurings

MAY 2009



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Introduction

U.S. ABS CDOs

Collateralized debt obligations (CDOs) backed by asset-backed securities (ABS) have been in existence since the mid-1990s. This broad category of CDOs encompasses CDOs backed by consumer ABS, commercial ABS, real estate investment trusts (REITs), commercial mortgage-backed securities (CMBS) as well as other CDOs. As the credit dynamics of ABS changed during the 2000 to 2002 credit cycle, the composition of ABS within CDOs shifted in kind. In addition, the significant demand for ABS, driven by ABS CDO issuance, had a substantial impact on the composition of individual transactions and associated credit performance in the sector. Historically, the first ABS CDO portfolios were multi-sector in nature; these included both consumer and commercial ABS. However, by early 2002, ABS CDO portfolios became increasingly concentrated in subprime and Alt-A residential mortgage-backed securities (RMBS), reflecting the surge in mortgage origination and the higher yields available on RMBS. As the mortgage market significantly expanded, so did the CDO market. Overall CDO issuance grew from \$60 billion in 2002 to \$157 billion in 2004 and \$557 billion in 2006. ABS CDOs also significantly increased as a percentage of the entire structured credit market over this same period, growing from 8% of CDO issuance in 2000 to 45% in 2004 and to more than 65% in 2006.

The significant deterioration in the ABS market has driven a fundamental deterioration in a significant number of ABS CDOs. As a result, holders of these securities have been exploring a variety of options and techniques that can be applied to restructure existing distressed ABS CDOs.

A restructured ABS CDO transaction typically involves the sale of one (or more) securities issued by an existing CDO (or CDOs) to a newly formed special-purpose vehicle (SPV) that then issues one or more notes. These new securities are implicitly backed by the same underlying collateral that supports the target CDO being restructured.

Deterioration in the residential mortgage markets and in turn in RMBS (particularly 2005 to 2007 vintages) has caused dramatic downgrades on ABS CDOs (in some cases, 12 to 15 rating notches) and technical events of default. More than 50% of ABS CDOs issued from 2006 to 2007 have experienced events of default, and one-third of those have resulted in portfolio liquidations. Given the size of the ABS CDO market and the implications of this significant deterioration, many market participants are now holding impaired ABS CDOs.



While mezzanine and junior securities of ABS CDOs are severely (if not completely) impaired, the senior tranches may still be performing, if only barely. Such senior tranches may still receive cash flows and may still be supported by some performing collateral. Restructuring senior securities of ABS CDOs entails reclassifying the risk of one or more severely impaired securities into new securities with multiple risk levels. Post-restructuring, the holder of the existing distressed ABS CDO tranche can potentially hold new securities that may have a higher rating.

The role of DBRS as a credit rating agency in the ABS CDO market is to provide a third-party opinion as to the likelihood of the rated debt tranches paying interest and principal in full (an equity, or first-loss, tranche is typically unrated) over the term of the transaction. The following DBRS rating criteria should not be viewed as static. DBRS reviews market developments on an ongoing basis to ensure that its policies and criteria remain relevant. On an annual basis, DBRS reviews its criteria and, in the interim, may also publish updates, which are publicly available on www.dbrs.com.

U.S. ABS CDO Categories (2002–2007)

	Collateral Composition	Collateral Rating	Typical Deal Size
CDOs of mezzanine RMBS	Primarily subprime RMBS*	A to BB	\$400 million to \$600 million
CDOs of high-grade RMBS	Primarily subprime RMBS*	AAA to A	\$1 billion to \$1.5 billion
CDOs of commercial real estate (CRE)	Primarily CRE	A to BB	\$400 million to \$500 million

* Smaller portfolio percentages are dedicated to other ABS asset types.

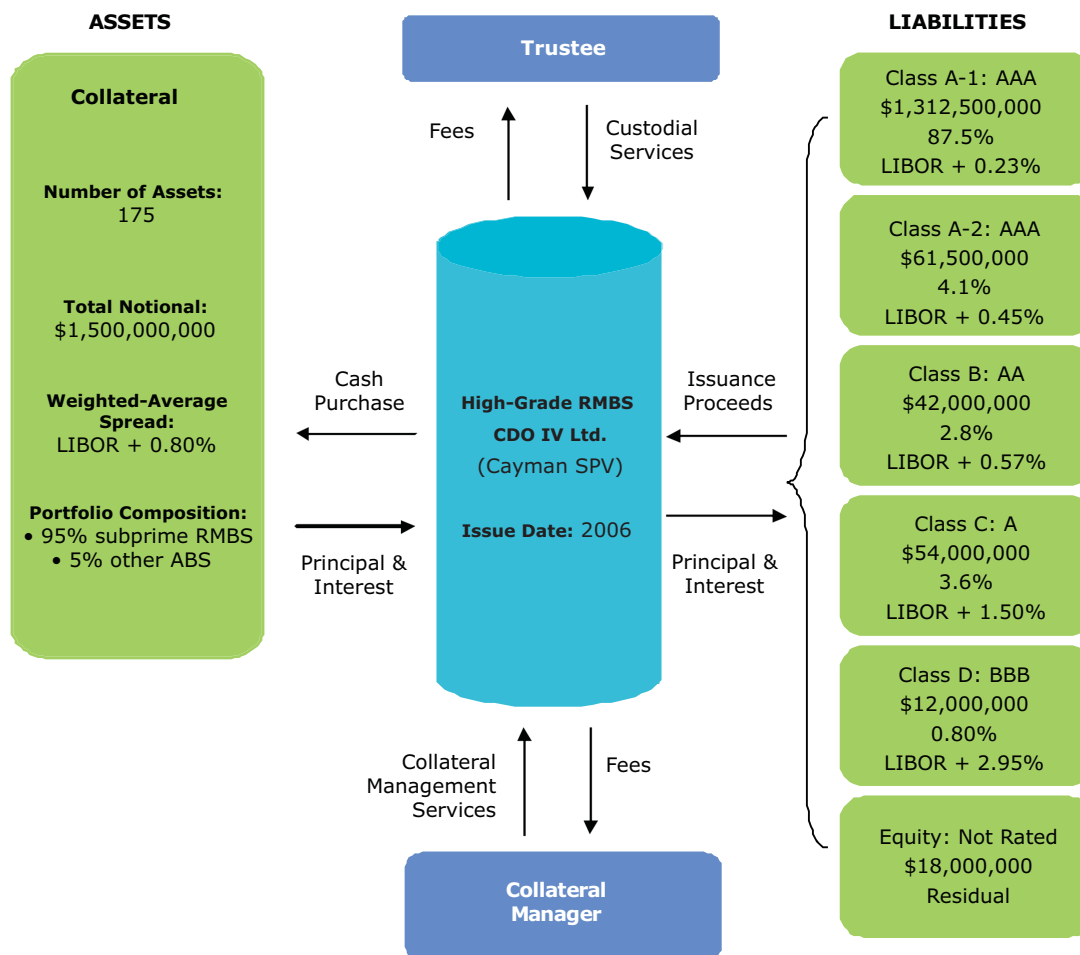


Structural Overview

U.S. ABS CDOs

U.S. ABS CDOs, like most CDOs, use securitization technology to tranche an ABS collateral pool into different securities by credit risk. The CDO, typically a tax-exempt SPV, or trust, is capitalized by an equity tranche and one or more debt tranches. The equity tranche receives all residual cash flows, while the debt structure is similar to a corporate bond (stated coupon, stated maturity, CUSIP, T+3 settlement, etc.). The CDO uses the proceeds from the equity and debt issuance to purchase a pool of U.S. ABS securities. The interest and principal proceeds generated from this ABS collateral are disbursed to each of the tranches based on a legally binding priority of payments, often referred to as the waterfall.

Typical U.S. ABS CDO*



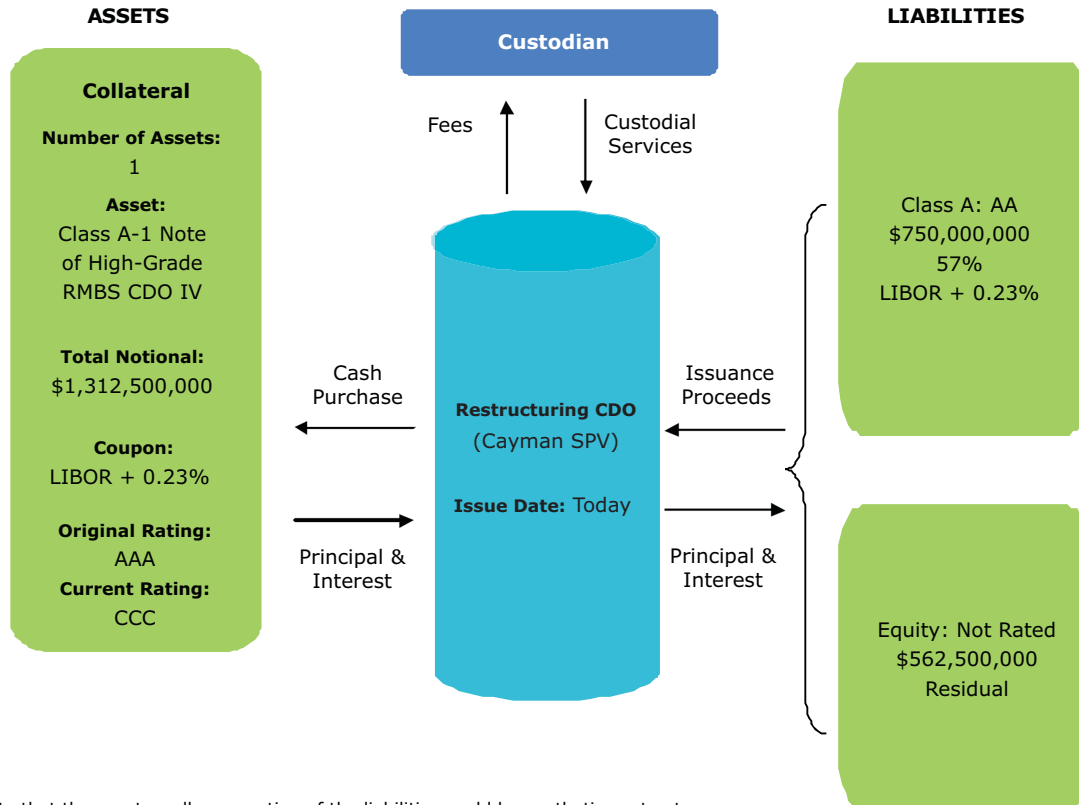
* The liability ratings are original ratings and all (or a portion) of the assets (or liabilities) could be synthetic contracts.



U.S. ABS CDO RESTRUCTURINGS

U.S. ABS CDO restructurings typically involve the sale of an existing target security (Restructured Asset) to a new bankruptcy-remote SPV (Restructuring Issuer) that will then issue one or more new notes. The sole asset of the Restructuring Issuer is, in general, the Restructured Asset and any proceeds generated therefrom. Otherwise, the Restructuring Issuer is a typical CDO, with mechanics and description very similar to the U.S. ABS CDO structure described above.

Typical U.S. ABS CDO Restructuring*



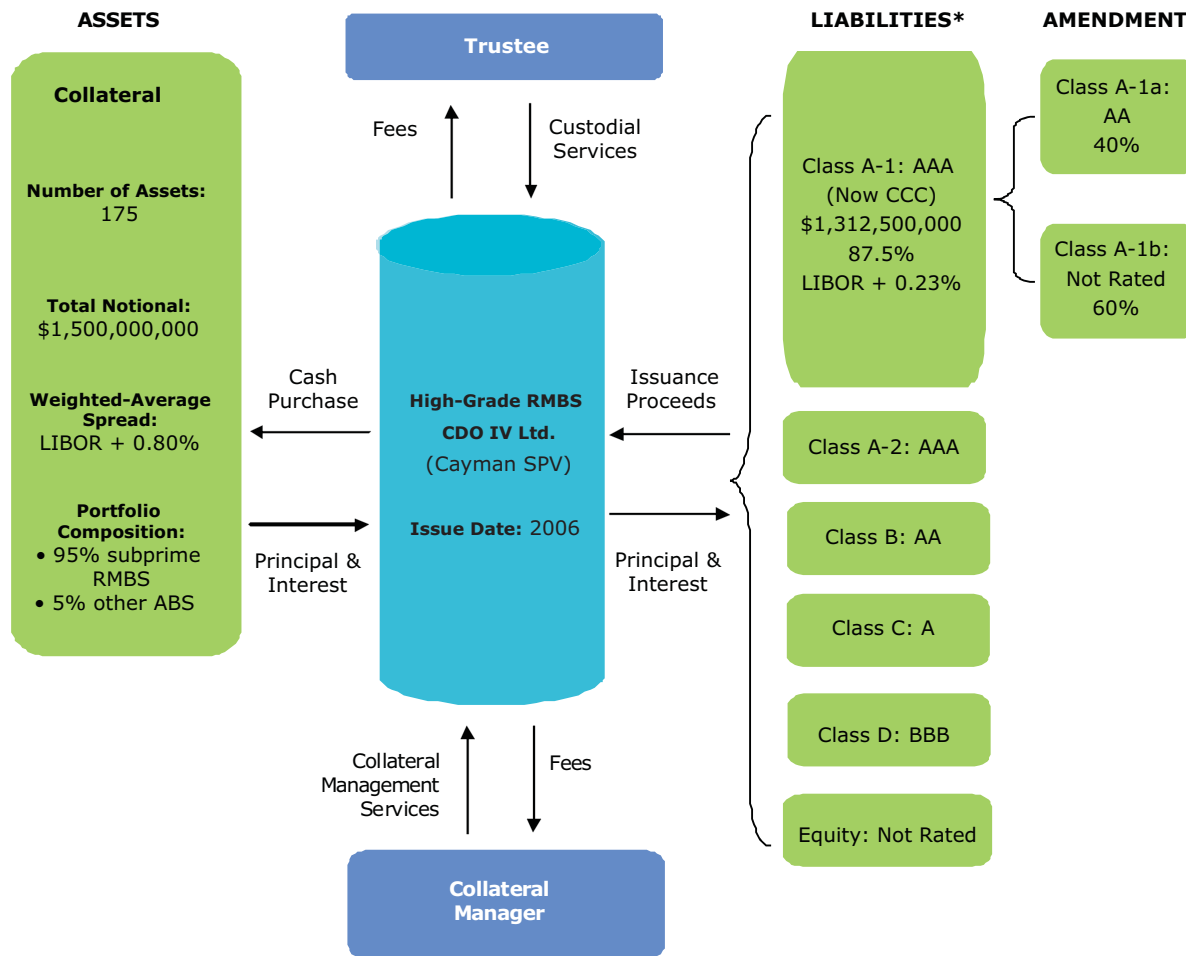
* Note that the asset or all or a portion of the liabilities could be synthetic contracts.



RESTRUCTURINGS THROUGH AMENDMENTS

Restructurings can also take place within an existing U.S. ABS CDO structure by amending the current documentation to create new senior and subordinated securities from an existing security.

Typical U.S. ABS CDO Restructured by Amendment



* Note that liability ratings are original ratings (unless otherwise noted).



Qualitative Methodology

The guidelines below are intended to provide a basic outline of the qualitative framework applied by DBRS when a structured credit transaction is evaluated. As each transaction reviewed by DBRS is unique, these guidelines are not intended to be exhaustive. DBRS does apply expert judgment (through consultation among analysts and rating committee members) and seeks outside legal counsel when necessary.

RATIONALE

DBRS endeavors to understand the motivation behind each rating it issues. Understanding the objective of each rating is key to (1) providing a framework for analysis and (2) identifying any potential issues that could affect the rating (or DBRS's ability to issue a rating). Understanding how a potential rating will be used is fundamental to analyzing a transaction and will help flag issues or discussion points as early as possible.

DOCUMENTS

DBRS structural analysis includes a careful review of all transaction documents. Internal or external counsel may be used on a case-by-case basis. Under no circumstances will a rating letter be delivered before an execution version of each document supporting a rating is received, reviewed and signed off by DBRS.

OPINIONS

DBRS must be permitted to review all legal opinions relevant to the transaction. The legal opinions delivered on the closing date should apply the law of the jurisdiction that has been chosen by the parties to the transaction as the governing law of the transaction documents. Any relevant enforceability (e.g., corporate-level) opinions should be received for major transaction counterparties. Lastly, DBRS should be listed as an addressee on all opinions.

TAX OPINIONS

If the transaction is modeled assuming the entity is not subject to entity-level tax (as is typical), DBRS will review tax opinions that express this. Typically, DBRS should expect to see an opinion from counsel to the issuer that the issuer will not be subject to tax in the SPV jurisdiction, as well as a U.S. tax opinion as to whether or not the entity will be considered to be engaged in a U.S. trade or business.

LIENS, TRUE SALE AND NON-CONSOLIDATION OPINIONS

The transaction must have a fully perfected, first-priority lien on all assets. For all transactions involving the transfer of cash assets to the issuer, DBRS requests true sale and non-consolidation opinions stating that the assets would be bankruptcy-remote to the asset seller. An exception to this would be a situation in which the asset seller is the purchaser of 100% of the notes and equity of the issuer. In that case, there is no true sale and the assets of the issuer would be consolidated. DBRS will consider rating this type of structure under the following scenarios:

- The purchase agreement states that the asset seller will be purchasing all of the notes and equity from the issuer.
- DBRS is immediately notified upon the transfer of any notes or equity away from the original purchaser (this mechanic must be in the governing documents).
- The rating letter must state that "in the event of a transfer of any notes or equity, DBRS will withdraw all ratings unless suitable true sale and non-consolidation options are provided to DBRS at the time of transfer."
- If the rating is public, DBRS would appropriately disclose that the notes are subject to rating-withdrawal risk as per the above mechanisms.



DERIVATIVE DOCUMENTATION

Credit default swap (CDS) agreements, total return swap agreements and other hedge agreements should be in International Swaps and Derivatives Association, Inc. (ISDA) format. The schedule, the confirmation and the credit support annex (CSA) will be reviewed for each transaction. In general, DBRS does not mandate any fixed-versus-floating interest rate hedges as the maximum amount of fixed-floating rate risk is captured in cash flow modeling stresses. Transactions that incorporate a material amount of basis risk must either be 100% hedged or would be stressed in the cash flow modeling on a case-by-case basis.

DBRS models and reviews interest rate hedges, currency hedges, basis swaps, CDS, total return swaps and any other hedge or derivative agreements in the Restructured Asset. DBRS does not rate restructured ABS CDOs where the underlying hedge agreements are unavailable.

EVENT OF DEFAULT

Given that Restructured Assets are typically deeply distressed, defaults and payment failures are likely scenarios. Such events of default (EODs) could be beneficial or detrimental to holders of the Restructured Asset. For example, acceleration following an indenture EOD may introduce market value risk in the analysis of a CDO restructuring. As a result, in general DBRS only reviews U.S. ABS CDO restructurings if the par amount of the Restructured Asset held by the Restructuring Issuer is sufficient to control a potential liquidation. EODs in related transaction documents are reviewed as well. For example, failure to pay under an ISDA swap agreement may introduce large hedge termination payments senior in payment priority to the Restructured Asset. DBRS assesses the impact of potential future default events from a legal as well as quantitative perspective.

COLLATERAL MANAGER

DBRS conducts on-site reviews of CDO collateral managers. If a Restructured Asset is managed by a collateral manager, but the portfolio is no longer tradable (e.g., if certain transaction covenants are significantly breached), a collateral manager review by DBRS may be waived.

COLLATERAL POOL

First and foremost, it is imperative that the documentation and the modeling be in sync. DBRS mandates that the collateral pool must match the modeled pool. For restructured ABS CDOs, DBRS will assess whether or not the collateral pool is expected to remain static for the life of the transaction. If the pool is expected to remain static, DBRS may rely on trustee and payment date reports for the restructured ABS CDO to model the collateral pool. If trading is expected to resume, DBRS will take trading parameters into consideration when assessing the collateral pool.

INTEREST AND PRINCIPAL PROCEEDS

The definition of interest and principal proceeds has an impact on modeled results in view of the fact that interest and principal are generally treated differently in the structural waterfalls. Interest proceeds and principal proceeds are a particular issue for restructured U.S. ABS CDOs, since coupons paid on the Restructured Asset may contain both interest and principal proceeds from the assets underlying the Restructured Asset.

DBRS individually models each restructured U.S. ABS CDO. If, however, the principal component of any coupon paid on the Restructured Asset is not counted as principal proceeds by the Restructuring Issuer, a given rating may require more subordination should principal be used to pay interest.



ELIGIBLE INVESTMENTS

Uninvested cash may be invested in eligible investments. Eligible investments should minimize the deal's exposure to credit, duration and counterparty risk. Eligible investments should mature before the next payment date. If eligible investments reside in accounts where payment could be demanded at any time, such eligible investments should be redeemable on demand at par. Each eligible investment *must* have an R-1 (high) short-term rating by DBRS. If the investment is not rated by DBRS, a review is conducted to confirm that each eligible investment would be rated equivalent to R-1 (high).

FEE AND EXPENSE ISSUES

No credit will be given to any cash flows distributed below uncapped expenses. All fees and expenses in the waterfall of the Restructured Asset will be modeled.

Quantitative Methodology

The credit quality of pools underlying the ABS CDO Restructured Asset is expected to be significantly distressed. As a result, the quantitative analysis is more conservative than might otherwise apply to a newly issued CDO, a collateralized loan obligation (CLO) or a structured credit vehicle backed by other types of collateral.

GENERAL – MODELING

To apply this methodology, any reference to “portfolio” should be interpreted as the portfolio underlying the Restructured Asset. The structures of both the Restructured Asset and the Restructuring Issuer are reviewed. DBRS applies its proprietary model, the CDO Toolbox, to generate rating-based loss rate percentiles (RBLRPs) using the current portfolio of the Restructured Asset. In addition to modeling the underlying assets of the Restructured Asset, pro forma cash flow modeling is performed both on the Restructured Asset and the Restructuring Issuer.

ASSET DEFAULT MODELING

Ratings

Each security in the portfolio will be assigned an internal assessment by DBRS. Internal assessments constitute the internal opinion of DBRS with respect to an individual security or issuer and is expressed through the DBRS public ratings scale. This is done to ensure consistency with respect to DBRS views on individual sectors and the application of those views to structured credit transactions.

Any security with an internal assessment of C is assumed to default immediately with no recovery. In general, no credit is given to projected cash flows on securities with an internal assessment of C. However, DBRS may assign some interest-only credit to C-rated assets in the cash flow model, depending on the liability rating to be assigned and certain characteristics of the asset.

For example, tranches of CDOs of ABS may be assigned interest-only credit depending on (1) whether the tranche is paid above the senior-most overcollateralization or interest diversion test and (2) the assumed rating the client is seeking on the liabilities of the Restructuring Issuer. Certain RMBS and CMBS may be given interest-only credit as well.

Recoveries

DBRS recovery rates are based on both public information and DBRS views on the sector and its overall performance. Recovery rates for non-RMBS that are otherwise ABS are determined on a case-by-case basis by DBRS.



DBRS Recovery Rates by Security Type

	2003–2004	2005–2007
Senior RMBS AAA at closing	78%	78%
Non-senior RMBS AAA at closing	50%	30%
RMBS AA at closing	29%	20%
RMBS A at closing	9%	9%
RMBS BBB at closing	5%	5%
RMBS BB at closing	2.5%	2.5%
RMBS B at closing	0%	0%
RMBS CCC at closing	0%	0%

Industry Codes and Default Tables

Each security is assigned an Industry Code and Cumulative Default Curve based on Table 6, Appendix 1 and Appendix 2 of the published April 2007 methodology *The CDO Toolbox*.

Structured Finance Asset Classes

Code	Name	Cumulative Default Curve*
51	MBS – Prime	Structured Finance
52	MBS – Subprime (and CDOs of subprime MBS)	Structured Finance
53	MBS – Others	Corporate Finance
54	Consumer ABS	Structured Finance
55	Commercial ABS	Corporate Finance
56	CDO/CLO	Corporate Finance
57	CMBS	Structured Finance
58	REIT	Corporate Finance

* Consistent with the April 2007 The CDO Toolbox methodology, these assignments may be adjusted on a case-by-case basis by the analyst, depending on vintage, collateral quality, etc.

Any RMBS that is not prime (Alt-A, etc.) will be modeled as 100% correlated with subprime (as part of Code 52). A CDO will be assigned the asset class consistent with its underlying portfolio. For example, a CDO of primarily subprime RMBS will be assigned Code 52. Code 56 is reserved for CDOs and CLOs backed by corporate assets.

Exposure Tenor

Each security in the portfolio will be assigned an exposure tenor by the appropriate DBRS product group. Tenors will vary based on relative differences across sectors as well as individual differences across securities in the same sector.

Correlation Assumptions

DBRS applies the following standard correlation assumptions that are based on historical experience and DBRS's expert judgment:

- Within structured finance industry classes: 60%.
- Between structured finance industry classes: 36%.



ASSET DEFAULT MODELING OUTPUTS

DBRS's CDO Toolbox returns a RBLRP for each rating (from AA (high) to B (low)). This number can be interpreted as the amount of performing collateral that will be excluded in the relevant rating stress scenario.

LIABILITY MODELING

General

In order to fully capture the unique structural implications of distressed ABS CDO tranches, DBRS performs a pro forma cash flow analysis on the notes issued by the Restructuring Issuer. The modeling is performed on the underlying pool of assets held inside the Restructured Asset, and any interest and principal cash flows paid to the Restructured Asset then disbursed to the notes issued by the Restructuring Issuer as set out in the governing documents of the restructuring. This approach appropriately captures potential principal leakage at the Restructured Asset level (e.g., principal proceeds may be used to pay interest rate swaps as well as pay the current coupon on subordinated tranches). In addition, this approach incorporates any excess spread that may be used as credit support at the Restructuring Issuer level. In most cases, DBRS performs its own internal pro forma cash flow analysis in conjunction with those run by the transaction sponsor.

Collateral Pools

DBRS segregates collateral by interest rate type (fixed or floating), with separate amortization schedules for each component. It should be noted that when applying the interest coupon paid to the Restructured Asset into the mechanics of the restructuring, care is taken to correctly model the potential interest and principal components of that interest coupon. If the structure does not account for the principal component of the interest coupon as principal, potential principal leakage can occur at the restructuring level, and the transaction will be modeled to account for that potential leakage.

Default Timing

Collateral default rates are applied based on the following timing patterns. For each of the scenarios below, defaults are assumed to occur at the beginning of each deal payment period in the year. The required default timing scenarios are as follows:

Front-Loaded

- 40% in year 1 (starting in period 2)
- 30% in year 2
- 20% in year 3
- 10% in year 4

Back-Ended

- 20% in year 1 (starting in period 2)
- 30% in year 2
- 40% in year 3
- 10% in year 4

Smooth

- 30% in year 1 (starting in period 2)
- 30% in year 2
- 30% in year 3
- 10% in year 4

For transactions with either unusually short or long maturity structures, these scenarios are adjusted. DBRS will determine appropriate default patterns on a case-by-case basis for these types of transactions.



Interest Rates

All contractual interest rate hedging agreements are explicitly modeled for the Restructured Asset. The arranger will be responsible for generating a forward LIBOR curve (typically, a linear interpolation between the different key rates that make up the U.S. dollar swap curve). DBRS runs three interest rate scenarios: the forward interest rate curve, a rising interest rate curve and a declining interest rate curve. The rising and declining interest rate curves are generated by DBRS via stochastic models that are calibrated on historical data. Please contact DBRS for the most current set of interest rate stresses.

Other Modeling Assumptions

DBRS applies the following assumptions to certain miscellaneous items commonly found in ABS CDO structures:

- Senior expenses assumed to hit the cap (e.g., if senior expenses are capped at \$100,000 per annum, \$25,000 of senior expenses are assumed to occur in each quarterly payment period).
- No intra-period reinvestment of interest and principal proceeds (e.g., no income on eligible investments is assumed).

Liability Modeling Outputs

For each tranche, nine scenarios are developed (three default patterns times three interest rates). For each scenario, DBRS determines the maximum amount of collateral that may be lost without the restructured note losing any interest or principal (the break-even loss rate (BLR)). For each tranche, a stability cushion is typically calculated, equal to the average BLR minus the RBLRP associated with the desired rating (e.g., the amount of losses the restructured note can withstand versus the amount of losses that will occur under the rating stress scenario). For tranches with BLRs that vary widely across different interest rate stresses, DBRS assumes the worst-case interest rate environment to determine the governing BLR.

Bankruptcy Cram-Downs

Bankruptcy cram-down legislation in the United States may affect the RMBS internal assessments or the CDO analysis or both, depending on what legislation is adopted and how it is practically applied.

A cram-down is the reduction of the secured mortgage debt, in which the under-collateralization of a mortgage is re-characterized as unsecured debt and included among other similar debt subject to the debtor's reorganization. Such reduction is typically treated as a credit loss in RMBS transactions.

Similar to the effect of principal-forgiveness modifications, cram-downs may reduce default frequency by giving delinquent borrowers greater incentives to stay in their homes and, as such, lead to a faster stabilization of home prices, ultimately reducing loss severities. However, it may also cause certain bonds, typically the subordinate classes, to incur losses sooner than expected.

Generally speaking, if losses are allocated on a reverse sequential basis as is true for most subprime transactions, cram-downs will likely benefit the senior bonds more than the subordinate tranches given their respective positions in the capital structure. However, in prime and certain Alt-A shifting-interest transactions, cram-down losses can be allocated differently. In such cases, if the cram-down losses exceed a stipulated carve-out limit (generally below five basis points), losses can be allocated on a pro rata basis across the capital structure, resulting in write-downs in senior bonds that wouldn't otherwise have taken any credit losses. Although such losses to the senior bonds are generally expected to be insignificant, it may cause AAA-rated bonds to be downgraded. It is of note that such carve-outs have been declared unenforceable under H.R. 1106 (*Helping Families Save Their Homes Act of 2009*), which passed the House of Representatives on March 4, 2009, and is expected to be taken up by the Senate shortly.

Until the legislation is implemented and its effects seen in RMBS bond performance, the impact of additional (or reduced) losses at different parts of the capital structure remains uncertain and could lead to additional analysis and/or rating changes in RMBS and CDO securities.



Surveillance

The U.S. Structured Credit team reviews all rated transactions on an ongoing basis. For each transaction, rating actions are expected to be published quarterly, addressing any change in rating or review status or confirming ratings at their current levels.



Appendix: DBRS Rating Process

APPLICATION OF THE METHODOLOGY

The diagram below describes the overall process to analyze restructurings of ABS CDOs.

Asset Modeling

- (1) DBRS requests CUSIPs and par amounts for each asset inside the restructuring asset.
- (2) DBRS assigns an internal assessment to each asset and determines the category (e.g., RMBS, CMBS, CDO, etc.).
- (3) DBRS calculates default probabilities and recoveries for each asset based on ratings, category and tenor.
- (4) DBRS assigns asset correlation assumptions for each pair of assets based on category.
- (5) DBRS generates pool-wide loss rates for each rating level (RBLRPs) using the CDO Toolbox on the performing assets only (e.g., those assets that were not deemed C rated from the internal assessment process).

Liability Modeling

- (1) DBRS generates rep lines for the asset pool categorized on interest rate type and status (performing, interest-only credit, defaulted).
- (2) DBRS generates a set of scenarios that varies the pattern of defaults and interest rates.
- (3) DBRS models the structural features of the restructuring asset (hedges, waterfall, coverage tests, etc.) in the DBRS Cash Flow Model.
- (4) DBRS overlays the tranching and structural features of the restructuring issuer in the DBRS Cash Flow Model.
- (5) DBRS calculates the maximum amount of collateral losses (in terms of performing assets only) that the tranches issued by the restructuring issuer can withstand, the break-even default rate (BLR), for each scenario using the DBRS Cash Flow Model.
- (6) For transactions with minimal interest rate risk, the average BLR is used; for transactions with material amounts of interest rate risk, the minimum BLR is used.

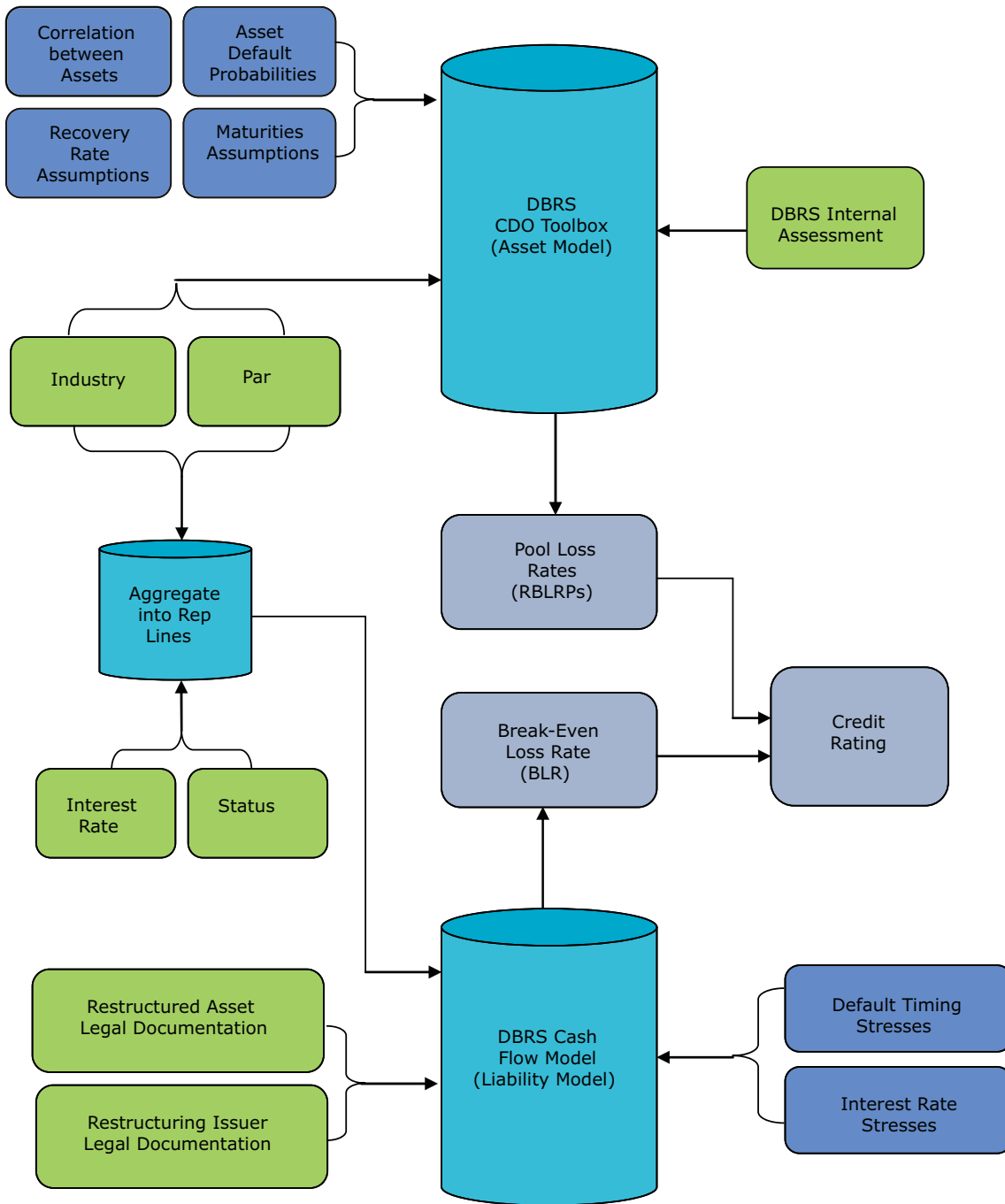
Determining the Rating

DBRS compares the BLR with the set of RBLRPs to determine the appropriate rating (e.g., the maximum RBLRP that is less than the applicable BLR).

The CDO Toolbox and the DBRS Cash Flow Model are substantial components of the DBRS rating process. A material deviation from the rating implied by both models would be defined as a three-notch rating difference. The quantitative and qualitative factors that could result in a material deviation are included in this methodology.



DBRS CDO ABS Restructuring Rating Process



Key



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