

Canadian Structured Finance Newsletter

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THE SKY IS NOT FALLING ON AUTO FLOORPLAN DEALS

On May 1, 2009, DBRS placed the Series 2007-D1, Series 2007-D2 and Series 2007-D3 notes (collectively, the Notes) issued by Canadian Revolving Auto Floorplan Trust (CRAFT) Under Review with Developing Implications following the announcement by Chrysler LLC (Chrysler) that it had filed for Chapter 11 bankruptcy protection in the United States on April 30, 2009. CRAFT was an automotive floorplan securitization transaction sponsored by DaimlerChrysler Financial Services Canada Inc. (DCFSC) whereby amounts owed to DCFSC from Chrysler dealerships across Canada had been securitized. The bankruptcy filing by Chrysler constituted an early amortization event (but did not constitute an event of default) under the CRAFT legal documents. As a result of the occurrence of an early amortization event, all principal collections received by CRAFT from Chrysler Canada dealers were allocated to the Notes on a pro rata basis.

In anticipation of the filing by Chrysler, another National Recognized Statistical Rating Organization took substantial rating action on the securities issued by CRAFT. By placing the Notes Under Review with Developing Implications however, DBRS took a different approach. DBRS considered a number of factors including structural protections included in the transaction and DBRS's expectation of a Chapter 11 reorganization of Chrysler as opposed to a Chapter 7 liquidation. DBRS also noted that the bankruptcy filing was restricted to the U.S. manufacturing entity.

DBRS confirmed the ratings of the CRAFT Notes on July 15, 2009. The confirmation was based on the continued strong performance of the transaction and the announcement from Chrysler that it had emerged from bankruptcy protection in the United States. On August 17, 2009, DBRS discontinued the ratings of CRAFT as all Notes had been repaid in full.

Those less familiar with structured finance may find it surprising that Notes with such a close connection with Chrysler would be repaid in full so soon after the bankruptcy of Chrysler. The quick payout of the Notes was no fluke and illustrates how structured finance is intended to work. Much of the time and effort put into structuring these transactions centres around ensuring that the special purpose vehicle (SPV) issuing securities, CRAFT in this instance, is bankruptcy remote. Bankruptcy remoteness is obtained when the bankruptcy of any party to the transaction will not result in the bankrupt entity's creditors having a claim on the assets of the SPV, or a claim on cash flows to the SPV and subsequently to noteholders. In the CRAFT transaction, Chrysler acted as a Performance Guarantor of the servicer while the cash flows owed to noteholders, both in the normal course and after an amortization event, originated from Chrysler Canada's dealership network of over 400 independent dealers. The obligations of the dealerships were supported by a security interest in the vehicles. Notwithstanding any downturn in business they may have experienced as a result of Chrysler's bankruptcy filing, it is evident that the vast majority of these dealerships continued to sell and service cars and trucks and continued to pay their bills.

Over the last 12-18 months, most developed economies have experienced the most severe economic downturn since the widespread adoption of securitization as a corporate funding source. It is inevitable in such an environment that securitization structures and transactions will be tested as they never have been before. In the case of CRAFT, securitization passed the test.

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