Methodology

Canadian Structured Finance Surveillance Methodology

MAY 2014

DBRS

Insight beyond the rating.
DBRS is a full-service credit rating agency established in 1976. Privately owned and operated without affiliation to any financial institution, DBRS is respected for its independent, third-party evaluations of corporate and government issues, spanning North America, Europe and Asia. DBRS’s extensive coverage of securitizations and structured finance transactions solidifies our standing as a leading provider of comprehensive, in-depth credit analysis.

All DBRS ratings and research are available in hard-copy format and electronically on Bloomberg and at DBRS.com, our lead delivery tool for organized, Web-based, up-to-the-minute information. We remain committed to continuously refining our expertise in the analysis of credit quality and are dedicated to maintaining objective and credible opinions within the global financial marketplace.
Canadian Structured Finance Surveillance

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Executive Summary

DBRS performs surveillance as part of the standard rating process. Once DBRS assigns a final short- and/or long-term rating to a security, the surveillance process begins and is continued for as long as DBRS maintains a rating on the security. All outstanding structured finance public and private ratings are monitored on a regular basis to ensure each rating reflects all data and information requested, received and sourced by DBRS. Ratings for structured finance vehicles reflect an opinion of the ability of the pooled assets to fund repayment to investors according to each security’s stated payment obligation.

The seller, servicer, financial services agent or administrator, as the case may be, is requested by DBRS to supply performance information and data over the life of the transaction at the time that a rating is assigned, and the maintenance of this rating is conditional upon the ongoing timely receipt of this information and data. Performance information and data for each outstanding transaction are reviewed upon receipt. In the event that the asset pools underlying a security are performing outside of expectations, or beyond the parameters commensurate with the assigned rating, further analysis is undertaken and, as warranted, a rating recommendation to take a rating action may be made to the DBRS structured finance rating committee. If a rating action is deemed appropriate, a summary of the action and its basis is published on the DBRS website in a press release and, in some cases, in an updated rating report.

Surveillance data and indexes that compile information on sector performance and related commentary are published on www.dbrs.com.

General Surveillance Approach

The Canadian structured finance surveillance process begins after DBRS assigns a final rating to a series of notes, or assigns a transaction assessment to a Canadian structured finance transaction entered into by an asset-backed commercial paper (ABCP) conduit. The process continues until the rated security has been fully repaid or the rating is discontinued-withdrawn. All outstanding structured finance notes with public or private ratings and all transaction assessments are monitored to ensure that the underlying assets and credit enhancement available are sufficient to repay interest and principal on the notes according to the terms of the related legal documents and remain commensurate with the current rating.

The maintenance of each rating relies on the timely receipt of performance information and data from the seller, servicer, financial services agent or administrator. Upon receipt of this information, DBRS surveillance analysts review the information and may contact the seller, servicer, financial services agent or administrator to gain additional information should any inconsistency or question arise. If the quality of information provided to DBRS is not considered sufficiently reliable to properly monitor the transaction, DBRS may discontinue the existing rating. DBRS also monitors changes in macroeconomic conditions and other events that may affect outstanding ratings.

The performance information received from the seller, servicer, financial services agent or administrator is entered into the DBRS surveillance database, which generally stores historical data, transaction triggers and key assumptions used in the initial analysis of the transaction. The database may also store calculated performance indicators, transaction-specific definitions, notes and other relevant information.

Following receipt of the performance data related to each rated security or transaction assessment, DBRS analysts undertake a review of each transaction. DBRS conducts periodic reviews for all outstanding transactions and each transaction is reviewed by a rating committee at least annually.
The review of each transaction encompasses an analysis of the related assets’ current credit performance and trends and a review of pool performance taking into consideration transaction-specific triggers, the financial strength of counterparties and other factors that may affect the rating.

As a result of this surveillance process, DBRS surveillance analysts may identify transactions that are not in compliance with their triggers as defined in the legal documents for the transaction. Transactions that have breached any trigger, as well as transactions that are performing within the expected parameters but exhibit signs of deterioration in their financial or operational strength, may be placed on an internal watchlist. These transactions may be subjected to more in-depth analysis to ensure the transaction mechanics, such as cash traps, counterparty replacement, servicer replacement, sale perfection and any other required action as per the transaction documents, have been implemented and/or maintained according to the terms of the documents.

If, at any time, the underlying assets are expected to continue performing below DBRS-expected parameters, or any counterparty in a transaction does not perform as expected or is no longer considered to be commensurate with the rating of the notes or the transaction assessment, the transaction may be reviewed by the structured finance rating committee to determine whether a rating action is necessary.

Likewise, if at any time the underlying assets are expected to continue performing above DBRS-expected parameters, or if credit enhancement levels have increased to a level that would warrant a rating action, the transaction may be reviewed by the structured finance rating committee. However, higher levels of credit enhancement than initially provided may not be enough for subordinated notes to be upgraded due to the subordinated structure.

All Canadian structured finance rated securities or transaction assessments with an outstanding balance are reviewed by rating committee at least annually. For the annual review process, the surveillance analysts, together with the transaction analysts, undertake a review of the performance of the underlying assets, credit enhancement and various other terms of the transaction, within the context of their legal documents and the appropriate DBRS methodology. Based on the review, an appropriate rating recommendation is made to the rating committee.

For more information on DBRS rating policies, including the rating committee process, rating actions and rating scales, please refer to www.dbrs.com under “About Ratings.”

DISCLOSURE
In order to provide market participants with updates and to provide greater transparency to the markets, once a rating action has been taken on a public rating, DBRS publishes a press release and, in some cases, an updated rating report. The press release includes the name of the issuer, the rating action taken, the rating assigned to the notes, the rationale behind the rating action, the title of the relevant methodology(ies), links to other related information available, such as the rating report where a more detailed description of the structure is available, and a list of DBRS contacts.

Prior to public dissemination, the draft documents of the press release and/or the updated rating report, as applicable, are provided to the seller, servicer, financial services agent or administrator for a review of factual information and to ensure that they do not contain any confidential information belonging to the organization.

When a rating action on a transaction with a private rating has been taken, a rating letter may be provided to the issuer, seller, servicer, financial services agent or administrator, or to the party that has engaged DBRS to provide the private rating, as appropriate.
For both public and private ratings, the seller, servicer, financial services agent or administrator may request an appeal of a DBRS rating action. For more information on the Rating Appeal Policy, please refer to DBRS rating policies, which can be found on www.dbrs.com under “About Ratings.”

In addition to providing the market with updates on the ratings assigned to each transaction, DBRS publishes four reports, with free access, that contain key performance metrics for each public transaction in the Canadian structured finance market that has an outstanding balance in the reporting period. The purpose of these reports is to allow market participants to assess the ongoing performance of related notes and transactions. The reports are found on the DBRS website, www.dbrs.com, under Research/Monthly Reports and are published on a monthly basis. The reports are:

1. Monthly Canadian ABS Report
2. Monthly Canadian ABCP Report
3. Canadian Securitization Market Overview Report
4. Monthly Canadian Covered Bond Report

DBRS also produces industry benchmarks to provide additional transparency to market participants, such as the credit card index, automotive cumulative credit losses by issuance year and residential mortgage-backed securities (RMBS) defaults for prime mortgages, which are published in the Canadian Securitization Market Overview Report.

Finally, DBRS publishes press releases to indicate when a series of notes has been fully repaid and/or the rating has been discontinued.

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**Canadian Asset-Backed Securities**

The purpose of this section is to set forth the surveillance methodology and process DBRS follows in its ongoing surveillance of Canadian asset-backed securities (ABS) (or transaction assessments, if applicable).

The Monthly Canadian ABS Report (the ABS Report) is published based on the information provided to DBRS. The ABS Report provides market-level data for outstanding ABS issued by all Canadian ABS issuers rated by DBRS. In addition, the ABS Report provides detailed information at the issuer level for public transactions on the performance of the portfolio of assets.

Each month, DBRS also publishes the Canadian Securitization Market Overview Report (the Market Overview Report). The Market Overview Report provides information with respect to market size, market share and asset composition of the securitization market rated by DBRS. This report includes trend charts of key performance metrics for the largest asset classes, such as Canadian automotive static net loss curves, Canadian credit card performance metrics and quarterly residential mortgage default rates.

The following provides specific performance-related metrics by asset class that DBRS structured finance surveillance analysts may regularly review during the surveillance process.
Auto Loan and Leases

OVERVIEW
Traditional retail auto loan securitizations represent the contractual obligations of customers who have financed the purchase of their vehicles. It is important to note that the vehicles are owned by the individual obligors and cannot be returned to the dealer unless repossessed by the financing entity. The major risk in securitizations of traditional auto loans is the credit risk associated with the monthly payments receivable from the obligors. However, the introduction of new products that combine lease-type features (through a put option) and traditional loan financing may add residual value risk to this type of securitization.

Auto lease securitizations represent the contractual obligations of customers who have financed their vehicles via lease contracts. A typical consumer lease contract in Canada is a closed-end lease whereby the obligor has the option to purchase the car at the end of the term at a predetermined price, extend the lease or return the vehicle to the financing entity. It is important to note that ownership of the vehicles is maintained by the financing entity and, as a result, residual value risk is significant in a lease securitization.

There are several different elements of risk that affect an auto loan or auto lease transaction. DBRS reviews these risks and monitors their development.

<table>
<thead>
<tr>
<th></th>
<th>Retail Auto Loan</th>
<th>Retail Auto Lease</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concentration Risk</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Credit Risk</td>
<td>Low to medium</td>
<td>Low to medium</td>
</tr>
<tr>
<td>Residual Value Risk</td>
<td>n/a</td>
<td>Medium to high</td>
</tr>
<tr>
<td>Manufacturer Risk</td>
<td>Low</td>
<td>Medium to high</td>
</tr>
<tr>
<td>Asset Features</td>
<td>Amortizing</td>
<td>Amortizing</td>
</tr>
<tr>
<td>Enhancement</td>
<td>Cash</td>
<td>Cash (embedded loss)</td>
</tr>
<tr>
<td></td>
<td>Overcollateralization</td>
<td>Overcollateralization</td>
</tr>
<tr>
<td></td>
<td>Subordinated notes</td>
<td>Subordinated notes</td>
</tr>
<tr>
<td></td>
<td>Excess spread</td>
<td>Excess spread</td>
</tr>
</tbody>
</table>

Strengths of securitized auto loan and lease portfolios include highly diversified pools of obligors and the remarketability of the assets. Potential challenges for these assets include the sensitivity of pool performance to general economic conditions, the health of the vehicle manufacturer, consumer credit behaviour and seasonal and cyclical used-vehicle prices.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Gross Loss/Recovery Rates: DBRS tracks cumulative net losses for amortizing pools, which are a function of gross losses and recoveries. Increased gross loss rates, when recovery rates are constant, lead to higher net losses and greater stress on available credit enhancement.

The actual cumulative net loss curve is compared against expectations and stresses used in the original rating of the transaction to determine if the transaction is performing within the expected parameters for the rating level assigned. If the transaction is performing outside expectations, remaining net cumulative
credit losses are projected and measured against the credit enhancement available to the noteholders to
determine if the loss coverage ratio is still commensurate with the rating assigned.

Cumulative losses are projected over the remaining life of the security, using the greater of (1) the annual-
ized net loss rate assumed at the onset of the transaction and (2) the actual annualized loss rate experienced
by the assets.

Losses are a function of market conditions, collateral, originator and obligor type.

Residual Value: In evaluating a pool of leased vehicles, it is clear that residual value risk represents the
single-largest component of overall risk in an auto lease securitization. DBRS compares the actual cumu-
lative residual value losses realized in the pool with the expectations set at the onset of the transaction
and projects the residual value losses over the remaining life of the transaction, based on the outstanding
pool, by applying standard stress levels for each rating.

Delinquency: As a leading indicator, later-stage delinquencies (60 days or more) tend to be an accurate
leading indicator of defaults, since obligors that fall behind in payments tend to have difficulty recovering.

Prepayments: Payments that are received in advance of the scheduled payment dates are termed prepay-
ments. Voluntary prepayments result from factors such as obligors deciding to pay off auto loans early as
a result of trade-ins or sales of the financed vehicles. Involuntary prepayments are due to loan liquidations
arising from insurance claims or obligor status. Prepayment rates are also important to monitor as high
levels of prepayments may lead to lower excess spread available in the future.

Credit Enhancement/Excess Spread: Credit enhancement typically consists of a minimum level of cash,
which provides short-term liquidity to the transaction; a combination of subordination, overcollateraliza-
tion and excess interest rate spread; or acceptable third-party forms of enhancement.

Excess spread arises when the interest rate earned on the collateral in the underlying asset pool is greater
than the sum of expenses and funding costs. Excess spread creates an additional cushion to withstand
collateral losses and cash flow shortfalls, as the excess spread is additional cash that is available at the
end of every month. Excess spread can be either retained as internal support or be released back to the
originator, depending on the transaction structure and pool performance.

RATING METHODOLOGY
Further information about the DBRS rating methodology for Canadian auto loan and lease securitiza-
tions can be found in the following publication available on the DBRS website:

Rating Canadian Auto Retail Loan and Lease Securitizations
Auto Fleet Leasing

OVERVIEW
Lease contracts in Canadian auto fleet leasing structures have typically involved open-end corporate auto fleet leases of cars; light-, medium- and heavy-duty trucks; sport-utility vehicles; some specialized trucks; and equipment, with the obligors assuming all risk for the value of the vehicle at the time of disposition. To date, fleet transactions in Canada have contained only a small percentage of closed-end leases. An auto fleet leasing structure is exposed to residual value risk to the extent that the portfolio includes closed-end leases.

In an auto fleet leasing structure, investors receive interest and principal payments based on collections from customers on the monthly lease contracts for use of the vehicle, management fees and, where applicable, proceeds received from the disposition of vehicles in the portfolio of leases. Management fees arise from services offered by the management companies to their customers, such as fuel services, repairs and maintenance, accident services, titling, tax services, licensing, remarketing and other ancillary services. In some cases, the management fee represents a significant portion of the total monthly cash flow as the vehicles in the portfolio depreciate, resulting in an increasing yield on the portfolio.

There are several different elements of risk that affect an auto fleet leasing transaction. DBRS reviews and monitors these risks.

<table>
<thead>
<tr>
<th>Corporate Auto Fleet Leasing</th>
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</thead>
<tbody>
<tr>
<td>Concentration Risk</td>
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<tr>
<td>Credit Risk</td>
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<tr>
<td>Residual Value Risk</td>
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<tr>
<td>Manufacturer Risk</td>
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<tr>
<td>Asset Features</td>
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<tr>
<td>Enhancement</td>
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<td></td>
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</tbody>
</table>

Strengths of auto fleet leasing structures include low credit risk, diversification of exposure to vehicle manufacturers and remarketability of the assets. Potential challenges for these assets include obligor concentration risk, the financial health of the fleet company and used-vehicle prices.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Industry and Obligor Concentrations: Given that auto fleet lease transactions are characterized by a portfolio of corporate obligors that lease a small-to-large number of vehicles, obligor concentration risk is greater than in a transaction backed by consumer auto leases. The credit rating of the obligors is an important element in the assessment of the portfolio and required credit enhancement in the transaction. As the best proxy for the ability to pay, DBRS monitors and relies on published credit ratings of the obligors.
**Loss Rate:** Obligor defaults in auto fleet lease transactions have historically been associated with the bankruptcy of the obligor. If the obligor is reorganizing under bankruptcy protection, the fleet manager will, in many cases, be considered a critical vendor due to the role played by the vehicles in the obligor’s business. If the obligor foregoes a restructuring and liquidates its property to pay off its creditors, the fleet manager can repossess the assets prior to their becoming part of the liquidation and can remarket the vehicles to maximize recovery. Losses in auto fleet lease pools have historically been low.

**Credit Enhancement/Excess Spread:** Credit enhancement generally consists of excess spread, overcollateralization, subordination and a cash reserve or letter of credit (L/C) amount. The cash or L/C provides short-term liquidity to the transaction.

Excess spread arises when the interest rate earned on the collateral in the underlying asset pool is greater than the sum of expenses and funding costs. Excess spread creates an additional cushion to withstand collateral losses and cash flow shortfalls, as the excess spread is additional cash that is available at the end of every month. Excess spread can be either retained as internal support or be released back to the originator, depending on the transaction structure and pool performance.

A unique characteristic of auto fleet lease pools is that the excess spread on most portfolios increases as the lease contracts age. This increasing yield is due to the fact that the management fee is usually a fixed dollar amount per lease per month, while the lease amortizes in line with the depreciation charges on the vehicle.

**RATING METHODOLOGY**
Further information about the DBRS rating methodology for Canadian auto fleet lease transactions can be found in the following publication available on the DBRS website:

*Rating Canadian Auto Fleet Lease Transactions*

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**Rental Car Securitization**

**OVERVIEW**
A typical Canadian rental car securitization involves the creation of a limited partnership, with ABCP trusts or a master trust (Funding Trust) as the primary funding source and possible limited partner, and the rental car company as the general partner. Proceeds from the rental contracts and vehicle dispositions are distributed to the partners and, ultimately, to the noteholders.

The rental car fleet is composed of program vehicles and non-program vehicles. Vehicles are referred to as program vehicles when there is a repurchase agreement negotiated between the vehicle rental company and the corresponding auto manufacturer. Under the terms of these repurchase agreements, the auto manufacturer, subject to certain conditions, agrees to repurchase its vehicles from the rental company at an agreed-upon price. The vehicles that are not part of a repurchase agreement are referred to as non-program vehicles or at-risk vehicles and are held by the rental vehicle company and disposed of at the end of their life as a daily rental vehicle. The entity (the manufacturers or the daily rental company) that bears the residual value risk drives the unique structuring features of a rental car fleet securitization transaction.

Structures established for rental car fleet transactions have been different from those for auto lease or loan transactions. The difference evolved from the reliance on the rental car company to manage its fleet efficiently, which includes the purchase, rental, maintenance and ultimate sale or return of the fleet in a cyclical environment.
There are several different elements of risk that can affect a rental car transaction. DBRS reviews these risks and monitors their development.

### Daily Rental Car Fleets

<table>
<thead>
<tr>
<th>Risk Type</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concentration Risk</td>
<td>High</td>
</tr>
<tr>
<td>Credit Risk</td>
<td>Low</td>
</tr>
<tr>
<td>Residual Value Risk</td>
<td>Medium (Non-Program Vehicles)</td>
</tr>
<tr>
<td>Manufacturer Risk</td>
<td>Medium (Program Vehicles)</td>
</tr>
<tr>
<td>Asset Features</td>
<td>Revolving</td>
</tr>
<tr>
<td>Enhancement</td>
<td>Cash, Overcollateralization, Subordinated notes, Letters of credit</td>
</tr>
</tbody>
</table>

Strengths of rental car securitizations include low credit risk and remarketability of the assets. Potential challenges for these assets include reliance on the success of the rental car company and its ability to continue to generate cash flow from the fleet of vehicles to repay the noteholders, as well as the sensitivity of pool performance to general economic conditions, volatility in the used-car market and the financial health of the vehicle manufacturer.

**SURVEILLANCE**

While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

**Residual Value**: The cash flow generated by the activities of the bankruptcy-remote entity involved in the securitization is designed to include the depreciation of the vehicles on a monthly basis. The depreciation rates are determined for non-program vehicles based on an estimated residual value of the vehicles when they are retired from the fleet. The extent to which vehicles do not depreciate in line with expectations will determine the amount of gain or loss on the sale of these vehicles at the time of disposition. Any losses beyond a predetermined amount may require a step-up of enhancement.

**Cash Flow Coverage**: The cash flow coverage ratio measures the monthly cash flows required to service and operate the rental fleet. A significant decrease in the cash flow coverage ratio is an early warning sign that the operator is not managing the fleet efficiently, potentially resulting in an early termination of the transaction.

**Credit Enhancement**: Credit enhancement levels in rental car securitizations are dynamic. They are based on changes in the composition of the collateral and in the ratings of the vehicle manufacturers. Credit enhancement generally consists of cash, L/Cs, subordination and overcollateralization (capital contribution or equity in the partnership provided by the general partner). Since the fleet is turning over on a regular basis, DBRS requires a minimum level of cash in the enhancement structure to cover expected residual value losses, ensuring sufficient liquidity in the transaction to meet periodic interest payments.

**RATING METHODOLOGY**

Further information about the DBRS rating methodology for Canadian rental car securitizations can be found in the following publication available on the DBRS website:

*Rating Canadian Rental Car Fleet Securitizations*
Floorplan Financing

OVERVIEW
Floorplan funding is provided to dealers of automobiles, heavy equipment, recreational vehicles or other equipment to finance the inventory while in their possession. Such financing is generally provided from the time of receipt of the inventory by the dealers from the manufacturer to the time of its sale to the end user. Repayment of floorplan financing is ultimately linked to the sale of the inventory to the end user. These floorplan financing loans are originated by both captive financing companies and third-party financing companies. The financial strength of the manufacturer and individual dealers, the concentration of dealerships and the type of assets being financed are among the factors considered by DBRS when assessing floorplan finance transactions.

While the assets supporting floorplan financing can vary from consumer products to commercial equipment, to date the Canadian securitization market has focused on floorplan transactions in which the inventory has consisted of automotive vehicles, agricultural machinery, construction equipment and their related parts.

There are several different elements of risk that affect a floorplan transaction. DBRS reviews these risks and monitors their development.

<table>
<thead>
<tr>
<th></th>
<th>Floorplan</th>
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<tbody>
<tr>
<td>Concentration Risk</td>
<td>High</td>
</tr>
<tr>
<td>Credit Risk</td>
<td>Low</td>
</tr>
<tr>
<td>Residual Value Risk</td>
<td>n/a</td>
</tr>
<tr>
<td>Manufacturer Risk</td>
<td>High</td>
</tr>
<tr>
<td>Asset Features</td>
<td>Revolving</td>
</tr>
<tr>
<td>Enhancement</td>
<td>Cash</td>
</tr>
<tr>
<td></td>
<td>Overcollateralization</td>
</tr>
<tr>
<td></td>
<td>Subordinated notes</td>
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<td></td>
<td>Excess spread</td>
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</table>

The strengths of these assets are the low credit risk and remarketability of the vehicles and equipment. Potential challenges are the high concentration risk and reliance on the manufacturer’s financial strength. Retail support to the dealers is often provided by the manufacturer at the front end of the sales process through sales incentives, program warranties and replacement parts. Most manufacturers are also active in the back end of the sales process by creating online auctions for remarketing used equipment.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Payment Rate: Similar to those of other revolving asset classes, floorplan loans are supported by short-term obligations that are repaid regularly, with the proceeds used to fund newly generated receivables. Specifically, as the inventory turns over, the proceeds from sales are used to repay the loans, and new loans are advanced as the dealer purchases new inventory from the manufacturer. Floorplan transactions rely heavily on a consistent and stable monthly payment rate to ensure timely payment of interest and principal. Close inspection of payment rates in floorplan structures will generally reveal cyclical or
seasonal payment rates that reflect underlying consumer demand within the specific industry to which the floorplan loans are linked.

A high payment rate typically would indicate robust demand for the manufacturer’s product and the ability of the network of dealers to turn over the inventory. A low payment rate may be due to seasonality or may be an early sign suggesting that the pool is at risk of experiencing potential defaults in the dealer networks as a result of weakening demand for the product. Moreover, payment rates are the key determinant in how quickly investors are repaid in a rapid amortization scenario, thus either extending or reducing the amount of time investors may be exposed to asset deterioration.

**Default and Loss Rates:** Net losses are the result of the default frequency and severity of loss upon disposition of the assets. Historical default rates are low for ongoing floorplan deals. A high level of loss rates reduces available credit enhancement.

**Credit Enhancement/Excess Spread:** Credit enhancement is typically provided by way of overcollateralization and a cash reserve account usually funded at inception. Subordinated notes may also be incorporated, allowing the senior notes preferential access to cash flows.

Excess spread arises when the interest rate earned on the collateral in the underlying asset pool is greater than the sum of expenses and funding costs. Excess spread creates an additional cushion to withstand collateral losses and cash flow shortfalls, as the excess spread is additional cash that is available at the end of every month. Excess spread can be either retained as internal support or be released back to the originator, depending on the transaction structure and pool performance.

Other performance triggers include used-vehicle limits and a minimum test on the total number of receivables in the pool available to repay principal and interest.

**RATING METHODOLOGY**

Further information about the DBRS rating methodology for Canadian floorplan securitizations can be found in the following publication available on the DBRS website:

*Rating Canadian Floorplan Securitizations*

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**Equipment Finance**

**OVERVIEW**

The financed assets range from small-ticket items, such as office equipment, to medium- and large-ticket items, such as transportation vehicles and farm implements. While equipment securitization transactions have similar credit characteristics as other amortizing pools, such as auto loans and leases, they also have a number of unique features that must be considered in the analysis of the transaction. In particular, equipment securitization can encompass a wide variety of asset types that must be analyzed. The specialized nature of the equipment and the remarketing channels must be considered as part of the recovery valuation. Also, certain sectors, such as agriculture, have seasonal cash flows characterized by periodic payments, which the transaction structure must account for.

Although the financial obligations are either loans or leases, there is minimal exposure to the residual value as the obligor is usually responsible for any shortfall upon remarketing of the equipment, thereby eliminating many of the cash flow differences between these forms of financing.
Strengths and challenges for equipment finance structures depend on the type of equipment leased as they have an impact on the performance of the deal with respect to default and recovery rates. While large-ticket items typically retain their value and result in much higher recoveries in the event that they have to be liquidated, the resale value for small-ticket items is low or nil.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Gross Loss/Recoveries: DBRS tracks cumulative net losses, which are a function of gross losses and recoveries, on a monthly basis. Increased gross loss rates, when recovery rates are constant, lead to higher net losses and greater stress on available credit enhancement.

The actual cumulative net loss curve is compared against expectations and stresses used in the original rating of the transaction to determine if the transaction is performing within the expected parameters for the rating level assigned. If the transaction is performing outside expectations, remaining net cumulative credit losses are projected and measured against the credit enhancement available to the noteholders to determine if the loss coverage ratio is still commensurate with the rating assigned.

Cumulative losses are projected over the remaining life of the security, using the greater of (1) the annualized net loss rate assumed at the onset of the transaction and (2) the actual annualized loss rate experienced by the assets.

Losses are a function of market conditions, collateral, originator and obligor type.

Delinquency: As a leading indicator, later-stage delinquencies (60 days or more) tend to be an accurate leading indicator of defaults, since obligors that fall behind in payments tend to have difficulty recovering.

Prepayments: Payments that are received in advance of the scheduled payment dates are termed prepayments. Prepayment rates are also important to monitor as high levels of prepayments lead to lower excess spread available in the future.

Credit Enhancement/Excess Spread: The credit enhancement for an equipment securitization structure is typically a combination of overcollateralization, cash reserves, subordinated notes and excess spread. In addition, other forms of enhancement, such as L/Cs or guarantees, can be considered.

Excess spread arises when the interest rate earned on the collateral in the underlying asset pool is greater than the sum of expenses and funding costs. Excess spread creates an additional cushion to withstand collateral losses and cash flow shortfalls, as the excess spread is additional cash that is available at the end of every month. Excess spread can be either retained as internal support or be released back to the originator, depending on the transaction structure and pool performance.

RATING METHODOLOGY
Further information about the DBRS rating methodology for Canadian equipment finance securitizations can be found in the following publication available on the DBRS website:

Rating Canadian Equipment Finance Securitization Transactions
Credit Cards

OVERVIEW
Credit cards are unsecured revolving lines of credit. Credit card receivables are generated when cardholders use their cards to finance the purchase of goods and services or make cash advances. Cardholders are typically only required to make a minimum payment each month on the outstanding balance in order to remain in good standing. However, the entire outstanding amount is contractually payable on demand.

Strengths of this asset class typically include its diversified pools of obligors, the strong and consistent payment rates and low loss rates. Challenges for this asset class include the sensitivity of asset performance to general economic conditions, consumer-credit behaviour and exposure to changes in the credit, as well as the collection and/or underwriting policies of the originator.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Loss Rate: Losses are defined as write-offs less recoveries, if applicable. Delinquent receivables over 180 days overdue are required to be written off as uncollectible by the servicer, according to guidelines set by the Office of the Superintendent of Financial Institutions (OSFI). Obligors that file for bankruptcy and/or enter into consumer proposals are also written off per standard credit and collections policy. Increased loss rates may be attributable to the changes in macroeconomic conditions, such as unemployment trends, consumer wealth formation and household leverage ratios, or changes in the consumer’s personal situation, such as divorce, job loss or medical issues. Increase in loss rates may also reflect the changes in the issuer underwriting and servicing standards of the accounts. A high level of net loss rates reduces available credit enhancement.

Gross Yield: Portfolio gross yield is generated from finance charges, which include interest charges, annual card fees, interchange fees, cash advance fees, over-limit fees and other miscellaneous fees levied on cardholders. DBRS tracks the individual components of yield separately to the extent data are available. This allows DBRS to assess trends at a more detailed level.

Monthly Payment Rate: Payment rates represent total monthly collections received from cardholders divided by the receivables balance. Higher payment rates mean that more receivables are converted into cash. It is an important metric to determine the length of time needed to repay the notes during either controlled accumulation or early amortization periods. In the case of an early amortization, a low payment rate extends the amount of time investors may be exposed to asset deterioration.

Credit Enhancement/Excess Spread: Credit enhancement is typically provided by excess spread, subordination of notes and a cash reserve account that may be funded at closing or structured to build up if excess spread levels fall below certain thresholds. Overcollateralization and L/Cs may also be used as a form of enhancement.

Excess spread is equal to the portfolio yield less the sum of funding costs, losses, servicing fees (if applicable) and other trust fees. The excess spread in a credit card transaction is a key source of credit enhancement as it is generally the highest among all asset classes. Compression of excess spread may result in a negative impact on the ratings of credit card transactions. Excess spread can be either retained within the transaction structure or be released back to the seller, depending on the transaction documentation and/or pool performance.
Stress Testing: In addition to general trend analysis of key performance variables, DBRS performs cash flow stress testing for each rated class at least once a month on an “as is” basis. The performance variables are stressed without applying any haircut or assumptions, thereby identifying any performance deviation from DBRS expectation at issuance, sufficiency of available enhancement and possible rating impacts.

RATING METHODOLOGY
Further information about the DBRS rating methodology for Canadian credit card securitizations can be found in the following publication available on the DBRS website:

DBRS Criteria for Canadian Credit Card Securitization

Home Equity and Personal Lines of Credit

OVERVIEW
Personal lines of credit (PLC) are typically revolving loans with an approved credit limit that allow borrowers more flexible access to funds, compared to a traditional amortizing loan. PLCs generally allow borrowers to draw and repay an amount for an indefinite period (the revolving period), as long as the account is in good standing and the outstanding balance is within the credit limit. To remain in good standing, borrowers are typically required to make the minimum payment as stipulated in the contract terms; however, the entire outstanding amount is contractually payable on demand. PLCs may be either unsecured or secured by an asset or collateral owned by the borrower.

A home equity line of credit (HELOC) has a residential property as underlying security to the lender and provides the borrower with the flexibility and convenience of a line of credit with a more favourable rate than an unsecured line of credit. The credit limit on a HELOC is set according to the property value and the loan-to-value (LTV) ratio of the property at origination, which takes into account the lien of the HELOC lender and any other liens with priority on the property.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Loss Rate: Loans are considered in default once they are delinquent for a certain period of time or are written off according to the originator’s credit and collection policy. The loss rate is calculated as the amount written off, net of recoveries, in one period as a percentage of the amount of receivables outstanding. A high level of net loss rates reduces available credit enhancement.

Gross Yield: Portfolio gross yield is generated from finance charges, which include interest charges and other miscellaneous fees.

Monthly Payment Rate: Payment rates represent total monthly collections received from borrowers divided by the receivables balance. Higher payment rates mean that more receivables are converted into cash. It is an important metric to determine the length of time needed to repay the notes during either controlled accumulation or early amortization periods. In the case of an early amortization, a low payment rate extends the amount of time investors may be exposed to asset deterioration. Payment rates are affected by several variables, including the credit quality of the obligors, contract terms, general economic conditions and consumer spending and borrowing patterns.
Credit Enhancement/Excess Spread: Credit enhancement is typically provided by excess spread, subor-
dination of notes and a cash reserve account that may be funded at closing or structured to build up if excess spread levels fall below certain thresholds. Overcollateralization and L/Cs may also be used as a
form of enhancement.

Excess spread arises when the interest rate earned on the collateral in the underlying asset pool is greater
than the sum of expenses and funding costs. Excess spread creates an additional cushion to withstand
collateral losses and cash flow shortfalls, as the excess spread is additional cash that is available at the
end of every month. Excess spread can be either retained as internal support or be released back to the
originator, depending on the transaction structure and pool performance.

RATING METHODOLOGY
Further information about the DBRS rating methodologies for home equity and personal lines of credit
securitizations can be found in the following publications available on the DBRS website:

DBRS Criteria for Canadian Credit Card Securitization
Appendix 1: Personal Lines of Credit

Rating Canadian Residential Mortgage-Backed Securities (RMBS) and Home Equity Line of Credit (HELOC) Transactions

Residential Mortgages

OVERVIEW
The securitization of residential mortgages in Canada typically involves the financing of first mortgages
secured by property. Residential mortgages in Canada have historically exhibited excellent performance
due to the conservative underwriting practices applied in the origination of the pools securitized and/
or the equity in the underlying property, as most originators have strict maximum LTVs that may be
advanced to the borrower.

Insured mortgages have the added feature of an insurance policy that covers the lenders for the losses or
expenses that may be incurred should the borrowers default.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to
monitor the following performance metrics to develop a more comprehensive picture of a transaction’s
performance.

Losses: Losses on defaulted mortgages are determined by the sale proceeds of foreclosed properties and
the mortgage amount outstanding, in addition to the available insurance payment. The credit loss on
insured mortgages should generally be negligible as insurers guarantee the full repayment of principal and
accrued interest when the borrowers default on the mortgage. A high level of credit losses reduces credit
enhancement available.

Prepayment Rate: Prepayment speed measures the rate at which borrowers make their principal repay-
ments above the requirement prior to the scheduled maturity date. Prepayments reduce the outstanding
principal balance of a mortgage, thereby reducing possible defaults and the severity of loss given default
in the future.
Default Rate: The foreclosure process on a property can only begin after the borrower defaults on the mortgage payments, which is over 90 days past due in Canada. A large negative deviation of actual default experience from DBRS expectation at issuance would warrant a reassessment of sufficient credit enhancement levels and potential rating impacts.

Credit Enhancement/Excess Spread: Common forms of credit enhancement are a cash collateral account, subordination, overcollateralization, L/C and/or excess spread.

Excess spread is the difference between the mortgage yield and the sum of funding costs, credit losses, servicing expenses (if applicable) and other fees. Excess spread may be released back to the seller, retained as part of credit protection or stripped and issued as margin-related securities, depending on the transaction structure and/or pool performance.

RATING METHODOLOGY
Further information about the DBRS rating methodology for Canadian residential mortgage-backed securities can be found in the following publication available on the DBRS website:

Rating Canadian Residential Mortgage-Backed Securities (RMBS) and Home Equity Line of Credit (HELOC) Transactions

Reverse Mortgages

OVERVIEW
A reverse mortgage is a non-recourse mortgage loan offered to elderly individuals or couples interested in obtaining cash as a lump sum payment in return for a first-ranking security interest in their residential property. The reverse mortgage is secured solely by the property. No interest or principal payments are required during the owner’s occupancy, although interest does accrue on the mortgage. This means that the loan balance is accreted until the loan matures.

The advance allowed at origination is usually set at a conservatively low LTV limit to ensure that the property value, even with a modest appreciation, will be larger than the accreting loan amount when the mortgage is due. In addition, as a general policy, an LTV cap may be set for the maximum accrual of a single reverse mortgage.

SURVEILLANCE
DBRS endeavours to monitor the amount of losses, if any, experienced by the managed portfolio of reverse mortgages, in addition to the weighted-average LTV of the pool portfolio, debt leverage and mortgage repayments to get a more comprehensive picture of pool credit performance, credit enhancement levels and liquidity available for the payment of interest and principal to the noteholders.

Credit Enhancement: Common forms of credit enhancement are subordination, a cash account established to mitigate the uncertainty of the cash flows, overcollateralization, L/C and excess spread.

RATING METHODOLOGY
Further information about the DBRS rating methodology for reverse mortgage-backed securities can be found in the following publication available on the DBRS website:

Rating Canadian Structured Finance Transactions
Appendix: Reverse Mortgages
Trade Receivables

OVERVIEW
Trade receivables securitization provides funding to sellers in exchange for an acquisition of receivables originated in the course of providing goods or services. Trade receivables portfolio performance is quite different across industries and even between companies within the same industry. Payment terms may also vary by customer and business line, ranging from very short terms to a deferred receivable with a fixed payment date related to the seasonal nature of an industry.

Strengths of trade receivables securitizations include generally low losses, high turnover and strong creditworthy sellers and/or customers. Some of the challenges are that receivables are typically unsecured and therefore recovery rates are extremely low. In addition, some programs may not be highly diversified, with some customers representing a material portion of the pool.

SURVEILLANCE
While reporting requirements and data availability may vary between issuers, DBRS endeavours to monitor the following performance metrics to develop a more comprehensive picture of a transaction’s performance.

Losses: Losses incorporate all receivables related to an obligor who has become insolvent, plus all receivables entering a specified aging period of delinquency beyond which the likelihood of full repayment is significantly reduced.

Delinquency Rate: A receivable’s aging period is compared with sales for the period in which they were originated. Delinquency rates are a good indicator of potential future losses.

Dilution Rate: Dilutions are non-cash adjustments reflecting changes to the value of the receivable made subsequent to the initial record of sale. These generally relate to discounts, returns, retroactive price adjustments and disputes or other processes that reduce or eliminate amounts owing for reasons other than for collections or losses. Monitoring dilutions is important as they reduce the value of receivables owned by the trust. Trade receivables securitizations typically include a dilution reserve or an indemnity from the seller to protect, to some extent, the noteholders from this type of risk.

Credit Enhancement: Trade receivables securitizations use a dynamic credit enhancement reserve that adjusts according to the performance of the portfolio, recognizing that the performance of the receivables can vary widely from month to month.

Credit enhancement is typically provided by way of overcollateralization, which consists of unfunded receivables contributed to the conduit by the seller. An L/C from an acceptably rated financial institution may also be used as a second-loss component of credit enhancement.

RATING METHODOLOGY
Further information about the DBRS rating methodology for trade receivables securities can be found in the following publication available on the DBRS website:

Rating Canadian Trade Receivables Securitization Transactions
Flow-Through Ratings

OVERVIEW
A flow-through rating refers to a rating assigned to a security based on the credit strength of a third-party entity rather than on the credit strength of the issuer or the underlying assets that back the issuer’s security. Due to the nature of the flow-through ratings, when the third-party entity’s rating decreases, or it appears to DBRS that the third-party entity will not be able to meet its payment obligations to the issuer, the rating of the issuer’s securities will likely be affected.

SURVEILLANCE
DBRS monitors the ratings on the third-party entity and requires confirmation that scheduled payments to the noteholders are being made.

RATING METHODOLOGY
Further information about the DBRS rating methodology for flow-through rated securities can be found in the following publication available on the DBRS website:

North American Structured Finance Flow-Through Ratings

Asset-Backed Commercial Paper

The purpose of this section is to set forth the surveillance methodology and process DBRS follows in the ongoing surveillance of Canadian ABCP issuers. The section includes an overview of the Canadian ABCP market and a discussion of the surveillance process and key credit factors that DBRS reviews.

OVERVIEW
ABCP is an asset-backed security with a term to maturity not more than one year from the date of issuance, created to fund various types of assets. Asset-backed transactions involve the legal separation of a pool of assets and their associated cash flows and contractual rights from the entity that originates them and in all cases owns the assets prior to the transaction (the Originator). This separation comprises the transfer of assets from the Originator to a special-purpose vehicle (SPV) and the SPV’s issuance of debt to fund the purchase of the assets. In Canada, an SPV usually takes the form of a trust. An SPV that issues ABCP is referred to as an ABCP conduit. The entity that establishes and administers the conduit is commonly referred to as the conduit sponsor.

Canadian ABCP is typically backed by traditional, non-synthetic, non-levered financial assets. Traditional assets include, but are not limited to, automotive and equipment loans and leases, trade receivables, credit card receivables, HELOC receivables and commercial and residential mortgages.

Conduits may be single-seller conduits that purchase assets exclusively from one Originator, or multi-seller conduits that purchase assets from numerous Originators.

Although most transactions entered into by conduits do not carry public, explicit ratings, DBRS conducts an analysis of the credit aspects of each asset purchased by the conduit (or the conduit’s interest therein), as well as the structural features of the transaction to designate a transaction assessment level by using the DBRS long-term rating scale. In evaluating each transaction, DBRS applies its methodology for rating Canadian ABCP and the applicable asset class specific methodology.
SURVEILLANCE

DBRS ABCP ratings are monitored as long as the rated securities remain outstanding to ensure that the credit quality of the underlying transactions and related transaction structures remain commensurate with the ratings of the ABCP.

The reports provided by the conduit sponsor provide information on the various transactions in the conduit, as well as conduit-level information, including any breach of triggers at the transaction level or events of default at the series and/or conduit level. DBRS reviews this information in order to ascertain whether a rating action is appropriate. If a sponsor is unable to provide such information, or refuses to permit DBRS to disclose the information provided, DBRS may discontinue the related rating.

Key elements addressed in the conduit sponsor reports may include, but are not limited to, the following:
• A summary of the assets in the conduit.
• Each transaction’s name.
• The outstanding funded amount of each transaction.
• Relevant performance ratios for each transaction.
• Transaction-specific credit enhancement levels.
• Series-wide credit enhancement levels, if applicable.
• Program-wide credit enhancement levels, if applicable.
• The ratings of counterparties, if applicable.
• Portfolio performance as related to transaction-specific amortization triggers.
• Conduit or series level events of default.

As a general rule, during the surveillance process, each transaction is reviewed under the applicable asset-specific methodology and corresponding documentation.

Based on the information provided to DBRS in the conduit reports, DBRS publishes the Monthly Canadian ABCP Report (the ABCP Report). The ABCP Report provides market-level data for outstanding ABCP issued by all DBRS-rated Canadian ABCP conduits. In addition, the ABCP Report is summarized by the conduit sponsor and gives detailed information on the performance of each transaction in the conduit.

RATING METHODOLOGY

Further information about the DBRS rating methodology for Canadian ABCP can be found in the following publication available on the DBRS website:

Rating Canadian ABCP
Covered Bonds

OVERVIEW
Canadian covered bonds are on-balance-sheet, direct, unconditional, unsubordinated and unsecured obligations of the issuer, with additional recourse to a portfolio of specific assets (the Cover Pool) in the event the issuer defaults on its payment obligations.

SURVEILLANCE
In addition to the issuer rating, the key component of surveillance in a covered bond transaction is the Cover Pool.

Cover Pool: The quality and quantity of the assets in the pool are subject to regular review. Monthly reports are provided by the issuers, with high-level portfolio information. Each quarter, loan-level details are generally provided as per the provisions of the transaction documents for the assessment of an appropriate asset percentage commensurate with the ratings assigned.

Based on the information provided to DBRS, DBRS publishes the Monthly Canadian Covered Bond Report (the Covered Bond Report). The Covered Bond Report provides market-level data for outstanding covered bonds issued by all DBRS-rated Canadian covered bond programs. In addition, the Covered Bond Report is summarized by issuer and gives detailed information on the performance of each program.

RATING METHODOLOGY
Further information about the DBRS rating methodology for Canadian covered bonds can be found in the following publication available on the DBRS website:

Rating Canadian Covered Bonds