Methodology

General Corporate Methodology

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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.
# General Corporate Methodology

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Introduction to DBRS Methodologies

- DBRS publishes rating methodologies to give issuers and investors insight into the rationale behind DBRS's rating opinions.
- In general terms, DBRS ratings are opinions that reflect the creditworthiness of an issuer, a security or an obligation. DBRS ratings assess an issuer’s ability to make timely payments on outstanding obligations (whether principal, interest, preferred share dividends or distributions) with respect to the terms of an obligation. In some cases (e.g., non-investment grade corporate issuers), DBRS ratings may also address recovery prospects for a specific instrument given the assumption of an issuer default.
- DBRS rating methodologies include consideration of historical and expected business and financial risk factors as well as industry-specific issues, regional nuances and other subjective factors and intangible considerations. Our approach incorporates a combination of both quantitative and qualitative factors.
- The considerations outlined in DBRS methodologies are not exhaustive and the relative importance of any specific consideration can vary by issuer. In certain cases, a major strength can compensate for a weakness and, conversely, a single weakness can override major strengths of the issuer in other areas. DBRS may use, and appropriately weight, several methodologies when rating issuers that are involved in multiple business lines.
- DBRS operates with a stable rating philosophy; in other words, DBRS strives to factor the impact of a cyclical economic environment into its ratings wherever possible, which minimizes rating changes due to economic cycles. Rating revisions do occur, however, when more structural changes, either positive or negative, have occurred, or appear likely to occur in the near future.
- DBRS also publishes criteria which are an important part of the rating process. Criteria typically cover areas that apply to more than one industry. Both methodologies and criteria are publicly available on the DBRS website and many criteria are listed below under “Rating the Specific Instrument.”

Important Note

Please check the DBRS press release or rating report for the credit being reviewed to ensure that this methodology has been identified. Unless there is specific reference to it, this methodology is not part of the approach used by DBRS (and there will be another primary methodology referenced).

Application

DBRS has a wide range of corporate methodologies that provide insight into its approach and opinions for rating entities within specific industries. However, despite this wide coverage, there are a limited number of occasions where DBRS encounters unique credits that do not fit well within any published methodology, and for a variety of possible reasons, DBRS has chosen not to develop a typical methodology-based approach for the specific credit in question. In these cases, DBRS provides this General Corporate Methodology as a common starting point for the relevant methodology-based approach, noting that it should be used in combination with additional guidance in the related rating report or press release and/or the attached appendix, with respect to the individual corporate credit in question.
Overview of the DBRS Rating Process

- There are generally three components to the DBRS corporate rating process: (1) an industry risk rating (IRR); (2) an issuer rating; and (3) considerations for specific securities. The figure below outlines this process.
- An IRR is a relative ranking of most industries that have a DBRS methodology, typically using just three ranges of the DBRS long-term debt rating scale (i.e., “A,” BBB and BB), without making use of the “high” or “low” descriptors. The IRR is a general indication of credit risk in an industry and considers, among other things, an industry’s: (1) profitability and cash flow; (2) competitive landscape; (3) stability; (4) regulation; and (5) other factors. An “industry,” for the purposes of the IRR, is defined as those firms that are generally the larger, more established firms within the countries where the majority of DBRS’s rated issuers are based; this remains true for DBRS methodologies that are more global in nature. The IRR helps DBRS set the business risk rating (BRR) grid (see below) in that it positions, in an approximate way, an average firm in the industry onto the BRR grid. For firms in industries with low IRRs, the IRR can, in effect, act as a constraint or “cap” on the issuer’s rating.
- The issuer rating is DBRS’s assessment of the probability of default of a specific issuer. It is a function of: (1) the BRR, determined by assessing each of the primary and (where relevant) additional BRR factors in the BRR grid for a specific issuer; and (2) the financial risk rating (FRR), determined by assessing each of the primary and (where relevant) additional FRR metrics. The two components, BRR and FRR, are combined to determine the issuer rating; in most cases, the BRR will have greater weight than the FRR in determining the issuer rating. Throughout the BRR and FRR determination process, DBRS performs a consistency check of the issuer on these factors against the issuer’s peers in the same industry.
- The issuer rating is then used as a basis for specific instrument ratings. DBRS assigns, for example, a recovery rating and notches up or down from the issuer rating to determine a specific instrument rating for instruments of non-investment grade corporate issuers. (See “Rating the Specific Instrument and Other Criteria” below.)
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INDUSTRY RISK RATING
• While the DBRS report on the credit being reviewed is not likely to specifically mention an IRR, DBRS does consider the industry in its credit specific methodologies attached in the appendix hereto.

PRIMARY BRR FACTORS
• DBRS typically identifies three to five primary BRR factors which drive the determination of a BRR. For purposes of the appendix to this methodology, the most important of these BRR factors will be cited with a discussion of how they relate to the specific issuer in question.

Sovereign Risk
• The issuer rating may, in some cases, be constrained by the credit risk of the sovereign; in other words, the rating of the country in which the issuer operates generally sets a maximum rating for the issuer. If the issuer operates in multiple countries and a material amount of its business is conducted in a lower-rated country, DBRS may reflect this risk by downwardly adjusting its issuer rating.

Corporate Governance
• Please refer to DBRS Criteria: Evaluating Corporate Governance for further information on how DBRS evaluates corporate governance and management.

PRIMARY FRR METRICS
• In its credit-specific methodologies, DBRS typically identifies not more than one or two primary FRR metrics which drive the determination of an FRR. Many of the following points apply only for those credit-specific methodologies where specific FRR metrics are identified.
• DBRS ratings are primarily based on future performance expectations, so while past metrics are important, any final rating will incorporate DBRS's opinion on future metrics, a subjective but critical consideration.
• It is not unusual for a company’s metrics to move in and out of any ranges noted for an FRR at a given rating level, particularly for cyclical industries. In the application of this matrix, DBRS looks beyond the point-in-time ratio.
• Financial metrics depend on accounting data whose governing principles vary by jurisdiction and, in some cases, industry. DBRS may adjust financial statements to permit comparisons with issuers using different accounting principles.
• Please refer to DBRS Criteria: Financial Ratios and Accounting Treatments – Non Financial Companies for definitions of, and common adjustments to, various financial ratios that DBRS may use from time to time.
• Liquidity can be a material risk factor, especially for lower-rated non-investment grade issuers. DBRS will consider available sources of liquidity including cash on hand, cash flow, access to bank lines, etc., as well as uses of liquidity such as operations, capital expenditures, share buybacks and dividends for every issuer.
• While market pricing information (such as market capitalization or credit spreads) may on occasion be of interest to DBRS, particularly where it suggests that an issuer may have difficulty in raising capital, this information does not usually play a material role in DBRS’s more fundamental approach to assessing credit risk.
• Profitability, particularly in the medium term, can be an important differentiator of credit risk. DBRS may assess profitability through a variety of metrics, including return on capital.
• While free cash flow (i.e., net of changes in working capital, dividends and capital expenditures, etc.) can be volatile and, on occasion, negative, DBRS may use this and/or other cash flow metrics to assess a company’s ability to generate cash to repay debt.
Blending the BRR and FRR into an Issuer Rating

• The final issuer rating is a blend of the BRR and FRR. In most cases, the BRR will have greater weight than the FRR in determining the issuer rating.
• At the low end of the rating scale, however, particularly in the B range and below, the FRR and liquidity factors play a much larger role and the BRR would therefore receive a lower weighting than it would at higher rating levels.

Rating the Specific Instrument and Other Criteria

• For non-investment grade corporate issuers, DBRS assigns a recovery rating and reflects the seniority and the expected recovery of a specific instrument, under an assumed event of default scenario, by notching up or down from the issuer rating in accordance with the principles outlined in the criteria DBRS Recovery Ratings for Non-Investment Grade Corporate Issuers.
• Preferred share and hybrid considerations are discussed under Preferred Share and Hybrid Criteria for Corporate Issuers.
• The issuer rating (which is an indicator of the probability of default of an issuer’s debt) is the basis for rating specific instruments of an issuer, where applicable. DBRS uses a hierarchy in rating long-term debt that affects issuers that have classes of debt that do not rank equally. In most cases, lower-ranking classes would receive a lower DBRS rating. For more detail on this subject, please refer to the general rating information contained in the DBRS rating policy Underlying Principles.
• For a discussion on the relationship between short- and long-term ratings and more detail on liquidity factors, please refer to the DBRS policy Short-Term and Long-Term Rating Relationships and the criteria Commercial Paper Liquidity Support Criteria for Corporate Non-Bank Issuers.
• The existence of holding companies can have a meaningful impact on individual security ratings. For more detail on this subject, please refer to the criteria Rating Holding Companies and Their Subsidiaries.
• Guarantees and other types of support are discussed in Guarantees and Other Forms of Explicit Support.
• For further information on how DBRS evaluates corporate governance, please refer to DBRS Criteria: Evaluating Corporate Governance.
• Please refer to DBRS Criteria: Financial Ratios and Accounting Treatments – Non Financial Companies for definitions of, and common adjustments to, these ratios.
Appendix – Credit Specific Considerations

CANPOTEX LIMITED

Canpotex Limited (Canpotex) is a Saskatchewan-based, Canadian corporation owned by the three major international fertilizer producers that have potash production operations in Saskatchewan: Agrium Inc., Mosaic Canada Crop Nutrition, LP (a wholly-owned subsidiary of The Mosaic Company) and Potash Corporation of Saskatchewan Inc. Canpotex is a marketing and logistics company with exclusive rights for the purchase, sale and distribution of all potash produced by its three shareholders in Saskatchewan that is to be sold to markets outside of Canada and the United States. Canpotex is one of the largest potash marketing and logistics organizations in the world. It has long-term access to key shipping and infrastructure assets, including rail, port facilities and ocean shipping assets.

Canpotex borrows under its own authority. While there are certain support arrangements documented in the shareholder agreement, including an indemnity of its shareholders to pay – on a several basis – any expenses that Canpotex cannot pay, Canpotex debt is not directly guaranteed by any of its shareholders. Canpotex benefits from a flow-through of all cash flow arising from export sales of potash purchased from its shareholders such that Canpotex’s operating expenses (including debt and interest expense) are paid by Canpotex before any funds are paid to its shareholders for the potash purchased from them. Canpotex is fully reliant on its shareholders for its existence, business purpose and supply of potash, but the linkage to the ratings of its individual shareholders is not direct, given that the shareholders’ ratings incorporate factors that are not particularly relevant to Canpotex, including their respective non-potash operations and certain financial metrics.

The primary factors used to determine Canpotex’s rating are outlined below.

Export Sales of Potash from Saskatchewan Producers

This factor considers the general risks in potash mining as well as a fundamental analysis of potash sales on the international market, including potash production risks, potash price volatility, competitive actions by foreign competitors and other related risks and vulnerabilities. It also considers the importance of Canpotex’s export sales of Saskatchewan potash to the province of Saskatchewan.

To a large degree, the issuer debt ratings of the three shareholders incorporate these factors as well, although the debt ratings of shareholders also reflect other factors that may have only indirect relevance to Canpotex (such as the financial leverage of each shareholder) and still others that have even less relevance (such as non-potash operations).

Shareholder Contractual Arrangement

Canpotex’s shareholder agreement outlines a number of important terms, including Canpotex’s exclusive right to market and distribute its shareholders’ Saskatchewan-produced potash to customers outside Canada and the United States, and the right to deduct all expenses (including debt and interest expenses) incurred from potash sale proceeds before remitting the net revenue to its shareholders. This essentially puts Canpotex’s costs (including debt and interest expense) in priority over production costs of the shareholders. In addition, while not explicitly guaranteeing Canpotex’s debt, each shareholder severally indemnifies Canpotex for all approved expenses and its proportionate share of debt. These indemnities continue to attach to a shareholder even if the shareholder withdraws from the shareholder agreement (which can be done on any December 31 with six months’ notice). The legal obligations of each shareholder are clearly highly beneficial to Canpotex. In addition, Canpotex can survive the bankruptcy (and possibly even the liquidation) of one or more shareholders, such that Canpotex’s rating could generally be expected to be higher than those of its shareholders given its first-taker status in revenues from potash sales.
**Economic Value (Importance) of Canpotex Services**

As noted above, shareholders can exit from the contractual shareholder arrangement, although certain indemnities continue until requirements are satisfied. It is useful to consider, therefore, the economic value that Canpotex provides to its shareholders as this will have a direct bearing on their long-term commitment to giving Canpotex continued exclusive rights over export sales. It would be very expensive to develop alternatives to Canpotex’s existing capacity. Export sales are a large component of each shareholder’s potash sales and export potash sales are the only segment with significant growth potential. Each shareholder is already in the process of expanding its Saskatchewan production capacity. The benefits from economies of scale, the need to find outlets for expanding potash production capacity and Canpotex’s control of critical potash-related export infrastructure (particularly port capacity) all provide strong economic incentives for shareholders to stay with the arrangement.

**Government and Regulatory Factors**

Potash production is an important component of the GDP of Saskatchewan and international sales are an important growth market. Government regulation may have an impact on Canpotex’s operations domestically and through international trade laws.

**Financial Metrics**

Canpotex’s shareholders’ arrangement is clearly an integral part of the credit strength of the company. Canpotex has unconventional financial statements (e.g., there is nominal equity and Canpotex generates no net income) that are a function of the shareholders’ arrangement. Normal DBRS credit metrics may not fully reflect the creditworthiness of the company. As such, financial metrics on their own contribute a lower weighting to the overall rating in comparison with more typical corporations.
LEISUREWORLD SENIOR CARE LP
Long-term care (LTC) providers, including Leisureworld Senior Care LP (Leisureworld), are an extension of the provincial healthcare system and fulfill an important mandate. As independent private-sector operators, however, they are not viewed by DBRS as being as essential and as closely tied to provincial governments as public hospitals. Entities active in the LTC sector generally benefit from the stability of provincial funding and demand for services, but they also face extensive operating requirements and constrained revenue generating capability. They are also influenced by several other factors.

DBRS’s rating on Leisureworld is based primarily on the following:
• **Highly regulated industry with significant barriers to entry.** Under the *Long-Term Care Act*, providers must be granted a licence to operate an LTC facility in Ontario, with terms of 15 to 25 years depending on the class of the facility. Any new licence issued by the government represents a significant funding commitment due to the capital funding stream provided with every licence. This has historically greatly limited the provision of licences and the supply of LTC beds in Ontario, ensuring high average occupancy in the sector.
• **Stable and predictable government funding.** Because it is part of the broader health care sector, which is a top priority of provincial governments, and due to the significant cost advantage it provides relative to hospitals, the LTC sector has historically benefited from very stable funding support from provincial governments, even at times when other programs were subject to cuts.
• **Strong demand outlook due to aging population.** Demographic projections from Statistics Canada indicate that 12% of the population will be of age 75 and older by 2036, compared with fewer than 7% in 2011. Over the same time period, persons aged 85 and up are forecast to grow to 3.6% of the population compared with 1.9% in 2011. The current waitlist for LTC beds of approximately 24,000 further highlights the strong demand profile for the sector.
• **Government construction funding covering a significant portion of debt servicing.** Every licence awarded in Ontario comes with a 20-year capital grant meant to support the repayment of construction costs (approximately $75,000 per bed). The funding is not dependent on occupancy and accounts for a significant portion of Leisureworld’s debt servicing requirements.
• **Limited ability to grow revenue.** Ontario LTC providers receive the majority of their revenues through funding envelopes. Provincial funding is provided for nursing and personal care (NPC), programs and support services (PSS) and raw food. Any unspent funds in the NPC, PSS and raw food envelopes must be returned to the Province of Ontario (the Province), which only leaves the accommodation per diem and preferred room premiums (about 30% of Leisureworld’s revenues), both regulated by the Province, as the only source for the operator to retain a profit. However, co-payments are paid by the government if a resident is unable to pay, which greatly limits collection risk.
• **Regulatory and funding policy risk.** LTC providers in Ontario operate under licences from the Ministry of Health and Long-Term Care and are subject to significant service delivery requirements, limiting operational flexibility. The high level of monitoring and control exerted by the government ensures high operating standards and leads to the quick resolution of compliance issues. However, failure to meet standards can have negative implications if not promptly rectified, such as increased monitoring, suspension of admissions and, ultimately, revocation of a licence.
• **Debt affordability.** The high barriers to entry, strong demand for services and low credit risk of major funding sources generally result in very stable cash flows for competent Ontario LTC providers, allowing for the accumulation of relatively heavier debt burdens, a situation akin to infrastructure credits. Nonetheless, the key debt metrics (debt service coverage and debt-to-EBITDA ratios) of an LTC provider are still expected by DBRS to point to a sustainable debt load. In the case of Leisureworld, the Master Trust Indenture also includes covenants that are common for infrastructure credits, including limits on additional indebtedness, permitted distributions and allowable activities.
• **Management proficiency.** Given the highly regulated nature of the sector, it is essential that LTC providers have a highly qualified, efficient and diligent management team in order to meet operating targets and the requirements under the service agreements with the Ministry of Health and Long-Term Care. A weak or aggressive management team can adversely affect operating performance and/or result in excessive leverage.
DBRS notes that the parent of Leisureworld (Leisureworld Senior Care Corporation) operates with a focus on growth across a broader spectrum of seniors living, including independent living facilities and retirement homes, which do not receive provincial funding and are subject to much more competition. As a result, these sectors have weaker credit fundamentals than LTC. However, DBRS does not incorporate these activities in its assessment of Leisureworld given the following: (1) the segregation provided by Leisureworld’s limited partnership structure and financial covenants; (2) the absence of guarantee provided by Leisureworld to its parent; and (3) the separate bank accounts maintained by Leisureworld and its subsidiaries. Furthermore, external counsel had provided a legal opinion to DBRS that in an insolvency proceeding, the assets and liabilities of Leisureworld would not be substantively consolidated with those of the non-LTC subsidiaries of its parent, which ultimately provides comfort that the acquisitions undertaken by the parent do not dilute the risk profile of Leisureworld.

Given the dependence of LTC providers on provincial funding, their credit ratings would be unlikely to match that of their government funder and deterioration in the Province’s rating could eventually have rating implications for LTC providers.
ONTARIO INFRASTRUCTURE AND LANDS CORPORATION (OILC)

Ontario Infrastructure and Lands Corporation (OILC) is a non-share capital corporation 100% owned by the Province. The operations of Infrastructure Ontario (IO) consist of three primary activities: (1) the provision of infrastructure loans to eligible Ontario public-sector entities; (2) the management of provincial capital projects delivered using the Alternative Financing and Procurement (AFP) model; and (3) the management of the Province’s real estate portfolio. OILC is also an agent of the Crown but it does not act as a Crown agent when borrowing, nor does it benefit from a guarantee from the Province. Furthermore, although it is owned by the Province and fulfills an important mandate, OILC is not viewed by DBRS as being as essential and as closely tied to the provincial government as public hospitals, for example.

As a result, the entity is not deemed to benefit from implicit support from the Province and is rated solely on the basis of its merits, which primarily include the following:

- **Substantial reserve fund.** The reserve fund carried by the entity, which was funded with subordinated loans from the Province and the Ontario Clean Water Agency (OCWA), is mainly invested in high-quality, liquid fixed-income securities and covers a significant portion of outstanding debt.
- **High-quality loan portfolio.** OILC’s loan portfolio consists primarily of loans extended to Ontario municipalities. Internal DBRS analysis indicates that approximately 85% of municipal debt in Ontario is serviced by entities rated AA or higher or that exhibit credit characteristics consistent with that of AA-range ratings. Borrowers with credit fundamentals that are generally weaker than municipalities have been added to the loan portfolio over the years but IO has introduced tighter credit and risk management policies to strengthen its lending standards.
- **Access to provincial grant interception mechanism.** A provision is embedded in almost all loan agreements between OILC and provincially funded borrowers that entitles the Minister of Finance to intercept, on OILC’s behalf, funding paid by the Province to any delinquent borrower in OILC’s loan portfolio. While this clause does not materially change the underlying credit quality of borrowers, it provides additional incentives to borrowers to service the unsecured loans. As such, this provision is not viewed as beneficial for loss recovery purposes.
- **Provincial policy risk.** OILC is subject to government policy and its financial integrity could be adversely affected by political intervention or policy changes, such as the loosening of loan eligibility criteria, changes to legislated powers (for example, the loan intercept mechanism) or pressure to further expand lending activities into sectors with weaker credit fundamentals.
- **Potential asset and liability mismatches.** Although OILC makes an effort to minimize asset-liability mismatches, disparities are likely to continue to exist between the time to maturity of its assets and liabilities, creating interest-rate risk. OILC attempts to match terms as closely as possible and has an agreement in place with the Ontario Financing Authority (OFA) to manage its investment portfolio and help reduce its exposure to interest-rate risk through various hedging strategies, including the use of swaps.

Factors such as management quality and the set of policies and procedures guiding the origination and management of the loans are also considered in the analysis. In particular, a certain level of discipline and diligence is expected to be exercised when reviewing loan applications. Given the mandate and nature of the agency, however, lending criteria are not designed to exclude applicants with weak credit profiles or achieve a certain return or credit quality target, unlike those of financial institutions. Instead, OILC generally seeks to adjust the scope of the project of an applicant to stay within established lending policy thresholds.

The agency operates in several business lines, but most of the rating process focuses on lending activities as they are the driver of borrowing needs and the other businesses are conducted on behalf of the Province on a cost recovery basis. Therefore, the credit quality of OILC is primarily dependent on that of its loan portfolio and on the adequacy of its reserve fund, which is an integral part of the credit and can be viewed as credit enhancement for the portfolio.
Reserves Relative to Loan Portfolio Expected Losses

While not the only determinant of the rating, DBRS will use its collateral debt obligation methodology (i.e., the CDO Toolbox, publicly available on DBRS's website) to determine the rating that current OILC reserves can support. This is done in the following manner.

DBRS first evaluates the credit quality of the underlying pool of loans by scoring each individual obligor in one of four risk buckets (AA (low), “A”-range, BBB-range, BB-range) based on public ratings assigned by DBRS or established competitors or, in the case of unrated obligors, on a simplified application of the relevant DBRS rating methodology. These internal assessments do not encompass the full amount of work and research that would be incorporated into a definitive rating. For example, there is no contact with the management of individual obligors. For the odd sector for which there is no DBRS rating methodology (e.g., hospices) or for which historical operating and financial data may not be available, the respective loans are prudently allocated to the highest risk bucket established for the loan universe. The risk buckets become, in effect, proxies for ratings of each individual loan.

DBRS then determines the portfolio’s required collateral (as a percentage of loans outstanding) at various rating levels using the CDO Toolbox as well as certain assumptions pertaining to loan diversification, correlation across sectors and credits, expected rating transitions and the term to maturity of underlying loans. The various required collateral levels suggested by the CDO Toolbox are then compared to current reserves to help determine the rating viewed by DBRS as sustainable for OILC over the long term.

In the early years of OILC’s operations, reserve levels were larger than even outstanding loans, let alone reserve levels required to support a AAA rating using the CDO Toolbox. However, the initial rating of AA was assigned (and continues to this day), notwithstanding a reserve amount well in excess of AA reserve requirements, because DBRS believes that such reserve levels relative to AAA requirements are unsustainable in the long run given OILC’s growth and reserve projections as well as the nature of its lending activities.

This approach allows DBRS to track the evolution of the portfolio along with the adequacy of the reserve and eventually voice concerns if, due to growth in outstanding loans and/or erosion in the portfolio’s credit quality, reserve requirements, as suggested by the CDO model, approach actual reserve levels.

Given the high level of reserves maintained by OILC and the steady stream of loan repayments received from borrowers, liquidity is generally not a concern. Nevertheless, DBRS expects reserves to be invested in high-quality assets, which according to OILC’s internal policy for reserve fund assets, shall include long-term debt of Canadian federal, provincial and municipal governments, sovereigns and supranationals, and Schedule I Canadian Banks, along with investments in short-term high-quality corporate issuances. Furthermore, because OILC funds part of its lending operations with commercial paper (CP), DBRS will generally require OILC to constrain its issuance of CP so that reserves are sufficient to cover at least 1.5 times the amount of CP outstanding. This credit-specific requirement is in replacement for the dedicated back-up line of credit generally required from corporate CP issuers. DBRS will tolerate a program limit in excess of the steady-state level of issuance permitted by the reserves provided the excess room is maintained in the program for contingent purposes only.

OILC’s rating is not capped at the level of the Province’s rating and can exceed that of its parent. Given the strong link between OILC and the Province, however, deterioration in the Province’s rating would eventually have rating implications for OILC.
ONTARIO SCHOOL BOARDS FINANCING CORPORATION (OSBFC)

Ontario School Boards Financing Corporation (OSBFC) is a not-for-profit, non-share capital corporation created to facilitate access to the capital markets for Ontario school boards. OSBFC historically purchased debt issued by one or more participating school boards and in turn sold undivided co-ownership interests in these debts to investors in the form of OSBFC debt series. The last issue of OSBFC occurred in 2007. Since then, school boards' capital-related debt needs have been addressed by the Province.

The underlying debenture of each participating school board ranks pari passu with all other debentures and financial instruments issued by that board. However, there is no joint and several liability among school boards participating in a specific OSBFC debt issue. Furthermore, OSBFC and the participating school boards do not act as a Crown agent of the Province when borrowing, nor do they benefit from a guarantee from the Province.

In DBRS’s view, however, several factors support the credit profile of OSBFC and contribute to linking it very closely to that of the Province, including primarily the following:

- Provincial funding accounts for nearly three quarters of total school board funding in Ontario, and education has been a top priority of provincial governments, constituting by far the second-largest program after health care. There is also broad political consensus around the importance of government funding for education among the population, with voters voicing their desire that spending levels be maintained. This gives the Province a strong incentive to ensure the sector remains adequately funded and has historically translated into steady and predictable provincial funding, even in regions where enrolment has been declining.
- The Province closely monitors the financial condition of school boards and has demonstrated its willingness to appoint supervisors for poorly performing school boards, which fosters discipline and allows for early resolution of financial problems. The framework is regularly reviewed and enhanced. School boards must submit financial forecasts to the Province when requesting approval to proceed on a project. Provincial surveillance is complemented by legislation requiring school boards to have balanced operating budgets and to seek provincial approval for capital projects.
- All funds used by school boards to service OSBFC debt series originate from the Province in the form of capital grants. Thanks to the capital funding wrap-up initiated by the Province in fiscal year 2010-11, much of the enrolment-sensitive capital funding formerly used to service the majority of OSBFC debt series has been replaced with unconditional capital grants, with the exception of renewal grants which remain enrolment-based. As such, the Province effectively retains most of the enrolment risk pertaining to OSBFC debt servicing and generally finances the bulk of OSBFC debt servicing requirements on an unconditional basis.

Due to the importance of the Province and its funding to the system, it is inconceivable that the rating on OSBFC debt series could exceed that of the Province.

However, the rating on one or more specific OSBFC series could be lower than that of the Province should, for example, one of the participating school boards demonstrate excessive financial stress with no credible plan to overcome the problems or an adverse unexpected development in the sector lead DBRS to question the commitment of the Province to the sector or the tightness of the provincial monitoring framework. While in such a situation a one-notch downgrade would be the most likely outcome, a multi-notch differential could develop if, for example, the financial erosion experienced by one or several participating school boards was deemed considerable.
TMX GROUP LIMITED

TMX Group Limited (TMX) operates markets and clearing houses in Canada for equities, fixed income, derivatives and energy. TMX provides services encompassing listings for issuers, trading, clearing, settlement and depository facilities, data delivery solutions and products, as well as technology services for the international financial community. TMX is not making markets or taking proprietary positions within the markets it shepherds.

The primary subsidiaries of TMX include the Canadian Depository for Securities Ltd. (CDS), Alpha Trading Systems L.P. and TMX Group Inc., which in turn owns/runs Natural Gas Exchange Inc., the Montreal Exchange and the Toronto Stock Exchange (among others). CDS is the sole provider of equity and fixed-income clearing, while TMX’s four exchanges have a combined market share of 83% (Q1 2013).

The primary factors used to determine TMX’s rating are outlined below.

Franchise Strength
Franchise strength refers to the company’s ability to generate earnings to withstand adverse events. Market share and product diversification, components of franchise strength, are affected by competition and technological innovation, but also the interconnectedness of the products and businesses. Furthermore, if the businesses are highly important to the financial system, systemic support would more likely be forthcoming, which would be viewed favourably for the rating.

In Canada, TMX is easily the preeminent player in these markets, with significant market share across a breadth of products. In the issuer services business, TMX has over 3,700 issuers combined between the Toronto Stock Exchange and the TSX Venture Exchange, whereas the one other recognized alternative exchange has fewer than 200 listed securities. For equity trading, there are several alternative platforms competing with TMX’s four exchanges, which combined have an 83% market share as at Q1 2013. TMX does compete with over-the-counter alternatives for derivatives trading and energy trading, but is the sole provider in derivatives clearing and energy clearing services. CDS is the sole provider of equity and fixed-income clearing in Canada. To maintain market leadership, TMX is heavily dependent on leading technology. Barriers to entry include the need to develop scale, which creates efficiencies to ward off price-based competition, but, more importantly, trade execution. Diversification of products and revenues, cross-selling opportunities and even the ability for the TSX Venture Exchange to act as an incubator for future Toronto Stock Exchange listings can benefit the rating relative to other organizations that don’t have the same breadth or depth of offerings.

CDS is currently the sole provider of a number of clearing and settlement services, and the Toronto Stock Exchange is the largest and clearly most visible stock exchange. These factors ensure regulatory attention and the potential for Canadian government support, if necessary, at the operating company levels (exchanges and clearing house). DBRS considers this possibility, while recognizing that, absent a guarantee from its subsidiaries, TMX may not be the direct receiver of this support.

Risk Management and Governance
Risk management and board governance are factors generally expected to be very strong for a company that assesses listing companies. Operational risk and reputational issues are critical for exchanges and clearing houses. A failure of systems, errors in processing or slow trade matching can damage the company’s reputation. The plethora of controls, collateral agreements, margin arrangements, delivery versus payment processes, risk sharing of members, the ability to assess members to cover losses and legal priority positioning, etc., are all important factors in assessing the riskiness of the organization and the rating. Consequently, DBRS considers the apparent effectiveness of such controls, rules, conservativeness of margin requirements and the ability of the operations to make margin calls in a time of crisis in its assessment.
Management and board governance are factors generally expected to be very strong for TMX, which, as a neo-regulator itself, generally sets a good example for the best practices that the TMX’s exchanges suggest for their listing clients.

Despite the complexities of the businesses, TMX appears to be successfully managing operational risk, as losses have not been notable. TMX businesses are not intended to take direct market risk. Any direct capital market exposure would likely be considered by DBRS to be a departure from TMX’s fundamental principles, which would be negative for the rating. Operating under Canadian law, relative to other jurisdictions, is a positive factor when closer scrutiny of legal agreements would be needed.

**Structure**

The ownership structure can have an impact on the strategies, operations and governance of the company, as well as providing support. Listed companies benefit from enhanced disclosure and oversight. A parent company with strong or weaker ratings could also have an impact on ratings. How debt at the holding company is transferred to its subsidiaries, either as debt or as an equity injection, can influence ratings because regulated operating subsidiaries would be susceptible to government or regulatory controls, which can include limitations on the issuance of dividends.

TMX is a public company, with significant ownership by a group of 11 notable players in the Canadian investment industry. Nine of the 11 have ratings from DBRS (or their parent companies do), three of which are AAA, four AA and two AA (low) as of March 2013. The group of investors originally gathered in order to keep the four Canadian exchanges controlled in Canada, as many of TMX’s businesses are highly important to the Canadian financial system. The owners collectively constitute a sizable percentage of TMX’s customer base.

The operating subsidiaries of TMX have no externally issued debt (other than operating/clearing lines). This absence of debt at the operating subsidiaries allows DBRS’s analysis to generally be done on a consolidated basis with a view to examining the strength of the overall organization. DBRS will continue to assess where TMX’s debt obligations reside. In the event that the subsidiaries begin to issue external debt, it is likely that DBRS will more explicitly incorporate use of the DBRS methodology Rating Holding Companies and Their Subsidiaries in the analysis. This has the potential to necessitate the inclusion of rating notches to recognize the structural subordination of the holding company. DBRS will assess whether any guarantees from subsidiaries justify a difference in the ratings of guaranteed versus non-guaranteed obligations issued by TMX itself.

**Regulation**

DBRS considers the strength and safety that come from regulatory oversight in the operating businesses. While potentially burdensome for the expense lines, regulation is examined as part of the rating process and generally considered a positive rating factor in financial services businesses.

TMX subsidiaries have extensive oversight by various regulators, inside and outside of Canada. This oversight provides additional scrutiny at the operating subsidiaries, which is positive for the ratings. Notwithstanding, TMX subsidiaries are also exposed to additional regulatory risk due to uncertainty surrounding regulatory requirements.

**Financial Metrics**

Profitability (as measured by return on equity), the degree of volatility in revenues and income, leverage and interest coverage are important metrics for assessing the credit risk of exchanges and clearing houses. Unlike other types of financial institutions that do assume market risk, underwriting risk or deposit obligations, liquidity is not a large factor in the rating, nor is the absolute level of total capital.
Given the acquisitions in 2012, the historical financial statements of TMX make it difficult to assess the company’s financial metrics. As such, DBRS uses pro forma financial information to assess the Company’s ability to meet its obligation. Financing has been raised for general corporate purposes and expansion/acquisitions, not to finance trading. Implied in this analysis is a view of the level of fixed costs (including maintenance capex), which can be considerable.

Exchanges and clearing houses, as a general matter, fall somewhere in the middle of the risk spectrum between a regulated utility and a non-regulated industrial company. With this in mind, DBRS has derived the key ratios in the table below, which guide the financial risk component of TMX’s rating.

<table>
<thead>
<tr>
<th>Key Ratios</th>
<th>AA</th>
<th>A</th>
<th>BBB</th>
<th>BB</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt-to-EBITDA</td>
<td>&lt; 2.5x</td>
<td>2.5x to 4.0x</td>
<td>4.0x to 6.0x</td>
<td>&gt; 6.0x</td>
</tr>
<tr>
<td>EBITDA interest coverage</td>
<td>&gt; 7.0x</td>
<td>5.0x to 7.0x</td>
<td>4.0x to 5.0x</td>
<td>&lt; 4.0x</td>
</tr>
<tr>
<td>Cash flow from operations-to-debt</td>
<td>&gt; 30%</td>
<td>20% to 30%</td>
<td>15% to 20%</td>
<td>&lt; 15%</td>
</tr>
<tr>
<td>Debt-to-capital</td>
<td>&lt; 25%</td>
<td>25% to 35%</td>
<td>35% to 45%</td>
<td>&gt; 45%</td>
</tr>
</tbody>
</table>