Article Title: ARCHIVE | Legal Criteria: Guide To Legal Issues In Rating Australian Securitization Data: (EDITOR'S NOTE: — This article is no longer current. It has been fully superseded by "Australian And New Zealand Asset Isolation And Special-Purpose Entity Criteria--Structured Finance," published Aug. 21, 2013.) Standard & Poor's Ratings Services is pleased to present this guide to legal issues in rating Australian securitization. This guide describes the key legal issues in rating securitization in Australia and explains Standard & Poor's approach to those issues. Although this guide aims to provide comprehensive coverage of a topic as dynamic as securitization, changes in markets and transaction structures will, over time, make aspects of this publication obsolete. Standard & Poor's will regularly update its criteria and commentary on market developments. Changes to Standard & Poor's criteria will be published online at www.standardandpoors.com. This guide is a tool for market participants, not an academic treatise. For that reason, it does not purport to identify and address every legal issue in Australian securitization. Rather, the focus is on legal issues that, in Standard & Poor's experience, regularly arise in practice and explaining the manner in which Standard & Poor's has applied its global criteria to those issues. This guide is divided into sections, in which we consider: The legal framework in Australia and, in particular, the insolvency regime that is a fundamental driver of our structural analysis; The concept of insolvency remoteness of special-purpose securitization vehicles; The essential tools for achieving legal separation of securitized assets from originators, either by true sale of the assets or by using a secured loan structure; The application of Standard & Poor's segregation criteria in Australia; and Specific legal criteria and issues regarding set-off, commingling, and guarantees, taxation, and legal opinions. The aim of this guide is to stimulate discussion about securitization legal criteria and the issues that drive them. As always, Standard & Poor's is ready to listen to the concerns of market participants so that it can continue to improve the securitization market in Australia. Ratings And Securitization In securitization, the ratings assigned by Standard & Poor's are issue credit ratings rather than issuer credit ratings, although there may be an analytical connection between the two. An issue credit rating is Standard & Poor's current opinion of the Standard & Poor's Structured Finance ■■Legal Criteria for Australian Structured Finance Transactions creditworthiness of an obligor regarding a financial obligation, a class of financial obligations, or a financial program (the issue). A rating is a statement of Standard & Poor's opinion of the issuer's ability to pay, in full, principal and interest on the issued financial instruments in a timely manner and in accordance with its terms. An issuer credit rating is Standard & Poor's current opinion of an obligor's overall financial capacity and willingness to meet its financial commitments as they become due. Counterparty credit ratings, corporate credit ratings, and sovereign credit ratings are all forms of issuer ratings. Securitization and structured financing transactions can be thought of as occurring along a spectrum. At one end of the spectrum, the originator of the assets is also the issuer. Its unsecured debt will be rated based on the issuer's general creditworthiness and the probability that it will default. In other words, the rating of the issue will be tied to the rating of the issuer. Further along the spectrum is the issuer's secured debt. Even further along the spectrum are transactions in which the likelihood of timely payment on the instrument has been enhanced, such as with a guarantee from a suitably rated counterparty. At the far end of the spectrum are "true" structured financings, in which the creditworthiness of the financial instruments reflects the underlying assets and is independent of the creditworthiness of the originator. True structured finance transactions seek to legally isolate the underlying assets from the insolvency of the transferor/originator, enabling purchasers of the issued instruments to consider the creditworthiness of the underlying assets when assessing the risk of their investment. The transaction structure will be designed to insulate payments on the issued financial instruments from the claims of entities, including the transferor/originator of the assets, that are either unrated or have issuer credit ratings lower than the desired credit rating on the issued instruments. Consequently, in a true structured finance transaction, the rating assigned by Standard & Poor's can reflect the creditworthiness of the underlying assets independent of the creditworthiness of the transferor/originator and other transaction participants. The closer a transaction is to the structured finance end of the spectrum, the more reliant it is on the structure of the transaction and the contractual allocation of risks and responsibilities. Accordingly, Standard & Poor's legal analysis of the transaction is more rigorous. Legal Issues: Our Approach When analyzing legal issues, Standard & Poor's closely reviews a transaction's proposed structure, documentation, underlying assets, and processes. The review process is consultative, involving discussions with transaction participants and their advisors, and is conducted in conjunction with a more general analytical review. Before assigning a rating, Standard & Poor's will consult the transaction legal advisors, seeking their opinions on various legal aspects of the transaction. During the course of the review, Standard & Poor's may also request that opinions be given about legal issues unique to the transaction. THE LEGAL FRAMEWORK IN AUSTRALIA The Commonwealth of Australia is a federation of states, with both federal and state/territory levels of government and legislation. State and federal legislation overlay common law adopted from England that has evolved locally. The common law basis of the legal system gives Australian law equitable concepts, including equitable interests and trusts, and supports the same principle-based approach to the legal analysis of securitization that occurs in other common law jurisdictions. The Commonwealth of Australia Constitution provides the Federal Parliament with various plenary powers for the peace, order, and good governance of the Commonwealth. Aspects of Commonwealth legislation do significantly affect securitization, but a large portion of the legislation relevant to securitization occurs at the state government level. Consequently, there is potential for the legal treatment of financial transactions to vary between states, particularly in the area of state revenues (for example, with stamp duty and ad valorem (according to value) taxes). On some issues, the states have adopted common legislation, such as the Uniform Consumer Credit Code, which gives some protection on borrowing or leasing for personal, domestic, or household purposes. On other issues, the states have markedly different approaches, such as in the laws governing hire-purchase agreements. Consequently, to the extent that a transaction involves assets or parties across multiple states, a state-by-state analysis of legal issues may be required for some transactions. Insolvency Regime The impact of the applicable insolvency regime(s) on a securitization structure is the central legal concern for any rating analysis. In Australia, the insolvency regime involves a mix of the Corporations Act 2001 and contract and common law. As in other common law jurisdictions, the statutory test for insolvency is primarily liquidity. An insolvent company is one that is unable to pay all of its debts as and when they become due and payable. The considerations for determining insolvency in Australia are similar to those in other common law jurisdictions and include consideration of an entity's ability to raise immediate finance by borrowing or selling assets. The usual method for establishing insolvency is an unsatisfied statutory demand made on a company. A determination of insolvency gives rise to three possible forms of administration: Voluntary administration; Liquidation; and/or Receivership. Voluntary Administration The administration regime under the Corporations Act gives a company that is insolvent or "likely to become insolvent at some future time" an opportunity to restructure and be restored to financial health. It gives some leeway in which an administrator can assess the distressed company's position and formulate a potential recovery plan to be offered to creditors. An administrator may be appointed to a company by a resolution made by the board of directors, or in writing by a liquidator or by the holder of an enforceable charge over the whole, or substantially the whole, of the company's property. Once appointed, the administrator assumes exclusive control of the company's affairs as agent of the company and has, subject to extension by application to the courts, 28 days to develop and present a deed of company arrangement to a meeting of creditors. Despite the requirement for a court application, market experience is that the administration period can be much longer than 28 days. During the administration period, the Corporations Act gives a distressed company "breathing space" by, among other things: Staying and suspending proceedings and enforcement processes against the company; Prohibiting owners and lessors of property that is used or occupied by the company from taking possession of the property or otherwise recovering it without the administrator's consent or the leave of the court; Prohibiting the transfer of shares in the company without court approval; In general, rendering void transactions with officers of the company purportedly on behalf of the company (including by receivers who are not both receivers and managers) and not by the administrator or with the administrator's consent; Prohibiting the voluntary winding-up of the company except in accordance with the administration process; and Prohibiting, generally, the exercise of charges over the property of the company without the administrator's consent or the leave of the court, unless the charge holder: has a charge or charges that, between them, are over the whole, or substantially the whole, of the company's property, and enforces the charge within 10 days of the commencement of administration. The exception to the administration regime that allows enforcement of a valid security charge over all, or substantially all, of the company's property underpins Standard & Poor's criteria requirement for recognizing security charges. To give full analytical recognition to any charge, Standard & Poor's requires that it be a valid charge over all, or substantially all, of the company's property and that it incorporates the immediate power to appoint a receiver and manager to the company. Administration has three possible outcomes: A deed of company arrangement is voted on, approved, and signed, with the company then becoming a "company under deed of arrangement". After signing, the company's creditors are bound by the deed of arrangement; The company's creditors resolve that the administration should end; or The company's creditors resolve that the company be wound up. Receivership In Australia, a receiver's rights and obligations are much the same as in other common law jurisdictions, and are the product of statute, contract, and common laws. As previously described, an administrator's functions and powers will be subject to the functions and powers of a receiver appointed under powers contained in a security charge over all, or substantially all, of the company's property that has been enforced within 10 days of the commencement of administration. Similarly, a receiver or a chargeholder exercising a power of sale can deal with the charged property outside of the liquidation process. Winding-up Winding-up is a statutorily defined process for liquidating a company's assets in an orderly manner and passing the proceeds to its creditors. The process of liquidation is similar to other common law jurisdictions and typically results in the fully liquidated company being removed from the company register. Winding-up may occur as a result of court order following insolvency, or as a voluntary process brought about by a special resolution of the members of the company. INSOLVENCY REMOTENESS: SPECIAL-PURPOSE ENTITIES To achieve "insolvency remoteness" of underlying assets from their originator, and for issued instruments to have the potential to be rated higher than the originator, the benefit of the underlying assets must be transferred to a securitization entity—a special-purpose entity (SPE)—in a manner that creates complete legal independence from the originator. Insolvency remoteness then allows credit analysis to focus on the credit quality of the underlying assets independent of the commercial viability of the originating transferor or the potential claims of any of its creditors. Standard & Poor's criteria for SPEs are globally consistent, although their application can vary in detail between jurisdictions. The Australian SPE criteria should be used for assessing companies and other entities that, upon insolvency or bankruptcy, would be subject to Australian insolvency or bankruptcy laws. Typically, such entities are companies incorporated in Australia and other entities that are resident in Australia. Types of entities that may satisfy the Australian SPE criteria include: Orphan companies; Subsidiary companies (in limited circumstances); and Trusts. The SPE criteria emphasize minimization of the risk of voluntary or involuntary insolvency or bankruptcy of the SPE—the state that is referred to as being insolvency remote or bankruptcy remote. To assess insolvency remoteness, Standard & Poor's criteria involve a consideration of: Contractual restrictions; Debt limitations; Prohibition of mergers, reorganizations, and changes in ownership; Separateness covenants; Fixed and floating security over assets; and Independence of directors. Each of these characteristics is important to the overall determination of an entity's insolvency remoteness, and each is examined in more detail below. Insolvency remoteness is not a perfect state because, in the absence of legislative intervention, no securitization is insolvency proof. Insolvency remoteness is more a matter of degree. If an entity is insufficiently insolvency remote from the originator, or from a parent entity that exerts control over it, any rating assigned may be limited by the lowest rated or unrated entity on which the SPE is dependent. Such dependency is often referred to as "weak linking". Typically, Standard & Poor's will require that elements of the SPE criteria be substantiated through legal opinions for each transaction. SPE Criteria Contractual Restrictions on Activities The fundamental characteristic of a special-purpose entity is that it is restricted as much as possible to only the activities necessary to perform the transaction. Activity restrictions are designed to reduce the risk that an SPE may become insolvent from claims unrelated to the securitized assets or the issuance of the rated securities. In other words, the SPE should not, and should not be permitted to, engage in business activities that do not relate to the underlying assets unless the parties to the transaction are willing to allow the rating on the issued instruments to reflect the potential effect of those unrelated activities on the entity's ability to meet its rated obligations. Consequently, an SPE should not engage in any business or activity other than what is necessary for, or incidental to, its role in the transaction. An SPE's activities may be restricted constitutionally, through its constitution and permitted objectives and powers, or contractually, through the transaction documents (in particular, by the security documents). Globally, Standard & Poor's has indicated its preference that constraints on the activities of SPEs are contained in the SPE organizational documents. In Australia, however, Standard & Poor's recognizes that there is a higher risk that the doctrine of ultra vires (beyond powers) may operate to limit an SPE's activities further than intended, and potentially below what is necessary to perform a transaction. Consequently, for Australian SPEs, Standard & Poor's considers that, on balance, it is preferable that restrictions on activities are contained in transaction documents. Debt Limitations An SPE should be restricted from incurring additional indebtedness, whether monetary or nonmonetary, if that indebtedness could affect the rating on the existing issued securities. An existing rating will be affected if the holders of additional indebtedness have an incentive to initiate insolvency proceedings to gain access to the SPE's assets and cash flows. That incentive may be reduced to the extent that the additional debt is subordinated to the issued debt, has the same rating as the issued debt, or is segregated from the issued debt. In considering debt limitations, Standard & Poor's expects that: The SPE would be prohibited from incurring additional indebtedness, monetary or otherwise, that does not secure the rated securities, unless the additional indebtedness is nonrecourse to the entity and assets that are available and required to pay holders of existing rated securities and does not constitute a claim against the entity to the extent that the entity does not have sufficient funds available to repay the additional indebtedness; and it either bears the same rating by Standard & Poor's as the rating assigned to the existing debt, is fully subordinated to the existing rated securities, is issued as a series that meets Standard & Poor's segregation criteria; Every agreement between the SPE and a creditor should include nonpetition language in which the creditor agrees not to initiate insolvency proceedings against the SPE and not to join any such proceedings; and Fees, expenses, indemnities, and other performance obligations of the SPE incurred directly in connection with the underlying assets and the issue of the rated financial instruments should be capped or subordinated to payments on those instruments. Alternatively, when analyzing the cash flow in the transaction, Standard & Poor's will size for those amounts. No Reorganization, Merger, or Change of Ownership The prohibition of reorganizations, mergers, and changes of ownership is meant to give comfort that, for as long as the rated securities are outstanding, the insolvency-remote nature of an SPE will not be undermined by the purchase of shares in the SPE or any reorganization, dissolution, merger, amalgamation, reconstruction, liquidation, or asset sale involving the SPE. As long as rated securities are outstanding, an SPE entity should not, without prior written notice to Standard & Poor's, engage in any dissolution, liquidation, consolidation, merger, or asset sale (other than as provided in the rated transaction documents), or the amendment of its organizational documents. Separateness Covenants Separateness covenants are designed to ensure that each SPE conducts its activities as an independent entity—independent of its parent, the originator, and all other transaction participants—thereby minimizing the risk that the courts may "pierce the corporate veil" of the SPE. Piercing the corporate veil is a judicial discretion in which the separate identity of an entity (as discrete from its controlling entity) is disregarded. The effect is that their enterprises are seen as effectively commingled. If the courts pierce the corporate veil of an SPE, they may include the SPE and its assets in the insolvency or liquidation of the overreaching entity. To minimize the risk of a parent or originator overreaching into the SPE, the SPE should agree to abide by the following separateness covenants: To maintain books and records separate from any other person or entity; To maintain accounts separate from any other person or entity; Not to commingle its assets with those of any other person or entity; To conduct its own business in its own name; To maintain separate financial statements; To observe all corporate formalities; To use separate stationery, invoices, and cheques; and To hold itself out as a separate entity and to correct any known misunderstanding regarding its separate identity. If there is any doubt regarding the degree of separation of the SPE from its parent or the originator, Standard & Poor's may call for a legal opinion confirming that there are no grounds for piercing the corporate veil and that neither the SPE nor its assets and liabilities may be substantively consolidated or otherwise available in any winding-up or liquidation of the originator or parent. Charge An appropriately structured charge over all of an SPE's assets granted in favor of the holders of the rated securities reduces the practical benefits and, therefore, the incentives, of insolvency proceedings being filed against an SPE by any equityholder or unsecured third-party creditor. It also enables the securityholders to obtain effective control of an SPE's assets despite the appointment of an administrator. This general rationale for requiring a charge is separate from the criteria regarding independence of directors. Independence of Directors The inclusion of an independent director on the board of an SPE gives some comfort that the SPE will act in its own best interests, and not be inappropriately influenced by a parent or originator. Among the decisions that may be made by the board of directors is the initiation of voluntary administration or winding-up processes. The inclusion of an independent director on the board of the SPE gives some comfort that the SPE will not take these steps contrary to the original objective of the transaction. Interlocking directorates—that is, an SPE having directors common with its parent—present a potential conflict of interest for those directors. If the parent becomes insolvent even though the subsidiary is meeting its debts as they fall due, and is otherwise in a satisfactory financial state, there may be incentive for the parent company to cause the subsidiary to voluntarily file for administration or winding-up. Standard & Poor's would expect an independent director to resist such a filing. As a general criteria point, Standard & Poor's expects an SPE to have at least one independent director on its board. In Australia, however, Standard & Poor's can attain a similar degree of comfort from a fixed-and-floating charge over the assets of the SPE combined with either an orphan SPE, or a charge over all of the shares in the SPE. To be considered an SPE, an entity will generally require an independent director on its board, unless: The SPE has granted a fixed-and-floating charge for the benefit of the rated securities; and either the SPE is an orphan, or all of the shares in the SPE have been charged in favor of the holders of the rated securities. Standard & Poor's views an independent director as a duly appointed member of the SPE's board of directors who is not at the time of appointment, and has not in the five years preceding appointment been: A direct or indirect legal or beneficial owner in the SPE, any affiliate of the SPE, the originator, or the arranger (excluding de minimis (of small things) ownership interests); A creditor, supplier, employee, manager, or contractor for or of the SPE; A creditor, supplier, employee, director, family member, manager, or contractor for, or of any affiliate of, the SPE (except, in the case of any director who is an independent director of another SPE), the originator, or the arranger; and A person who controls (whether directly, indirectly, or otherwise) any part of the SPE, its affiliates, the originator, or the arranger, or any creditor, supplier, employee, director, family member, manager, or contractor for any of the SPE, its affiliates, the originator, or the arranger. Tax Neutrality and Tax Consolidation Tax represents a potential payment outflow or leakage from a structured finance transaction. To the extent that a securitization vehicle is obliged to pay tax or to gross-up payments to compensate for tax withheld, the cash flow available to pay investors will be reduced by the amount of that tax. Tax neutrality describes the circumstances in which there is certainty that a securitization entity's obligation to pay tax will be minimal (if at all) and that it will have sufficient cash flow available to meet all of its tax obligations as they fall due. Standard & Poor's analysis of tax neutrality is a combination of cash flow and legal analysis, having reference to the tax opinions for the transaction. In performing its analysis, Standard & Poor's insists on certainty regarding the tax treatment and liabilities of the entity as well as its ability to meet those liabilities. In Australia, the group tax consolidation regime may undermine an SPE's tax neutrality. Standard & Poor's has published a comprehensive explanation of its approach to tax consolidation in Tax Consolidation and the Implications for Australian Securitization Vehicles (Jan. 27, 2004), reproduced here under the heading Tax Consolidation. Orphan Subsidiary An orphan subsidiary is an SPE whose shares are owned by a third party that is truly independent of the originator of the assets. As a result, there is no risk of the SPE being consolidated with the originator in any insolvency proceedings relating to the originator, and the risk of it being prematurely voted into winding-up is reduced. A true orphan subsidiary is also separate from the originator for accounting purposes. Typically, an orphan subsidiary's shares are held by a trust for the benefit of a charity or by a foundation or similar entity. It is Standard & Poor's general preference that all special-purpose companies are established as orphan entities. Trusts The use of trusts in Australian securitization structures is widespread because they offer a reasonably robust, yet flexible, vehicle that can enjoy tax neutrality. Trusts are typically used as the issuer of the rated securities, and the double trust structures common elsewhere in the Asian region are not as prevalent in Australia. Australia has a broad market of capable professional trustees that gives structures greater durability if they include the power to substitute trustees. Properly structured securitization trusts offer a number of benefits, including the power to clearly separate assets and achieve effective tax neutrality. In a properly structured securitization trust, the securitized assets are held in trust by a trustee who funds the asset acquisition or origination by issuing debt securities. Australian securitization structures typically involve trusts, established under common law, which issue equity interests through residual capital and residual income units. The interests in these units are fully subordinated to the securitized debt issuance. Although the concepts of statutory and trading trusts do exist in Australia, they are rarely used in Australian securitization transactions. Trustee Liability A common law trust is not a legal entity separate from the trustee. The term trust simply describes the basis upon which a person holds property. Accordingly, at law, debt securities are personal obligations of the trustee, meaning that the trustee can be sued by investors, subject only to the express limitations on liability in the relevant trust deed and other debt issue documents. Under the terms of the relevant trust deed, the issuer trustee's liability under the debt securities is generally limited to the proceeds from the underlying trust assets available to meet the issuer trustee's promise to pay principal and interest on the debt securities. Trustee's Right of Indemnity A trustee is not expected to meet the obligations of the trust from its own resources. It has a right to be indemnified out of the assets of the trust for properly incurred trust obligations. A trustee's right of indemnity arises from a combination of general common law principles, applicable trustee statutes, and, typically, the relevant trust deed. There are limitations to a trustee's right of indemnity. For example, the amount that can be recouped from the trust assets may be reduced as a result of a breach of trust by the trustee, and holders of the debt securities may suffer a shortfall. In a structured transaction, to better protect investors against such risk, a second trust is created. This is the security trust constituted by a security trust deed. The security trustee will be a different entity from the issuer trustee. Under the security trust deed, the issuing trustee covenants in favor of the security trustee that it will pay principal and interest on the issued securities. The issuing trustee provides a charge over the securitized assets to secure the performance of these covenants, and the holders of the debt securities gain direct recourse to the securitized assets through enforcement of the charge. Insolvency Because a trust is not a separate legal entity, it cannot technically be insolvent. A trust cannot sue or be sued and it cannot have a liquidator or bankruptcy administrator appointed to it. In securitization transactions, reference to a trust being insolvent is a shorthand way of describing a situation in which the obligations properly incurred by the trustee cannot be met from the proceeds of the trustee's indemnity. This is likely to result in acceleration of payment obligations and enforcement of security. Conversely, a trustee may itself become insolvent for any one of a number of reasons. Trustee insolvency should not trigger acceleration and enforcement of a transaction because the trust assets will be isolated from the trustee's other assets and will not be available for general creditors. The trust deed should provide for prompt replacement of the trustee and all trust assets to immediately vest in the new trustee. Taxation In general, an Australian securitization trust will be structured to ensure that, at all times, an Australian resident beneficiary is currently entitled to the net income of the trust. The trustee should not, then, be liable for tax on the income of the trust and the trust should be effectively tax neutral. Because there are exceptions to this simple principle and the Australian taxation landscape is continually changing, there can be no absolute assumption of tax neutrality. A thorough tax analysis is, therefore, always advisable. SEPARATION AND CONTROL OF ASSETS Transfer: True Sale Transferring underlying assets into a securitization structure in a way that establishes complete legal independence from the originating transferor and that will survive the liquidation, winding-up, or other demise of the transferor is fundamental to securitization. Standard & Poor's considers a transfer that achieves complete independence to be a true sale. As in other common law jurisdictions, Australian law supports the transfer of equitable interests in assets, independent of legal ownership. Securitization structures typically involve the initial transfer of an equitable interest in the assets, coupled with the vesting of sufficient powers and authority, to perfect or protect that equitable interest. To achieve true sale, the transfer of the underlying assets must operate in a way that ensures that the assets will not, in any circumstances, form part of, or be clawed-back into, the insolvency estate of the transferor, and that the transfer cannot be recharacterized as a secured loan. True sale in Australia is a question of the substance, fairness, and commerciality of the transfer. As part of its analysis, Standard & Poor's will expect to see legal opinions confirming that there are no aspects of the transfer that call true sale into question. In addition to the structure creating legal independence from the originating transferor, the underlying assets must themselves be freely transferable. Standard & Poor's asset-level criteria require the underlying assets to: Be freely assignable; Comply with regulatory requirements; Be free from potential set-off claims by the borrower; and Be managed by the securitization entity without impediment. Perfection of Title Perfection of title is the process of combining legal title in the assets with the existing equitable title to give full legal and beneficial ownership in the assets to the securitization entity. Perfection typically requires three actions: Registering the transfer of the security on the appropriate legal register (if any); Giving notice of assignment of the loan to the borrower; and Completing other documents prudently necessary to perfect the title of the securitization entity in the loans and security. Generally, this step would include creating a legal instrument of transfer or novation of the loans/receivables contracts. Title Protection Title protection is a term used to describe a legal arrangement that gives the practical protections of perfection, but that does not involve a legal transfer of the loans or receivables contracts to the securitization entity. Protection is not unique to the Australian market, but for local law reasons some issuers and arrangers prefer it to perfection. Protection involves: Registering the transfer of the security on the appropriate legal register (if any); and Giving notice of assignment of the loan to the obligor. The difference between protection and perfection is that in protection the third step for perfection is not completed. Following protection: The borrower can only discharge its payment obligation by payment to the securitization entity; The borrower cannot exercise any rights of set-off against the securitization entity; The securitization entity can meet all procedural requirements necessary to exercise all of the security rights of the assignor against the obligor; and The originating assignor must be joined in any legal proceedings against the obligor, but only as a matter of procedure, and no substantive cooperation is required. Secured Loan Structures For some asset and business types, secured loan structures can be an alternative to true sale for giving control of the underlying assets to the securitization entity. In Australia, commercial mortgage-backed securitizations and future-flow securitizations naturally lend themselves to secured loan structures. A secured loan structure is typically a two-tiered structure that has an issuing SPE at the top level and the asset-owning entity at the bottom level. The issuer SPE raises funds through the issue and lends them to the asset-owning entity (originator) secured against the underlying assets. When analyzing a secured loan structure, Standard & Poor's will focus on whether, as a matter of law, the transaction structure gives the securitization entity true control over the underlying assets via the security. It is inevitable that the degree of control held will be less than the degree required for true sale and that there will be greater risks to making full and timely payment. Consequently, Standard & Poor's analysis will involve, consistent with the rating level sought, an analysis of the incremental risks and the structural elements included to address those risks. The key risk that needs to be overcome in Australia is the risk of the asset-owning originator becoming subject to voluntary administration, with a consequential temporary moratorium on enforcement of some security interests. The three key aspects of Standard & Poor's legal analysis of secured loan are: The status of the originator and its relationship to the transaction structure; The enforceability of the loan and security, including the level of control over the underlying assets that it gives the securitization entity; and The nature and operation of liquidity facilities and other structural enhancements. Originator Experience has shown that financial instruments issued from secured loan structures have the greatest chance of achieving a rating that is significantly higher than the rating of the originator if the originator is a single-business/single-activity entity. In practice, if there is a real possibility that payment will be delayed because the originator is a multiple-business/multiple-activity entity or for any other reason, the level of enhancement above the originator's issuer credit rating on a secured loan will be small. On the other hand, if the originator is a single-business/single activity entity and it is possible to identify and closely analyze the risks relating to the underlying assets, and there is ample liquidity support for a transaction to be structured as a secured loan, a significant enhancement above the originator's issuer credit rating may be possible. A pledge or mortgage over all of the shares in the securitization entity is a structural element that will also be relevant to credit rating analysis, especially if the securitization entity remains on the originator's balance sheet. Legal opinions may be sought to confirm that there are no grouping or consolidation risks arising from the securitization entity remaining on the balance sheet. Security: Enforceability and True Control Standard & Poor's must be satisfied that, as a matter of law, the security gives the issuer securitization entity "true control" of the assets, is fully enforceable, and cannot be challenged under general law or insolvency law. If, via the security, the issuer has conduct of, or control over, the enforcement of the security, and has priority over all competing creditors, the security is over appropriate assets and is adequate to repay investors, Standard & Poor's may conclude that the securitization entity has true control over the assets. Enhancements Standard & Poor's will examine the liquidity risk inherent in each secured loan structure and will often require suitably rated liquidity support at a level appropriate to mitigate liquidity risk. Standard & Poor's will also consider other structural enhancements and elements that reduce incentives to file for the insolvency or winding-up of the securitization entity, or otherwise challenge the secured loan structure. Enhancements may also be included in a structure for other reasons, including mitigation of the timeliness risks associated with the enforcement of the security or the increased risk of loss of value of collateral resulting from a loss of true control. True Control The key to true control lies in ensuring that, in all potential circumstances, the issuer will have conduct of the enforcement of the security. If control could be lost, there is a risk that full receipt of interest and principal due on an issued instrument will only be possible after a delay caused by administration, insolvency, or other statutory or legal processes. Standard & Poor's analysis of a secured loan structure will include a consideration of the following issues: The question of whether or not the security package will defeat the claims of existing and potential creditors of the originator. The securitization entity should hold a first-priority fixed charge over the underlying assets of the originator, and the structure should minimize the potential for prior ranking claims being made against the assets. The nature, value, and liquidity of the assets subject to the security is highly relevant to Standard & Poor's asset level analysis. Clearly, the security, when enforced, must be more than adequate to repay investors. The nature of the underlying assets is also relevant. A secured loan transaction that relies on the cash flow generated by the underlying assets (rather than their market value) could default if forced to rely on the market value realized through the sale of assets (for example, in enforcement). If the assets are receivables representing a known and certain income stream (including receivables that are expected to generate repayments for the secured loan), security over them should be realized through the transfer of the originator's rights in those assets to the securitization entity (and not a sale on the open market). True control is achieved under such a security structure, by preserving the cash flow within the transaction, meaning that there should be little risk to full and timely payment. If the security is over the originator's real property or other market value assets, those assets may have to be sold to realize the security. A forced sale may mean that the security is insufficient to provide full payment to the investors. Under such a market value security, market value risk on enforcement is a threat to true control. A significant risk to true control in Australia is the administration regime. As outlined in the earlier section on insolvency, the potential for administration of the securitization entity creates risks of delay and reduced recovery. As explained previously, a valid charge over all, or substantially all, of the originator's property that incorporates an immediate power to appoint a receiver and manager will help to mitigate this risk. Standard & Poor's will, therefore, expect the security package to include a first-priority floating charge over all the originator's present and future assets not caught by the fixed charge over the underlying securitized assets. From a ratings perspective, if a secured loan is properly structured, the risk of an administrator being appointed should not necessarily lead to the conclusion that there is no control. Insofar as the enforcement actions of the issuer could involve additional costs to the issuer or create potential delays in payment, Standard & Poor's will generally look for appropriate support in the structure. The balance between fixed and floating security should be such that the assets subject to the floating charge are not relied upon primarily to generate funds to repay investors. Standard & Poor's will analyze the issuer securitization entity to ensure that it meets Standard & Poor's SPE criteria and that it has granted security over all, or substantially all, of its assets, incorporating the immediate power to appoint a receiver and manager. Standard & Poor's expects the security package to benefit from legal opinions confirming the valid creation of the security, its ranking, and freedom from competing claims in the insolvency of the grantor, including, for example, claims that it represents an unfair preference, an unfair loan, or an uncommercial transaction. Segregated Issue Structures In many securitization transactions, particularly in multijurisdictional transactions, the transaction sponsor may find it cost effective to set up a single program and issuing vehicle to issue multiple series of rated securities. To achieve this in a manner that allows Standard & Poor's to rate each series independently of the other series, the issuing vehicle, the program, and each series must be created in a way that ensures that the securitization vehicle is, essentially, insolvency remote for each series. That is to say, if one series defaults, then the issuer's creditors (including the relevant series noteholders) cannot render the issuer insolvent or accelerate its obligations generally. Typically, a segregated issue structure will involve an SPE issuer issuing multiple series (which may or may not be tranched) under an umbrella program, each series being secured by a separate portfolio of assets and having separate swap agreements and credit enhancement for the related cash flows. Effective segregation is not just a question of law and, although Australian law supports segregation, not every legal jurisdiction has laws that enable effective segregation. In its analysis, Standard & Poor's considers whether or not segregation is legally and practically effective by examining: The program issuer; The program structure; The identification and separation of series assets; The nature of the security interests; and The limitations on creditors' rights. The consideration of segregation in this section is limited to Australian program issuers with series assets located in Australia. The aspects of the program that Standard & Poor's examines to determine the effectiveness of segregation in Australia are generally the same as those in other jurisdictions. At a detailed level, however, the law applying to the program issuer, the transaction documents, and the assets will be vary from country to country and may not support segregation. To the extent that a segregated program involves multiple jurisdictions and governing laws, Standard & Poor's relies on the transaction arranger to identify the relevant jurisdictions and applicable laws, including the law applicable to the program issuer, the governing law of the transaction documents, and the laws applicable to the assets, the security interests, and the custodial arrangements (if any). Standard & Poor's must review every series issued by a program issuer (whether or not all series are rated) to determine if the program as a whole complies with its segregation criteria. Due to the way that segregation works, if one series fails to support segregation, it undermines the insolvency-remoteness of the series issuer for all series issued. If Standard & Poor's cannot establish that all series are effectively segregated, it will have to rate all series equally with the rating of the series tranche having the greatest likelihood of default (that is, the lowest rated or unrated tranche). Program Issuer Insolvency Remote Entity To support segregation, a program issuer must be insolvency remote and, preferably, an orphan entity. If the program structure is tiered, other entities within the structure may, depending on their roles, also need to be insolvency remote. Again, it is Standard & Poor's preference that such entities are orphan entities. Insolvency remoteness is required because a program issuer with differently rated series has, by definition, series of notes backed by assets that Standard & Poor's has determined have a different likelihood of default. If a lower-rated series defaults while a higher-rated series is performing, an operating company parent may have incentive to attempt to wind up the program issuer or to take other similar actions to preserve its economic interest in the issuer. Similarly, creditors and others with claims against a poorly performing or defaulting parent may attempt to penetrate the corporate structure to reach the program issuer's assets. Preferred creditors might also attempt to attach a program issuer's assets to satisfy claims against its corporate affiliates. For the same reasons, the seller of the underlying asset(s) should not have an equity interest in the program issuer. This limitation is intended to deter a seller, as owner, from inducing a program issuer to begin winding-up proceedings or to take other actions to protect its interest in the program issuer as a financing vehicle. Likewise, for each series, the program issuer should acquire the underlying assets in a true sale or comparable transaction so that ownership is beyond question. Attempts to reach a program issuer's assets by or through the seller or an operating parent may not ultimately succeed, but they may delay or prevent full and timely payment of amounts due to the holders of notes in performing series. An orphan SPE structure reduces this risk by separating the ownership interest in the SPE from the program issuer's activities and by separating the program issuer from the economic interests of a parent operating company. As well as meeting the general requirements for insolvency remoteness as an entity, a program issuer also needs to display effective insolvency remoteness between series. That is to say, the creditors of each series, including noteholders, need to be legally prevented from accessing the program issuer's assets that secure other series and from commencing insolvency proceedings against the program issuer. To reduce the risk of delay by ill-founded creditor claims, creditors (including noteholders) must agree to and be made aware of the limited recourse and nonpetition provisions that prevent them from accessing the assets of other series. Limited recourse and nonpetition are considered in more detail below. Program Structure

Documentation Standard & Poor's will review a program issuer's documents to determine whether the series assets and the obligations of the program issuer are unambiguously identified and segregated on a series-by-series basis. If a program issuer has previously issued unrated series, Standard & Poor's review will also include those unrated series. Areas of particular interest to Standard & Poor's include how security interests are granted, the remedies that can be exercised upon default, and the payment of fees and expenses (including enforcement expenses). Documents that include an indemnity from the program issuer are problematic if the program issuer does not have an uncommitted source of revenue to fund indemnity claims. In documenting segregated programs, the clearest and most preferable approach from a rating perspective is to have a new set of documents for each series, with no cross-references of any kind to any other series or documents. The form of the program and series documents is set when the program issuer is created and a full set of documents is reproduced for each new series, with information specific to the series and the series assets. Because program issuers usually enter into agreements with the same parties for each series, the transaction parties often seek to reduce the volume of documents required for each series. Often, that reduction is in the form of an agreed set of standard terms and conditions that are incorporated into documents for each series or master agreements that are supplemented for each series. If master documents are used, the obligations of the program issuer and the related series assets must, on a series-by-series basis, be unambiguously identified on the face of the documents, including each trust deed and series supplement. When a series is issued in accordance with master documents, legal opinions should address the enforceability of the master documents, as well as the documents for the specific series. If master documents are used, Standard & Poor's may seek additional legal opinion confirming that the legality, validity, binding effect, and enforceability of the obligations of the parties to the documents for a series of notes would not be affected by any illegality, invalidity, lack of binding effect, or enforceability of the obligations of any of the parties to the documents for any other series. If the master documents have that additional program, issuers may use the same program documents. Standard & Poor's will then, typically, request that the additional legal opinion include all such program issuers and all series issued by such other program issuers. Swaps The swap agreements relating to a series modify the cash flows generated by the underlying asset into the type of cash flows required to meet the payment obligations on the notes. If, because of its terms, a swap for a new series could be affected by events affecting the swap for an existing series, then, through the swap, the rating on the new series is dependent on the first series. Cross-defaults, cross-termination events, and the netting of payments between swap transactions are some of the provisions that may result in a conclusion that the swaps are not separate between series. The most straightforward approach to documenting series swaps is to use a separate master agreement, including schedule and confirmation, for each series. However, a program issuer will usually enter into swaps with the same counterparty for each series, and the parties will seek to reduce paperwork by creating some form of umbrella documentation structure. As long as the legal effect is to create separate agreements independent of other series, other documentation structures may be acceptable to Standard & Poor's. For example, if properly drafted, a master swap agreement and schedule with separate series confirmations may be adequate. Identification And Separation Of Series Assets General For each series, the program issuer should issue a separate series of debt obligations, with the assets that support each series being unambiguously identified and held separately from assets relating to other series. The clear identification and separation of series assets—together with the clear identification of the obligations of the program issuer that are secured by those assets—are necessary to ensure that if a program issuer defaults on any of its obligations, it is clear which assets of the program issuer are available for the exercise of remedies relating to that obligation. Clear identification and separation are also necessary to ensure that, in any enforcement action or proceedings (including insolvency of the program issuer), a court would uphold the related agreements by series creditors to look only to those assets of the program issuer designated to be available to satisfy its obligations to them. Series Assets Identification The existence of effective security interests and effective limitations on creditors' rights are fundamental to Standard & Poor's analysis of the incentives for noteholders and other creditors to take, or to attempt to take, action against a program issuer that might result in its insolvency or bankruptcy. Effective security interests and effective limitations on creditors' rights depend, in turn, on the unambiguous identification of the assets and of the obligations of the program issuer that are subject to such interests and limitations. Imprecise identification or the commingling of a program issuer's assets may result in a perception or determination that its assets are not segregated by series for the purpose of exercising legal remedies. Such a determination or perception may lead to the satisfaction, or attempted satisfaction, of claims relating to one series from assets that were expected to be available to satisfy obligations relating to another series. In circumstances like these, Standard & Poor's would view each series as a dependent rating for the others and, consequently, all tranches of all series would have the same rating. The unambiguous identification of the assets and obligations of a program issuer on a series-by-series basis is also needed to support the limitations on creditors' rights. If a creditor has agreed to look only to specified assets for satisfaction of its claims, but those assets have been imprecisely identified or commingled to the extent that they cannot be segregated from the program issuer's other, it may be that the creditor has not effectively agreed to the limitation. Such a creditor has an incentive, whether or not supported at law, to attempt to recover generally against all of the program issuer's assets. Similarly, if any of a program issuer's secured obligations are stated generally (for example, in the payment of fees and expenses, and not on a series-by-series basis), then the program issuer's failure to fulfill its obligations on one series may entitle or incentivize the trustee or the noteholders of other series to exercise, or seek to exercise, remedies generally against the program issuer. Again, this would result in the same likelihood of default and, therefore, the same rating for all series. Separation of Series Assets Series assets, including all proceeds from series assets, should be held and accounted for separately on a series-by-series basis and not commingled with the assets of other series. Likewise, the program issuer's obligations, including fees, expenses, and costs of enforcement, should be specified and accounted for on a series-by-series basis. Each program issuer's records should include separate accounts for each series, to which the series assets must be credited in a manner that clearly identifies the assets and the related series. The books and accounts of the trustee, and of any custodian to which the assets will be credited, should include separate entries clearly identifying the assets, the related series, and the capacity in which the party is acting. Sub-accounts within a trust account on the books of the trustee or custodian may be adequate if the arrangement is consistent with the creation and perfection of the required security interest. Suitable Asset Types Not all types of assets are suitable as series assets for program issuers. Standard & Poor's reviews, on a case-by-case basis, new asset types to determine their suitability for program issuance. Issuers and arrangers are encouraged to contact Standard & Poor's early to discuss the suitability of new classes of assets for any segregated program proposing to issue series of notes with different ratings. Nature of Security Interest The effectiveness of the security interests over the series assets is fundamental to Standard & Poor's creditor incentive analysis and the conclusion that a program issuer is insolvency remote. To this end, Standard & Poor's expects that a first-fixed charge or equivalent first-priority security interest, that will remain fully effective in the program issuer's insolvency, will be created and perfected over all of the program issuer's assets on a series-by-series basis. Standard & Poor's considers that creditors' incentives are reduced by the granting of effective security over all of the program issuer's assets on a series-by-series basis. If the noteholders of each series have a first claim on the related series assets upon enforcement of their security and the noteholders of other series have no claim to those assets, then, even if the program issuer is subject to insolvency, winding-up, or liquidation proceedings, little could be gained by the noteholders of a series attacking the assets of another series. Consequently, in these circumstances, Standard & Poor's considers the incentive of series creditors (including noteholders) to attempt to have such proceedings reduced. Similarly, if all of a program issuer's assets are subject to first priority perfected security interests that would be effective even when the program issuer is subject to insolvency, winding-up, or liquidation proceedings, the unsecured creditors of the program issuer have little to gain by beginning proceedings against the program issuer. Applying the same reasoning, cash flows should be structured so that there are, in effect, no uncommitted revenues or excess cash flows that could provide an incentive for noteholders or other creditors to attempt to reach such amounts through insolvency proceedings. As a general matter, Standard & Poor's will request legal opinions addressing the creation, perfection, priority, and effectiveness of the stated security interests in the assets for each series, including in the insolvency of the program issuer. Opinions will be requested from counsel in the jurisdictions in which the program issuer and the series assets are most likely to be subject to proceedings and, if different, the law under which the security interest has been created and perfected. Typically, the relevant jurisdictions will include the jurisdiction in which the program issuer is organized and domiciled, the jurisdiction in which the assets are located, and the jurisdiction selected to govern the security agreements. Limitations On Creditors' Rights General For each series, the related noteholders and other secured parties (including the swap counterparty, if any), the trustee, and other series service providers should agree to look only to the assets pledged as security for the series and not to seek recourse against any of the program issuer's other assets for satisfaction of the program issuer's obligations to them for the series. Series creditors should also agree that, upon default and the enforcement of the security over the related assets, the amount realized constitutes a complete discharge of the program issuer's obligations to them. Such limited recourse provisions should be included on all notes and global securities. Limited Recourse Standard & Poor's requirement that limited recourse provisions be effective in the insolvency of a program issuer is fundamental to its view that creditors' incentives to commence winding-up or insolvency proceedings against the program issuer are minimized, which, in turn, assists Standard & Poor's to ascertain whether or not the program issuer is insolvency remote. Arrangers, program issuers, and their counsel should understand that Standard & Poor's criteria require insolvency issues to be addressed in the relevant legal opinions, even when a program issuer has been organized as a limited-purpose entity. Limited purpose alone is not sufficient for Standard & Poor's to conclude that an entity is insolvency remote. If a series is issued without effective limited recourse provisions, the noteholders of that series may be entitled to satisfy the program issuer's obligations to them from any of the program issuer's assets. In the event of a default, this would give considerable incentive to noteholders to begin winding-up or insolvency proceedings, or to take other action to attempt to reach a program issuer's assets that are pledged to other series. Even if a claim against the program issuer's other assets did not ultimately succeed because of the prior security interests of the other noteholders, the attempt is likely to prevent the timely payment of amounts due to those other noteholders. Standard & Poor's will generally require program issuers to include limited recourse provisions for all secured parties in every series it issues, including unrated series. Limited recourse provisions should include the extinguishment of creditors' claims following realization of the series assets. Following a series default and enforcement of the security over the related series assets, distribution of the amount realized should constitute a complete discharge of the program issuer's obligations to the series creditors (including noteholders). If creditors are unable to assert claims for amounts beyond those realized from the series assets, there will be no basis to support a claim for further recovery against the program issuer or for winding-up proceedings. Extinguishment should also ensure that there is no basis for proceedings against the program issuer on the grounds that it is insolvent. It is important that the issuer does not become insolvent, because its directors may then have a fiduciary duty to take action that potentially includes winding-up. In addition, other creditors may seek to file against the program issuer if it is, or appears to be, insolvent. Standard & Poor's will generally request a legal opinion confirming the effectiveness of limited recourse provisions and that a court would not uphold a claim by the creditors of one series that the assets of the program issuer beyond the series assets should be available to them—even if the program issuer is subject to insolvency, winding-up, or liquidation proceedings. Standard & Poor's expects the opinion to also confirm that, to the extent that creditors claims against the issuer are subject to limited recourse provisions (including extinguishment), the issuer cannot be insolvent, because its liabilities cannot exceed the funds available to pay them. If, under applicable law, limited recourse provisions require notice to the limited party for the limited recourse agreement to be effective, counsel delivering the opinion will need to ascertain that procedures are in place that let it deliver an unqualified opinion. Nonpetition The noteholders and, to all possible extent, all other series creditors should agree not to file, or to join in any filing of, a petition, or take any other action for the winding-up, insolvency, or liquidation of the program issuer. Similarly, all transaction participants, including swap counterparties and credit support providers (if any), and all subsequent creditors of the program issuer should agree not to file, or to join in any filing of, a petition or take any such action until after all of the program issuer's rated obligations have been satisfied, including waiting for the expiry of any "unfair preference" clawback period. Standard & Poor's will typically request an enforceability opinion in connection with nonpetition agreements. In addition, noteholders' enforcement rights against the series assets should be vested in the trustee to reduce the risk that a noteholder, by mistake or deliberately, may seek to enforce its rights in a manner that is inconsistent with series segregation and the restrictions on its rights, including the limited recourse provisions. General and Preferred Creditors A general creditor is one whose claims against the series issuer are not effectively limited by appropriate limited recourse provisions. Each program issuer needs to be able to clearly demonstrate to Standard & Poor's either that it does not have general creditors or that it is adequately funded to meet the potential claims of its general creditors. Without effective limitation or appropriate provisioning, a general creditor may be able to bring successful insolvency or winding-up proceedings against the program issuer and undermine its insolvency remoteness. Preferred creditors are a subset of general creditors who will, by statutory prescription, rank ahead of noteholders in the assets of the program issuer in its insolvency. A program issuer's potential liabilities to preferred creditors should be minimized through the transaction structure and documentation, including the security documents. In assessing the potential liabilities of a series issuer to general creditors, Standard & Poor's expects the issuer and its legal advisors to consider and provide information: Identifying the creditors of the issuer who are not subject to effective limited recourse and nonpetition provisions; Commenting on the nature and priority of the interests that general creditors have in the assets of the issuer relative to the holders of the rated debt; and Explaining the manner in which liability to general creditors is mitigated or eliminated by the structure. Tax Taxes represent the potential claim of an unlimited general creditor. When assessing a potential, segregated program issuer, Standard & Poor's expects the issuer and its legal and tax advisors to provide a tax opinion confirming the tax neutrality of each series. Surveillance To support its ratings on the current and future issues of a series issuer, Standard & Poor's must perform regular surveillance on all outstanding series from that issuer, whether or not all series are rated. Without ongoing surveillance, Standard & Poor's would not be able to conclude that each series is effectively segregated from all other series and, accordingly, would have to rate all issued series equally with the series tranche having the highest risk of default (which may be an unrated series). Each series issuer should then agree to Standard & Poor's reviewing and maintaining surveillance on each series, whether or not it is rated by Standard & Poor's. SELECT LEGAL CRITERIA ISSUES Commingling Risk Commingling risk is the risk that securitized cash flows become mixed with the funds of a third-party or pass through the bank account of a third-party in such a way that, in the insolvency of that third-party, the cash flows become lost or frozen. Standard & Poor's considers a cash flow to have been lost if, following the insolvency of a third-party, the securitization entity's claim to the money would be treated at law as an unsecured debt of the insolvent entity. A cash flow is considered frozen if, following the insolvency of the third-party, the securitization entity retains a proprietary claim over the money, so that it does not form part of the assets of the insolvent entity, but is unable to deal with the cash flow promptly and without interference. A cash flow may be frozen in a number of circumstances other than by third-party insolvency, including through the operation of a security interest or by operation of law. In its analysis, Standard & Poor's treats lost cash flows as a total credit loss to the securitization entity. Frozen cash flows are not necessarily a total credit loss to the securitization entity, but are a liquidity stress on the transaction. In determining an appropriate stress level, Standard & Poor's will seek to determine how long it may take the securitization entity to recover frozen funds from the insolvent entity and in competition with its creditors. To overcome commingling risk and its effect on the rating of issued securities, a transaction needs to demonstrate features that enable the securitization entity to meet its obligations on the rated notes in full and on a timely basis, regardless of any delay in cash flows caused by a third-party's insolvency. If there are appropriate mechanisms in the transaction to meet the liquidity stress caused by the delay in recovering frozen funds, Standard & Poor's will give credit to some level of recovery of the frozen funds. The most common example of commingling arises where the obligors under sold receivables continue to make payments into the accounts of the originator/transferor. Regardless of whether or not the originator/transferor has sold the receivables to the securitization entity, if the transferor collects the proceeds from the receivables on behalf of the securitization entity, once the payments reach its account, they will be treated as having been lent by the securitization entity to the accountholder. As a consequence, on the insolvency of the transferor accountholder, the securitization entity's rights to the payments held in the accountholder's name will be an unsecured right to repayment of the loan. Standard & Poor's has seen a number of mechanisms added to transaction structures that can limit commingling risk. For example, an accountholder may declare a trust or grant a charge over the amounts standing to the credit of the relevant account for the benefit of the securitization entity. In each case, Standard & Poor's will need to be satisfied of the effectiveness of the mechanism, and this may require external legal opinions. Account Bank Insolvency The question of what happens to money held with a bank when the bank becomes insolvent is not strictly a commingling issue, but there is often a degree of confusion between the two issues, particularly when the transferor is a financial institution as well as the account bank for the transaction. When a person deposits cash with a bank, that person's claim to the balance of the account constitutes a debt owed by the bank to the accountholder. Since banks are not in the habit of granting security to their accountholders, the debt owed by the bank will be an unsecured debt and will be treated accordingly upon the bank's insolvency. Therefore, in its analysis, Standard & Poor's will assume that cash held with a bank not rated highly enough to support the rating on the corresponding notes is not available to the securitization entity. Account bank insolvency risk can be minimized by limiting the time that funds are held in an account with an insufficiently rated institution, either by moving the funds into an account with a suitably rated institution or by investing the funds in suitably rated eligible investments. Investing the funds should be done to ensure that proper security may be given over them, thereby protecting the securitization entity's interests in the event of account bank insolvency. Rating Triggers Under Standard & Poor's weak-linking rating methodology for analyzing a structure, an entity will only be assumed to be at risk of insolvency if that entity's current rating is below the rating of the issued notes (or if the entity is unrated). Accordingly, a transaction is not expected to have features designed to mitigate the effects of commingling if the SPE's cash is commingled only with cash belonging to entities rated as highly, or higher, than the notes. This is equally the case for account banks. Conversely, commingling funds or maintaining an account with an entity rated below the notes (including an unrated entity) will make the rating on the notes dependent on that entity's rating unless there are other mitigating factors. All other things being equal, the downgrading of such a dependent entity, or the placement of its ratings on "CreditWatch" with negative implications, would normally lead to the rating on the issued notes being downgraded or similarly placed on "CreditWatch" with negative implications. Set-Off Risk Set-off risk is a risk to the certainty and timeliness of payment. It is the risk that a payment may be reduced by the amount of a claim that the payer has against the payee or delayed by the payer pursuing such a claim. A successful set-off claim results in a netting out of the amounts of the two claims based on their respective merits. Consequently, the potential availability of set-off creates a risk that a securitized cash flow may be reduced in amount, or payment delayed, by a claim-back by the payer. The potential for set-off increases as the number and scope of the relationships between the payer and payee increase. For example, set-off risk is greater if a lending originator also provides deposit accounts and advisory services to borrowers, as well as lending it funds. Not all of a payer's claims of against a payee will substantiate a set-off claim. The law recognizes contractual, equitable, insolvency, and statutory bases for set-off rights. The grounds and potential application of set-off rights in any particular situation need to be considered under those four heads, although in some Australian states, statutory set-off has been repealed. In conducting its analysis, Standard & Poor's needs to be satisfied that there are no legal grounds for claiming set-off against securitized cash flows at any level of the securitization structure. Standard & Poor's will usually refer to the legal opinions for certainty regarding set-off. Standard & Poor's will also ask to see that the likelihood of delay caused by set-off claims, whether or not well grounded, is minimized. Standard & Poor's considers that a waiver of set-off given by the payee reduces the risk of a set-off claim being brought—the payee being expressly aware that he or she has foregone set-off rights. To the extent that Standard & Poor's is not satisfied that the risk of set-off has been fully addressed, it will size conservatively for the potential risk. Account Provider Set-Off Cash in a bank account may also be lost in the insolvency of the accountholder if the account provider is allowed to assert set-off. In other words, it may be lost if the accountholder owes money to the account provider and the account provider is allowed, under the terms of the account or under general principles of law, to set off the amounts owed to it by the accountholder against monies standing to the credit of the account. That set-off may include cash held in the account, but belonging to the securitization entity. The standard account operating terms of most authorized deposit-taking institutions explicitly permit the account provider to set off account balances against obligations owed to it by the accountholder. For Standard & Poor's to give credit to cash collections standing in an account in the name of a party other than the securitization entity, legal opinions must be provided to the effect that, as a matter of law, the account provider will not be entitled to effect set off against the accountholder. For example, this may be the case when the account provider is aware of a declaration of trust by the accountholder in favor of the securitization entity. In addition, to reduce the risk of delay through a set-off claim by the account provider (whether or not well grounded at law), Standard & Poor's requires that the account provider expressly waives its rights of set-off over the account. That requirement applies even in circumstances where, as a matter of law, set-off rights may have been lost through other causes. Guarantees Often, credit support is provided to a securitization structure through a guarantee or other, similar irrevocable and unconditional payment obligation. Examples of such payment obligations include parent guarantees, debt-purchase agreements, surety bonds, and insurance contracts. An effective guarantee can elevate the rating on the obligation guaranteed from the rating of the primary obligor to that of the guarantor. To allow a credit elevation to the rating or creditworthiness of the guarantor, there must be an appropriate degree of certainty, relative to the rating level sought, that the guarantor is unconditionally obliged to pay under the guarantee. Standard & Poor's examination of guarantees focuses on the circumstances in which the guarantor may be excused from making full payment under the guarantee. To give full benefit of a guarantor's rating to a guarantee, Standard & Poor's expects the guarantee to include or address the following concerns: The guarantee is one of payment and not of collection. In other words, the guarantee should be a promise by the guarantor to pay the guaranteed obligation on demand, rather than merely a promise by it to pay any deficiency remaining after the beneficiary has exhausted all of its remedies against the collateral and the primary obligors. The guarantor agrees to pay the guaranteed obligations on the date due and waives demand, notice, and marshaling of assets. Under applicable insolvency laws, the guarantor's obligations under the guarantee rank pari passu with its senior unsecured debt obligations; The guarantor's right to terminate or amend the guarantee is appropriately restricted. The guarantee is unconditional, irrespective of value, genuineness, validity, or enforceability of the guaranteed obligations. The guarantor should waive all other circumstances or conditions that would normally release a guarantor from its obligations. The guarantor should also waive its rights of set-off, counterclaim, and subrogation. In connection with lease transactions, the guarantee should also provide that in the event of a rejection of a lease in a bankruptcy proceeding, the guarantor will pay the lease payment, notwithstanding the rejection, and as though the rejection had not occurred. The guarantee must reinstate if any guaranteed payment made by the primary obligor is recaptured as a result of the primary obligor's bankruptcy or insolvency. The holders of the rated securities are beneficiaries of the guarantee. If a transaction involves guarantors that are domiciled outside of Australia, the guarantees must include appropriate tax and currency exchange provisions to give certainty to the amount that is guaranteed. TAX CONSIDERATIONS Tax Liabilities In all securitization transactions, Standard & Poor's analysis will examine the SPE's potential tax liability and, if relevant, that of any intermediary SPEs. In conducting that analysis, Standard & Poor's will look primarily to the advice provided by the issuer's tax advisors. In general, Standard & Poor's will be seeking to ascertain that the issuer has no tax liability or that it has sufficient available cash flow, after meeting all of its other obligations, so that it can meet its tax obligations as and when they fall due. In addition to these general considerations, multijurisdictional transactions potentially have additional tax liabilities that need to be examined. Nonresident Withholding Tax Whenever cash flows across a jurisdictional border, there is a risk that the tax authority in the jurisdiction from which the cash left will require part of that amount to be remitted to it in the form of withholding tax. This is often the case in cross-border structured finance transactions, when cash is passed from payers in one country to an SPE issuer in another country. If an issuer's ability to make full and timely payment on its rated notes relies on such third-party payments, Standard & Poor's rating analysis will need to consider whether or not those payments are subject to withholding tax. Standard & Poor's will also consider the extent to which an issuer may be liable for gross-up payments under issued instruments to overcome the effect of withholding tax. Withholding tax may occur with respect to payments under swaps and other derivative agreements entered into by the issuer for hedging purposes. It may occur in relation to payment under any third-party credit enhancement, such as a letter of credit, liquidity facility, or guarantee. It may also occur in relation to payments derived from a pool of underlying assets, such as loans, bonds, or other securities (collateral) and receivables that secure the issuer's rated obligations. To the extent that withholding tax may be imposed on any of these types of payments, an equivalent amount must be deducted from the relevant transaction's cash flow model when determining the amounts available to the issuer to meet its obligations under the rated notes. To obtain comfort that such a deduction is not necessary, Standard & Poor's will want to see the risk of withholding tax in a transaction either eliminated structurally or addressed legally. Structurally, the risk of withholding tax is removed if the third-party payer is required to gross up its payment obligations so that the issuer receives the same amount that it would have received had no withholding tax been payable. Obviously, the obligation to gross up must be legal, valid, binding, and enforceable under the applicable law, and will create a rating dependency on the party required to gross up. Alternatively, if it can be demonstrated that even net of applicable withholding tax there is sufficient cash flow to allow payment in full on the rated notes under the various stress scenarios, Standard & Poor's will not require additional comfort that mitigates withholding tax risk. Most often, express legal comfort that there are no withholding tax risks to the relevant payments will be required, as transactions are usually structured to eliminate this risk. Typically, that comfort will be provided by legal opinion confirming that, under the law of the jurisdiction of the third-party payer, no withholding tax obligation will arise on payments to the issuer. Although withholding tax opinions should come from external legal counsel, in some jurisdictions it may be appropriate for the opinion to be given by qualified accountants from suitably reputable firms. Also, with respect to withholding tax on swaps, derivatives, and external credit enhancement, Standard & Poor's may find it acceptable for these opinions to be issued by internal counsel to the relevant counterparty. In lieu of opinions, Standard & Poor's may accept the unqualified written representations of appropriately rated counterparties in swap and derivatives transactions confirming that payments by them to the issuer are not subject to withholding tax. Such representations should be in a form commonly accepted in standard financial transactions (for example, International Swaps and Derivatives Association (ISDA) form tax representations). For some types of credit enhancement, Standard & Poor's may also request that the enhancement provider delivers a similar representation. If payments on the rated notes depend on payments from collateral being made free of withholding tax, appropriate assurance regarding withholding tax will be required. To the extent that withholding tax risk is not eliminated, structurally robust comfort that there is no withholding tax risk will be required. Typically, such comfort will be in the form of a legal opinion. Alternatively, in the context of collateralized debt obligation (CDO) transactions, an unqualified written representation, in the form commonly delivered in standard financial transactions, from either the arranger and/or collateral advisor (as appropriate), may be accepted. Standard & Poor's expects that, in making such representations, the arranger and/or collateral advisor will have undertaken the requisite legal due diligence to ensure that there are no withholding tax risks when structuring the transaction and selecting the collateral. For transactions involving revolving or ramp-up periods, Standard & Poor's will also expect the parties to the transaction to demonstrate that, after closing, the transaction will not be subject to withholding tax risks. Such comfort may, for example, be in the form of deemed representations or through the definition of the collateral's eligibility criteria, confirming that the collateral purchased after closing is not subject to withholding tax. Additionally, in the context of CDO transactions, Standard & Poor's will accept a legal memorandum from tax counsel in the relevant jurisdiction stating that the collateral sold to the issuer does not attract withholding tax. Provided that the specific collateral purchased by the issuer clearly falls within the ambit of the memorandum, Standard & Poor's will not require any further opinions or representations to be delivered on the issue of withholding tax on the collateral. Assuming one of the alternative forms of legal comfort described above is delivered in the context of a structured finance transaction, Standard & Poor's will generally not require legal opinions on withholding tax. On a case-by-case basis, however, the issue of withholding tax may need to be addressed in a legal opinion. For example, opinions may be requested for new types of collateral or nonstandard contracts, or to the extent that the debtor or issuer of the collateral is located in a jurisdiction where the issue of withholding tax is not well settled. Permanent Establishment and Branch or Agency Many SPEs in international transactions are incorporated in zero or low-tax jurisdictions. They will, however, often own pools of assets located in high-tax jurisdictions. If the assets default, recoveries will have to be pursued in the local courts. Therefore, such transactions always carry a risk that the tax jurisdiction in which the assets are located will seek to confirm that the SPE, although located elsewhere, has a local permanent establishment, branch, or agency. This, in turn, may result in an SPE becoming taxable in that high tax jurisdiction. Almost invariably, the issue of whether a foreign corporation, such as the SPE, is to be deemed as taxable in a particular country will be determined by applying a combination of legal and practical tests. Consequently, Standard & Poor's does not expect that multijurisdictional transactions will have the benefit of legal opinions stating that, as an absolute matter of law, the SPE will not be held taxable in any particular jurisdiction. Standard & Poor's may, depending on the transaction, request a tax opinion that sets out the legal criteria that would result in the SPE becoming taxable in that jurisdiction and setting out the reasons why, under the transaction documents, such risk is removed or mitigated. Double-Tax Treaties Sometimes, transactions are structured to provide the SPE with the benefit of a double-tax treaty so that it can either receive amounts free of withholding tax or avoid being taxed in another jurisdiction. Depending on the treaty and transaction structure, the SPE may have a legal entitlement to the benefits of the treaty, or it may only have such entitlement if it has received confirmation or authorization from the relevant tax authority. In the former case, Standard & Poor's would expect to see an appropriately worded tax opinion confirming that the SPE may rely on the mandatory provisions of the relevant double-tax treaty. In the latter case, Standard & Poor's views it as impossible to determine with any degree of certainty the likelihood of obtaining the relevant administrative confirmation or authorization. Accordingly, no benefit will be given for the existence of the treaty until confirmation or authorization is actually granted. Stamp Duty or Registration Tax It may be that for the true sale of the securitized assets to have occurred or be opposable to (enforced against) third parties—as distinguished from binding only the transferor and the transferee—or be proved in court, payment of stamp duty or registration tax is required. Such cases fall into one of two categories: The duty or tax must be paid at the time of the transfer (or within a set period thereafter) and failure to make the payment cannot be remedied later or cannot be remedied without the involvement of a third-party outside of the SPE's control (such as the transferor, the transferor's insolvency officer, or the tax authority). In such circumstances, the transaction cannot be rated without the payment having been made. The duty or tax can be paid later (possibly with monetary penalties) and payment can be made by or on behalf of the SPE without the involvement of a third-party outside of the SPE's control. In those circumstances, Standard & Poor's will need to be satisfied that, at any point when the SPE may be required to make such payment, the SPE will have sufficient funds to do so. This can be done by funding a cash collateral account in the SPE's name that contains the necessary amounts, or by finding a suitably rated third-party provider of funds (such as the subordinated loan provider) who agrees to advance the necessary funds to the SPE when required. Alternatively, if Standard & Poor's is satisfied that the stamp duty or registration tax will not be payable until a certain date in the future, it may be acceptable for the SPE to accumulate a cash reserve from excess spread to set aside the necessary amounts prior to the date on which payment is needed. Secondary Tax Liability In some transactions, it is held to be necessary or useful for the SPE to be a subsidiary of another company (usually the transferor) rather than for it to be an orphan SPE. Care must be taken, however, that by having a shareholding link with an operating company the SPE does not, under the relevant tax legislation, become liable on a secondary basis for the taxes payable by that operating company. This would occur under some principles of "tax grouping". To the extent that, in the relevant jurisdiction, the SPE may become liable for another party's taxes, it will be a requirement of the transaction that the necessary steps to eliminate this liability are taken, or that the liability is quantified and that payment of such taxes would not make the SPE unable to meet in full its obligations on the rated notes. For more information on this topic, refer also to the following section of tax consolidation. Tax Consolidation Under the tax consolidation regime, the head company of a tax group is primarily liable for the tax liabilities of the consolidated group. If the head company fails to meet a tax liability on time, the subsidiary members of the consolidated group may become liable for all or part of that tax liability. The potential liability for the taxes of other group members, should the head company fail to pay, poses a significant risk to a securitization vehicle that is part of a consolidated group. The most obvious solution is to ensure that securitization vehicles are not members of any consolidated group, either by establishing them as orphan entities or by transferring sufficient equity to an unrelated entity to ensure that the securitization vehicle is not wholly owned within the consolidated group. Adequate protections must be in place to limit the tax risks where it is not possible or practical to deconsolidate the securitization vehicle. Tax-Sharing Agreements and Reasonable Allocation Tax laws offer protection in the form of a valid tax-sharing agreement (TSA). Under a TSA, each subsidiary member of the group may limit its potential liability to a reasonable allocation of the total amount of the consolidated group's tax liability. Although the Australian Taxation Office (ATO) has not issued a definitive statement on what would constitute a reasonable allocation of a group's tax liability for a securitization vehicle, its Receivables Policy, issued in April 2003, gives some indication that allocation on a stand-alone basis is reasonable. Standard & Poor's accepts that allocation of liability on a stand-alone basis is likely to be reasonable for an SPE. However, for a securitization trust in which the residual income beneficiary, not the trustee, is subject to tax on income derived by the trust, a reasonable allocation of liability should ideally be zero, reflecting the position that the trustee and the trust assets are separate from the beneficiary's group. Ultimately, if a securitization vehicle is, or will on election, become part of a consolidated tax group, Standard & Poor's will require a clear tax opinion that concludes that the securitization vehicle will have no greater liability for tax, as a consequence of consolidation, than it would have on a stand-alone basis. Practical Compliance Beyond the question of what is a reasonable allocation of tax liability, there are also practical issues regarding a TSA that need to be adequately addressed within the transaction structure. Satisfactory procedures must be in place to ensure that the TSA remains effective as the composition of the tax group changes. Similarly, a formal process is necessary to ensure that the securitization vehicle can provide a current copy of the TSA to the ATO on request, or ensure it is provided by the head entity. Finally, there must be provision for the securitization vehicle to maintain access to sufficient funds to pay its reasonable allocation of tax, rather than to pay it away to a head entity, which, Standard & Poor's may assume, becomes insolvent before it satisfies its tax obligations. Standard & Poor's recognizes that these practical issues are not peculiar to securitization vehicles and need to be resolved for the benefit of all consolidated group members that are seeking to rely on TSAs to limit their potential joint and several liability for unpaid group tax. Exposure Periods In analyzing the potential exposure associated with an election to consolidate, Standard & Poor's will look at tax risk over two periods. The first period is from the date of consolidation until the date on which the TSA is signed. The relevant legislation allows a decision to consolidate to be backdated to the beginning of the tax year, whereas a TSA cannot be effective prior to the date it is signed. Consequently, the date of consolidation may predate the TSA by a significant period. The second period is the period during which the subsidiary entity is subject to the TSA. This period will end with either the liquidation of the subsidiary entity or its deconsolidation from the tax group. During the first period, the subsidiary entity has joint and several liability for certain elements of the group's tax liability without the benefit of the nil allocation in the TSA. During the second period, the subsidiary entity is exposed to the risk of the TSA remaining valid, enforceable, and appropriately maintained (including being presented to the ATO within 14 days of request). Standard & Poor's Approach Standard & Poor's has considered a number of consolidation proposals. Each proposal is considered on its own merits, and Standard & Poor's approach has been largely driven by the rating on the head company, the rating on the debt issued by the SPE, the length of the two exposure periods, and the number and nature of the subsidiary entities involved. From its experience, Standard & Poor's has developed the following guidelines to assist in the analysis of the requirements for insolvency remoteness of a securitization vehicle issuing 'AAA' rated debt. If the head company is rated below 'BBB' or is unrated, Standard & Poor's will seek assurances regarding: Provisioning for the amount of any potential liability for the first period, the analysis of this financial risk will need to be supported by appropriate tax advice; How the TSA will be administered, including amendment for changes to the group structure, meeting the ATO presentation requirement, and reserving and funding of the allocation of tax payable by the SPE (if any). Administrative risk may be mitigated to some extent through the appropriate involvement of independent tax agents or independent trustees; The effectiveness of the TSA, including confirming that a nil or stand-alone allocation is reasonable. The analysis of this legal risk will need to be supported by appropriate legal opinion; and The length of time that the SPE will rely on the TSA to support its tax position. For head companies rated above 'BBB', Standard & Poor's assumes that the procedural aspects of a TSA will be managed, but will require appropriate assurances regarding: The amount of potential liability on the SPE for the first period; The reserving and funding of the allocation of tax payable by the SPE (if any); The effectiveness of the TSA, including confirming that a nil or stand-alone allocation is reasonable; and The length of time that the SPE will rely on the TSA to support its tax position. For head companies rated above 'AA-/A-1+', Standard & Poor's will assume that tax will be properly managed and accounted for, but may require assurance regarding the effectiveness of the TSA, including confirmation that a nil or standalone allocation is reasonable. These guidelines are intended to provide a framework for approaching tax consolidation for credit analysis and are by no means absolute. Standard & Poor's will continue to take a case-by-case approach to tax consolidation and the circumstances of any particular case that may dictate a need for additional assurances. LEGAL OPINIONS A Standard & Poor's rating is a credit opinion based on information provided by the issuer and its advisors. Standard & Poor's relies on representations made by issuers and managers that the information provided is true and accurate, and accepts no responsibility for verifying all aspects of the transaction. Standard & Poor's conducts only limited due diligence procedures on specific aspects of each transaction and may withhold a rating if it is not satisfied that the information provided is accurate. As a means of supporting the information provided by the issuer, it is usual to provide Standard & Poor's with copies of legal opinions issued in connection with the transaction. Opinions should be addressed to Standard & Poor's or include an express acknowledgement that copies of the opinions can be given to Standard & Poor's for the purpose of assigning a credit rating. Corporate And Enforceability Opinions Standard & Poor's relies on the transaction participants to ensure that all transaction documents (including all swaps, guarantees, and other forms of credit enhancement) are legally effective and address corporate enforceability matters. Corporate and enforceability opinions should include statements to the effect that: Each party is duly incorporated and existing with powers to enter into and deliver the documents and to exercise its rights and perform its obligations under the documents; All corporate action and other action required to authorize the execution and delivery of the documents and the performance of the obligations thereunder has been taken; The obligations of the party under the documents are legal, valid, binding, and enforceable in accordance with their terms; Each debt security will constitute a legal, valid, and binding obligation of the issuer enforceable in accordance with its terms in competent courts of the relevant jurisdiction; Each party is capable of suing and being sued in its corporate name; Each party cannot claim immunity for itself or its assets in any proceedings; The governing law chosen will be recognized; Any judgment obtained against a party will be recognized and enforceable; All acts, conditions, and approvals (as required for a party to lawfully enter into, exercise its rights, and comply with its obligations under the documents) ensure that its obligations are legal, valid, binding, and enforceable and make the documents admissible as evidence, have been applied and completed; and The execution, delivery, and performance by each party of its obligations under the documents will not conflict with, or result in the breach of, any of the terms or provisions of its memorandum and articles of association or the laws of the relevant jurisdiction. True Sale Opinion Often, a structured transaction involves a transfer of the underlying assets to the issuer of the rated securities. In exchange for the transfer of assets to the issuer, the seller of the assets will receive the proceeds of the issue of the rated securities. One of Standard & Poor's key concerns about an asset transfer is whether or not it constitutes a true sale. Even though a transfer of assets may be accomplished by means of a purchase agreement, the circumstances surrounding the transfer may lead a court to conclude that it was not a sale but a financing transaction, with the issuer making a secured loan to the seller. Such circumstances might include retention of rights by the seller with respect to the assets, or ability of the issuer to seek indemnification from the seller if the assets fail to perform satisfactorily. If the transfer of assets is recharacterized as secured financing, there is a risk that the assets could be affected by the insolvency and winding-up of the seller and interfere with payments on the rated securities. To provide Standard & Poor's with comfort that a transfer will not be recharacterized, true sale opinions may be required to the effect that: If the procedures contained in the purchase agreement are followed, title to the assets will pass to the issuer; If the seller is wound up, the assets transferred to the issuer will not constitute assets of the seller; and Title to the assets will pass to the issuer, notwithstanding that the seller or an affiliate of the seller, retains custody of the mortgage and the loan documents on trust for the issuer (where applicable). Security Interest Opinion In structured transactions, the issuer usually grants a charge over its assets to a security trustee. The security trustee holds the charge for the benefit of the holders of the rated securities and other secured creditors. Standard & Poor's typically requests opinions that address the effectiveness of charges and other aspects of the security trust, including that: The security trust is properly constituted; The security trust deed creates a floating and /or fixed charge over the charged property; The charge is registrable under the Corporations Act; The charge and all powers of attorney have been, or will be, registered; If the issuer is wound up, the charged property will be available to the security trustee for the benefit of the secured creditors; If the security trustee is wound up, the assets held by it will not be available to its general creditors but only to those creditors to whom debts were incurred in its capacity as security trustee; If the issuer is wound up, the assets covered by the charge will have to be applied to satisfy amounts owing to secured creditors in priority to unsecured creditors of the issuer; and The order of application of payments set out in the security trust deed is enforceable. Insolvency Opinions Insolvency laws allow certain transactions of an insolvent party to be set aside, or for payments by the insolvent party to be recovered by a liquidator. Although rated transactions are structured to minimize the risk that the issuer will become insolvent, Standard & Poor's requires legal opinions to the effect that the insolvency of the issuer or security trustee will not affect the rated securities. The specific opinions usually requested are as follows: In the event of the insolvency of the issuer or security trustee, the creation of the charges and the making of payments to the holders of the rated securities will not be an unfair preference; The issue of the rated securities does not constitute an unfair loan; The transactions effected by the documents are not uncommercial transactions; and There are no other provisions of the Corporations Act under which payments made by the issuer or security trustee may be set aside. Segregation Opinions In addition to the other opinions that may be required, when analyzing a segregated issuer, Standard & Poor's will require specific opinions confirming that the limited recourse provisions included in the transaction documents will be effective: To prevent secured creditors of one series of debt from seeking recourse against the assets attributable to another series; To prevent secured creditors of one series of debt making a claim against the issuer for any shortfall following realization of the assets attributable to that series; and To ensure that the issuer will not be considered insolvent if the assets available to the secured creditors of a series of debt are insufficient to fully repay that debt. For a more detailed explanation of the legal opinions that Standard & Poor's may want to see for a segregated series or issuer, refer to the earlier section on segregation. Tax Opinions An important issue for Standard & Poor's is the extent of the issuer's liability for tax and the resources available to it to cover its tax liability. Typically, the tax opinions that are required address the former. Examples of such opinions are: No ad valorem stamp duty is payable with respect to the documents or any aspect of the transaction, including the initial transfer of the assets or any subsequent perfection of title; The issuer is structured to be tax neutral, so that either it has no liability for tax, or its deductible expenses substantially offset its taxable income; and No withholding tax is payable on transaction payments, including any swaps entered by the issuer. For segregated issuers, multijurisdictional transactions, or situations in which tax consolidation