

short time after the issuance of investor certificates (within 120 days, except in the case of obligations having an original term of 30 years, in which case the period will not exceed two years). Any receivable so substituted is required to have characteristics substantially similar to the replaced receivable and will be at least as creditworthy as the replaced receivable.

In some cases, the affected receivable would be repurchased, with the purchase price applied as a payment on the affected receivable and passed-through to certificateholders.

#### *Interest Rate Swaps*

9. RBC-DR requests relief for both ratings dependent and non-ratings dependent swaps as described in Prohibited Transaction Exemption 2000-58 (65 FR 67765, November 13, 2000) (PTE 2000-58), subject to the same terms and conditions regarding interest rate swaps contained in that exemption.

#### **Conditions to Interest Rate Swaps**

10. Any class of certificates to which one or more swap agreements entered into by the trust applies will be acquired or held only by qualified plan investors. Qualified plan investors will be plan investors represented by an appropriate independent fiduciary that is qualified to analyze and understand the terms and conditions of any swap transaction relating to the class of certificates to be purchased and the effect such swap would have upon the credit rating of the certificates to which the swap relates.

#### *Yield Supplement Agreements*

11. A yield supplement agreement is a contract under which the trust makes a single cash payment to the contract provider in return for the contract provider promising to make certain payments to the trust in the event of market fluctuations in interest rates. For example, if a class of certificates promises an interest rate which is the greater of 7% per annum or LIBOR and LIBOR increases significantly, the yield supplement agreement might obligate the contract provider to pay to the trust the excess of LIBOR over 7% per annum. In some circumstances, the contract provider's obligation may be capped at a certain aggregate maximum dollar liability under the contract. Alternatively, a cap could be placed on the supplemental interest that would be paid to a securityholder from monies paid under the yield supplement agreement. For example, the yield supplement agreement would provide the difference between LIBOR and 7% but only to the extent that the

securityholder would be paid a total of 9% per annum. The interest to be paid by the contract provider to the trust under the yield supplement agreement is usually calculated based on a notional principal balance which may mirror the principal balances of those classes of certificates to which the yield supplement agreement relates or some other fixed amount. This notional amount will not exceed either: (i) The principal balance of the class of certificates to which such agreement or arrangement relates, or (ii) the portion of the principal balance of such class represented solely by those types of corpus or assets of the trust referred to in subsections III.B. (1), (2) and (3) of the proposed exemption. In all cases, the trust makes no payments other than the fixed purchase price for the yield supplement agreement and may, therefore, be distinguished from an interest rate swap agreement, notwithstanding that both types of agreements may use an International Swaps and Derivatives Association, Inc. ("ISDA") form of contract.

The Applicant notes that no "plan assets" within the meaning of the plan asset regulation (under 29 CFR 2510-3-101) are utilized in the purchase of the yield supplement agreement, as the sponsor or some other third party funds such arrangement with an up-front single-sum payment. The trust's only obligation is to receive payments from the counterparty if interest rate fluctuations require them under the terms of the contract and to pass them through to securityholders. The rating agencies examine the creditworthiness of the counterparty in a ratings dependent yield supplement agreement. The Applicant suggests that the relief for yield supplement agreements should be subject to the same conditions as for interest rate swaps, to the extent relevant. These conditions would include that the yield supplement agreement must be denominated in U.S. dollars, the agreement must not be leveraged, any changes in these conditions must be subject to the consent of the trustee, and the counterparty must be subject to the same eligibility requirements as an interest rate swap counterparty.

#### *Pre-Funding Accounts*

12. Although many transactions occur as described above, it is also common for other transactions to be structured using a pre-funding account and/or a capitalized interest account as described below.

The pre-funding period for any trust will be defined as the period beginning on the closing date and ending on the

earliest to occur of (i) The date on which the amount on deposit in the pre-funding account is less than a specified dollar amount, (ii) the date on which an event of default occurs under the related pooling and servicing agreement<sup>14</sup> or (iii) the date which is the later of three months or ninety days after the closing date. If pre-funding is used, the sponsor or originator will transfer to the trust on the closing date cash sufficient to purchase the receivables to be transferred after the closing date. During the pre-funding period, such cash and temporary investments, if any, made therewith will be held in a pre-funding account and used to purchase the additional receivables, the characteristics of which will be substantially similar to the characteristics of the receivables transferred to the trust on the closing date. Certain specificity and monitoring requirements must be met and will be disclosed in the pooling and servicing agreement and/or the prospectus<sup>15</sup> or private placement memorandum.<sup>16</sup>

#### *Capitalized Interest Accounts*

13. When a pre-funding account is used, the sponsor and/or originator may also transfer to the trust additional cash on the closing date, to be deposited in a capitalized interest account and used during the pre-funding period to compensate the certificateholders for any shortfall between the investment earnings on the pre-funding account and the pass-through interest rate payable under the certificates.

Because the certificates are supported by the receivables in the trust and the earnings on the pre-funding account, the capitalized interest account is needed when the investment earnings on the pre-funding account and the interest paid on the receivables are less than the interest payable on the certificates. The capitalized interest account funds are paid out periodically to the certificateholders as needed on distribution dates to support the pass-through rate. In addition, a portion of such funds may be returned to the

<sup>14</sup> The minimum dollar amount is generally the dollar amount below which it becomes too uneconomical to administer the pre-funding account. An event of default under the pooling and servicing agreement generally occurs when: (i) A breach of a covenant or a breach of a representation and warranty concerning the sponsor, the servicer, or certain other parties occurs which is not cured; (ii) a required payment to certificateholders is not made; or (iii) the servicer becomes insolvent.

<sup>15</sup> References to the term "prospectus" herein shall include any prospectus supplement related thereto, pursuant to which certificates are offered to investors.

<sup>16</sup> See the Proposal to PTE 2000-58 (August 23, 2000, 65 FR 51454, at page 51463) for a fuller explanation of pre-funding accounts.