Prime RMBS
Ireland
New Issue

# Mespil 1 RMBS Limited


## Analysts

Michael Greaney
+44 20 3530 1120
michael.greaney@fitchratings.com

Ketan Thaker
+44 20 3530 1392
ketan.thaker@fitchratings.com

**Surveillance**
Aksel Etingu
+44 20 3530 1186
aksel.etingu@fitchratings.com

**Operational Risk Group**
Mark Wilder
+44 20 3530 1122
mark.wilder@fitchratings.com


## Related Research

**Applicable Criteria**

- *EMEA Residential Mortgage Loss Criteria (February 2010)*
- *EMEA Residential Mortgage Loss Criteria Addendum - Ireland (February 2010)*
- *Counterparty Criteria for Structured Finance Transactions (October 2009)*
- *Criteria for Ratings Caps in Global Structured Finance Transactions (June 2010)*

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## Final Ratings

| Class | Amount (EURm) | Final Maturity | Rating | LSR | CE (%) | Outlook |
|---|---|---|---|---|---|---|
| A1 | 150.1 | August 2055 | AAsf | LS1 | 26.0 | Negative |
| A2 | 300.0 | August 2055 | AAsf | LS1 | 26.0 | Negative |
| A3 | 300.0 | August 2055 | AAsf | LS1 | 26.0 | Negative |
| Z | 250.0 | August 2055 | NRsf | n.a. | n.a. | n.a. |
| Total Issuance | 1,000.1 | | | | | |

Closing occurred on 21 December 2010. The transfer of the portfolio to the issuer occurred on 21 December 2010. The ratings assigned above are based on the portfolio information as of 31 October 2010, provided by the originators.

## Transaction Summary

This EUR750.1m rated transaction is the securitisation of owner-occupied and residential investment property loans originated by Haven Mortgages Limited (Haven, unrated), a wholly-owned subsidiary of EBS Building Society (EBS, rated 'BBB-'/Rating Watch Negative/'F3') and EBS. Fitch Ratings has assigned ratings to the notes issued by Mespil 1 RMBS Limited (Mespil or the issuer) as indicated above.

The ratings are based on the quality of the mortgage portfolio, available credit enhancement and the underwriting and servicing capabilities of the originators, as well as the financial and legal structure of the transaction. The ratings assigned to the notes address the ultimate repayment of principal by legal final maturity in August 2055 and the payment of interest in accordance with the terms and conditions of the notes.

### Key Rating Drivers

- **Rating Cap**: On 9 December 2010, Fitch downgraded Ireland's sovereign rating to 'BBB+'/Stable. It is Fitch's opinion that Ireland's sovereign risk has increased and may negatively affect the performance of RMBS transactions. Consequently, Fitch applied a 'AAsf' rating cap to all outstanding Irish structured finance transactions (see "*Fitch Downgrades 27 Irish RMBS Structured Finance Tranches, Affirms 8 Following Sovereign Downgrade*", dated 9 December 2010, for further details). Fitch's rating analysis showed that the class A notes could withstand loan losses at the 'AAAsf' level; however, the rating of the class A notes have been capped at 'AAsf', five notches above Ireland's sovereign rating.
- **Unhedged Interest Rate Risk**: The notes issued by Mespil pay a fixed interest rate and 67% of the portfolio is variable rate; the remaining 33% of fixed rate loans are expected to revert to a variable rate within 10 years of closing (with the vast majority of fixed rate loans expected to revert within three years of closing). At closing, the portfolio is yielding 3.65% p.a. and the weighted average (WA) fixed rate of the rated notes are paying 2.0% p.a.; consequently, the portfolio's yield is sufficient to service the interest cost of the notes. As the interest rate risk is unhedged, the transaction is exposed to potential interest rate shortfalls in a decreasing interest rate environment. To mitigate this risk, the servicer provides a covenant to not set the standard variable rate below 1.5% p.a. In addition, the product switch conditions only allow loans yielding greater than 2.5% p.a. to remain in the portfolio.
- **Provisioning for Defaults**: Due to the regulatory and legal environment in Ireland, the level of foreclosures is low for the given level of arrears. During the quarter ending September 2010, 81 repossession orders were granted by the

Irish courts. During the same period, 28,049 mortgage accounts were in arrears for greater than 180 days. Standard Irish RMBS transactions debit the principal deficiency ledger (PDL) when a loss is realised, ie upon the sale of a foreclosed property, which rarely occurs. Consequently, Mespil contains a mechanism in which 100% of the current balance of a loan will be debited on the relevant PDL once the relevant loan is 12 months or more in arrears. All proceeds from any enforcement will form the available revenue receipts.

- **Revolving Period:** This transaction has a one-year revolving period in which the originators may sell up to EUR100m of additional mortgages to the issuer, subject to certain conditions. Furthermore, the issuer may purchase further advances made to borrowers in the mortgage portfolio up to the call date on February 2016. The mortgage sale agreement contains certain asset conditions that limit the risk of lower credit quality loans being purchased by the issuer; as a consequence, Fitch has stressed the expected loss of the mortgage portfolio up to the limits contained in the mortgage sale agreement.
- **Broker Originations:** The mortgage portfolio comprises of broker-originated loans only. Fitch has reviewed historic arrears performance information segregated by vintage and origination channel (branch originations versus broker originations). The performance information provided showed that broker-originated loans had a higher level of arrears compared to branch-originated loans. Consequently, Fitch has increased the base default probability to account for the relative riskiness of broker-originated loans.
- **2006-2008 Vintages:** Approximately 71% of the portfolio was originated between 2006 and 2008. These vintages were originated in a benign economic environment at or close to the house price peak, just prior to the recession starting in 2008; consequently, borrowers from these vintages are suffering relatively worse than other borrowers. Arrears performance information for Irish mortgages shows that these vintages have the highest level of arrears compared to other origination vintages. Consequently, Fitch has increased the base default probability to account for the relative riskiness of 2006, 2007 and 2008 vintage loans.
- **Residential Investment Property (RIP) Loans:** Approximately 9% of the portfolio are RIP loans. The originators assessed the affordability for these loans using the estimated rental income of the property and the borrower's excess personal income. Due to the over-supply of properties in Ireland, RIP loans have been suffering from falling rents and worsening rental voids. These conditions have resulted in performance stresses for RIP loans. Consequently, Fitch has increased the default probability for RIP loans in the portfolio.
- **First-Time Buyers (FTBs):** 48% of the loans in the portfolio are to borrowers who have purchased a residential property for the first time. Fitch considers FTBs to be riskier due to the lack of a demonstrable track record of maintaining prior mortgage payments and has thus adjusted the default probability of such loans by 10%.

## Rating Sensitivity[1]

This section of the report provides an insight into the model-implied rating sensitivities to hypothetical changes in defaults and/or recoveries on the assets in a stressed environment. These increased defaults and/or recoveries on assets are relative to the WA foreclosure frequency (WAFF) of the mortgage portfolio (30.8% for the 'AAsf' rating scenario) and the WA recovery rate (WARR) of the mortgage pool (35.6% for the 'AAsf' rating scenario), respectively. They are assumed to occur immediately after closing of the transaction. The model-implied rating sensitivities

[1] These sensitivities only describe the model-implied impact of a change in one of the input variables. This is designed to provide information about the sensitivity of the rating to model assumptions. It should not be used as an indicator of possible future performance

based on such assumptions are only indicative of some of the potential outcomes and do not consider other risk factors to which the transaction is exposed.

## Rating Sensitivity to Defaults

**Rating Sensitivity to Default Rates**

| | Class A1 | Class A2 | Class A3 |
|---|---|---|---|
| Original rating | AAsf | AAsf | AAsf |
| 15% increase in default rates | AAsf | AAsf | AAsf |
| 30% increase in default rates | AAsf | AAsf | AAsf |

Source: Fitch

## Rating Sensitivity to Recovery Rates

**Rating Sensitivity to Recovery Rates**

| | Class A1 | Class A2 | Class A3 |
|---|---|---|---|
| Original rating | AAsf | AAsf | AAsf |
| 15% decrease in recovery rates | AAsf | AAsf | AAsf |
| 30% decrease in recovery rates | AAsf | AAsf | AAsf |

Source: Fitch

## Rating Sensitivity to Shifts in Multiple Factors

**Rating Sensitivity to Multiple Factors**

| | Class A1 | Class A2 | Class A3 |
|---|---|---|---|
| Original rating | AAsf | AAsf | AAsf |
| 15% increase in default rates and 15% decrease in recovery rates | AAsf | AAsf | AAsf |
| 30% increase in default rates and 30% decrease in recovery rates | AAsf | AAsf | A+sf |

Source: Fitch

## Model, Criteria Application and Data Adequacy

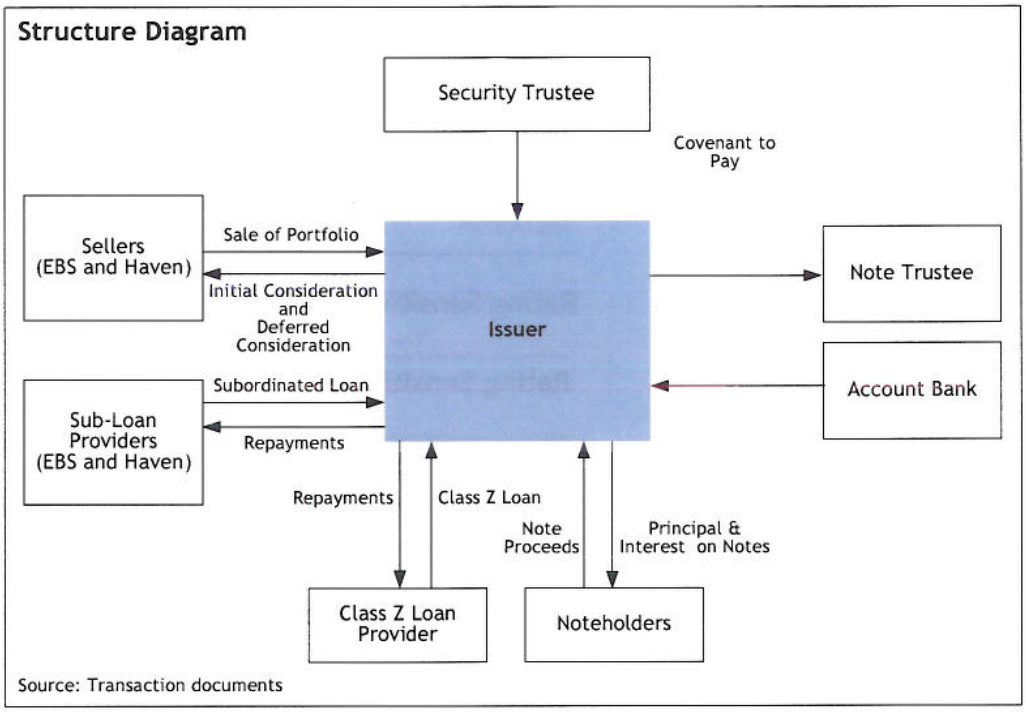
Fitch analyses the collateral for Irish residential transactions using a country-specific, loan-by-loan mortgage default model. The model subjects the mortgage loans to stresses based on Fitch's assessments of historical house price movements and mortgage defaults in Ireland. The agency's study showed that a borrower's loan-to-value (LTV), reflecting the size of their down-payment and their willingness to pay, and a borrower's debt-to-income ratio (DTI) – reflecting their ability to pay – to be the key determinants of default probability in Ireland.

EBS provided Fitch with a loan-by-loan data template; however, two data fields were missing. Despite these omissions, it is Fitch's opinion that the data available for the analysis is of good quality. It was unable to provide rental income information for all RIP loans in the portfolio. Fitch consequently assumed the relevant loans had the highest class 5 affordability measure. Furthermore, the agency has not received loan-level data in respect of borrowers' adverse credit history. However, EBS's and Haven's credit policies would not allow mortgage approvals to borrowers with past court judgements or past insolvencies. In addition, management at EBS and Haven have indicated to Fitch that instances where EBS/Haven has accepted borrowers with prior recorded arrears is rare (approximately less than 10 cases in the last five years); and in each these cases the borrower provided a satisfactory explanation of the arrears.

To determine the levels of credit enhancement needed to support Fitch's ratings, the agency simulated the transaction's cash flows, incorporating Fitch's cash flow stresses. The cash flow model was reviewed and tested to ensure that all key

structural features and cash flow mechanisms are correctly incorporated.

## Transaction and Legal Structure




### Legal Framework

Mespil is a private limited company incorporated under the laws of Ireland. On the closing date, the issuer acquired beneficial title to the collateral. As security for the payments of all monies payable with respect to the notes, Mespil entered into a deed of charge, creating security in favour of the trustee consisting of a first-ranking fixed charge over the issuer's rights, title, benefit and interest in and to the underlying collateral.

The transaction's structure is designed to ensure that any insolvency of the originator will not interrupt the timely payments of principal and interest to investors. The issuer has charged its rights, title and interest in and to the mortgages to the trustee. The issuer has no recourse to the originator except in limited circumstances.

### Representations and Warranties

The mortgage sale agreement contains representations and warranties given by the originators for the pool of mortgages as at the date of purchase. No search of title has been conducted by the issuer or the security trustee; rather, they relied on the following representations and warranties. If there is a breach of any of the representations or warranties, the seller will be required to repurchase the ineligible loan(s) in question.

The representations and warranties are, on the whole, standard for this type of transaction. Representations and warranties that relate to specific features within this transaction include the following.

- No borrower is an employee of the sellers.
- No loan has been in arrears other than technical arrears, (technical arrears means any arrears due to a non-credit related reason like incorrect or late set-up of direct debit mandates or minor arrears that are no more than 15% of the

scheduled mortgage payment).

- No loan has been approved by the relevant seller where the applicant is or has been subject to legal action for debt recovery, or is or has been declared bankrupt.

If a loan in the reference portfolio is found to be in breach of its representations and warranties, the seller must remove it by repurchase. The repurchase price payable will be an amount equal to the current balance on the loan plus all unpaid interest (including all accrued interest and arrears of interest) and any expenses payable on the loan.

### Sale of New Loans

Under the mortgage sale agreement, the issuer has agreed to acquire, and EBS/Haven has agreed to sell, new loans up to February 2012. The purchase of new loans will be subject to a number of conditions, namely the following:

- no event of default is continuing;
- the original LTV ratio of the portfolio after the sale of the new loans will not exceed the original LTV ratio of the portfolio at closing;
- the current LTV ratio of the portfolio after the sale of the new loans will not exceed the current LTV ratio of the portfolio at closing;
- the WA DTI ratio of the portfolio after the sale of the new loans will not exceed the WA DTI ratio of the portfolio at closing;
- the cumulative aggregate balance of all RIP loans purchased by the issuer will not exceed EUR10m;
- no new loan will contain an interest-only (IO) part;
- the yield of the new loans is at least 2.5% p.a.;
- the original and current LTV of the new loans is equal to or less than 90%;
- the sale of new loans will not result in the percentage of FTBs in the portfolio exceeding the percentage at closing plus 2%;
- no new loans will be purchased if the aggregate balance of loans more than 90 days in arrears (including loans that have been subject to an arrears capitalisation within 12 months of the test date) exceeds 3% of the outstanding balance;
- the cumulative aggregate balance of all new loans purchased by the issuer will not exceed EUR100m; and
- no new loans purchased have been in arrears (excluding technical arrears).

### Further Advances

Under the mortgage sale agreement, the issuer has agreed that EBS/Haven may make an offer to any borrower or accept an application for a further advance. The documentation and funding of the further advance will be the sole responsibility of EBS/Haven. The purchase of the further advance will be subject to a number of conditions, namely the following:

- no event of default is continuing;
- the original LTV ratio of the portfolio after the sale of the further advance will not exceed the original LTV ratio of the portfolio at closing;
- the current LTV ratio of the portfolio after the sale of the further advance will not exceed the current LTV ratio of the portfolio at closing;
- the WA DTI ratio of the portfolio after the sale of the further advance will not exceed the WA DTI ratio of the portfolio at closing;

- the yield of the further advance loans is at least 2.5% p.a.;
- each further advance loan complies with the loan warranties at the relevant sale date;
- the original and current LTV of the aggregated loans is equal to or less than 90%;
- no debit balance on the PDL and the general reserve fund is at its required amount; and
- no further advances will be purchased if the aggregate balance of loans more than 90 days in arrears (including loans that have been subject to an arrears capitalisation within 12 months of the test date) exceeds 5% of the outstanding balance.

If the seller elects not to sell a further advance to the issuer or the issuer is unable to fund the purchase of such further advance, the relevant seller may repurchase any loans secured by the property offered as security for the further advance. If the seller elects not to sell the further advance to the issuer or the issuer does not purchase the further advance, the relevant seller's interest in the loan and security shall be subordinated to the issuer's interest.

### Permitted Variations

A loan in which EBS/Haven has agreed to a request by a borrower to convert his or her loan into any other type of loan product offered by EBS/Haven may remain in the pool. The conversion of the loan is subject to certain conditions, including, no PDL debit outstanding, the reserve fund being fully funded, 90+ days arrears being below 5% of the outstanding pool and the proportion of IO loans (including part IO loans) in the outstanding pool being less than the proportion at closing plus 3%.

If EBS/Haven agrees to convert a loan contained in the reference portfolio that does not satisfy the conversion conditions, the issuer may sell to EBS/Haven the affected loan. The repurchase price payable will be an amount equal to the current balance on the loan plus all unpaid interest (including all accrued interest and arrears of interest) and any expenses payable on the loan.

### Disclaimer

For the avoidance of doubt, Fitch relies, in its credit analysis, on legal and/or tax opinions provided by transaction counsel. As Fitch has always made clear, Fitch does not provide legal and/or tax advice or confirm that the legal and/or tax opinions or any other transaction documents or any transaction structures are sufficient for any purpose. The disclaimer at the foot of this report makes it clear that this report does not constitute legal, tax and/or structuring advice from Fitch, and should not be used or interpreted as legal, tax and/or structuring advice from Fitch. Should readers of this report need legal, tax and/or structuring advice, they are urged to contact relevant advisers in the relevant jurisdictions.

## Asset Analysis

### Lender Adjustment

Fitch's base default probabilities assume that origination, underwriting and servicing practices and procedures are in line with those of a standard traditional Irish lender with market expertise, financial stability and relevant management experience.

As part of the analysis, the agency performs an operational review of the originator to assess the origination, underwriting and servicing capabilities of the seller. As a result of this review, if Fitch believes that origination, underwriting and servicing procedures are below market standard, an adjustment to the base default probabilities of the whole portfolio is warranted. The relevance of this adjustment is further sized by considering certain elements that cannot be factored into the analysis on a loan-by-loan basis, either because they are not available or because

they are only applicable on an aggregate basis.

Fitch has considered several strengths and concerns in its lender adjustment (see also section *Counterparty Risk/Servicer*). Among others, the main concerns are as follows.

1. No credit scorecard for underwriting.
2. The timeline from default to possession is lengthy. Under the Code of Conduct for Mortgage Arrears, EBS/Haven must wait at least twelve months from the time arrears first arise before applying to the courts to commence enforcement of any legal action for repossession of a property.
3. There has been a steep rise in three-months' plus arrears in the past 18 months, both for owner-occupied and RIP loans originated by EBS/Haven. The 2006, 2007 and 2008 vintages in particular are performing worse than older vintages. Around 71% of the portfolio belongs to the 2006, 2007 and 2008 vintages.

In Fitch's view, strengths to consider are as follows.

1. Good IT infrastructure resulting in origination and servicing processes being streamlined.
2. Underwriters conduct manual verification of income. Additional employer calls are conducted pre-offer and pre-completion to ensure borrower is still in employment.
3. All new purchases and remortgages require a full valuation.
4. In light of the current economic climate and the increasing level of arrears cases, EBS has conducted an internal review and implemented policies and procedures to handle the higher level of arrears cases.

Fitch has increased the base default probabilities in relation to all loans in the provisional pool, based on the considerations detailed above.

### Affordability

The WA DTI for the portfolio is 48.4% using Fitch's methodology. EBS/Haven's underwriting criteria for owner-occupied loans accepts loans with a maximum DTI between 45% and 60%, depending on the borrower's income. In assessing the affordability, EBS/Haven assumed debt repayments at a stressed rate of the European Central Bank (ECB) rate + 2.75%; however, given the recent low interest rates environment, EBS/Haven has applied a minimum stressed rate of 6% p.a. Furthermore, EBS/Haven determines the amount of additional debt the borrower may have outstanding and take this information into account in their affordability assessment.

For RIP loans, EBS was not able to provide all estimated rental income information. Consequently, Fitch conservatively assumed that these loans had the lowest interest coverage ratio (ICR), which is a class 5 affordability measure. The originators assessed the affordability for these loans using the estimated rental income of the property; if the estimated rental income was insufficient to service the debt, the underwriter assessed the borrower's excess personal income.

### Borrower Profile

**Self-employed:** 8.9% of the portfolio is to borrowers who are self-employed. For such borrowers, EBS/Haven checks financial information on trading for the past two years and, using audited accounts and/or certificates, establishes their capacity to repay the loan. Taxes paid (personal and business) and six months of bank statements are also checked. The income of these borrowers is taken only on a verified basis. Fitch considers self-employed borrowers to be riskier than employed borrowers, as the certainty of continuing employment for the former is lower.

Therefore, the probability of default for loans where the borrower is self-employed is adjusted higher.

**First-time buyers:** 48% of the portfolio is to borrowers who are FTBs of residential property. Fitch considers such borrowers to be more risky on account of the lack of a track record in servicing a home loan. Moreover, EBS/Haven's LTV criteria for FTBs is more aggressive than for other borrowers. Before April 2008, the maximum LTV allowed for such borrowers was 100%; after this date it was reduced to 92%. In comparison, the LTVs allowed for other borrowers have been 7%-9% lower. The default probability for such borrowers is increased by 10% in Fitch's analysis of the portfolio.

**Civil Servants:** 15.5% of the portfolio is lent to borrowers working for local and national government. Historically, civil servants were considered relatively low-risk borrowers as they tend to have stable employment and income. Considering the recent budget cuts in 2009/2010, civil servants have suffered pay-cuts and increased pension contribution obligations. No default probability adjustment was applied to civil servant borrowers.

### 2006-2008 Originations

Approximately 71% of the portfolio was originated between 2006 and 2008. Fitch's analysis of vintage arrears data from the originators and the rest of the Irish market show that the 2006-2008 vintages have the highest level of arrears compared to other vintages. Fitch has increased its base default probability expectation to account for the portfolio concentration to these vintages.

### Geographical Concentration

35% of the properties in the portfolio are located in Dublin. In comparison, Irish RMBS transactions typically have a Dublin concentration of between 40%-60%. The rest of the geographical distribution of properties is diverse, with Cork at 9% and 7% in Kildare, the next highest regional concentrations after Dublin.

### Illiquid Properties

6.6% of the loans in the portfolio are secured on properties that Fitch views as illiquid on account of their high value. Such high-value properties tend to experience higher loss severities, even in benign economic environments. Accordingly, Fitch has haircut the valuations for these high-value properties to account for the possibility of higher loss severity.

### Residential Investment Properties (RIP)

The mortgage portfolio comprises 9% RIP loans. EBS/Haven assesses affordability for RIP loans on a net disposable income basis, taking into account the financial commitments of the borrower on other lending. EBS/Haven does not require that the potential rental income from the investment property is sufficient to service the debt repayment obligations on the investment property; however, it does ensure that the borrowers have sufficient personal income to meet their repayment obligations.
Fitch views these loans as more likely to default than standard RIP loans, as EBS/Haven's's RIP loans may not yield sufficient income to service the debt; therefore, there is a greater reliance on capital appreciation to make this a viable investment, in addition to being a drain on the borrower's personal income.

Fitch has reviewed the historical arrears performance of EBS/Haven's RIP portfolio. The arrears levels for the RIP loans are higher than the owner-occupied loans, even though EBS/Haven historically lent on RIP loans at much lower LTVs. This supports Fitch's view that RIP loans are more sensitive than owner-occupied loans in a recessionary environment. In addition, many initiatives provided by the Irish government or financial regulator to help distressed borrowers have been focussed on lending against the borrower's primary residence, not on investment properties, thus further supports Fitch's view on the relative risk of RIP loans and owner-

occupied loans.

In its default analysis, Fitch increased the base default probability of RIP loans by 50%.

## Default Model Results

The following table illustrates the asset analysis results across different rating scenarios. It shows the default model output for the provisional mortgage portfolio.

**Fitch Default Model Output (Static Pool at Closing)**

| Rating level (%) | WAFF[a] | WARR[b] | MVD[c] |
|---|---|---|---|
| AAA | 36.6 | 31.6 | 59.1 |
| AA | 30.6 | 35.6 | 54.8 |
| A | 24.6 | 39.5 | 50.5 |
| BBB | 18.7 | 43.5 | 46.2 |

Recovery time (3.5 years for 'AAAsf' rating scenario): Interest accrued on contractual rate for 3.5 years at 'AAAsf'
Recovery cost: Variable - 3%; Fixed - EUR18,500
[a] Weighted-average foreclosure frequency
[b] Weighted-average recovery rate
[c] Market value decline
Source: Fitch

The transaction has a one-year revolving period in which EBS/Haven can sell further loans to Mespil, subject to the conditions described above in the *Transaction and Legal Structure* section. Fitch has stressed the portfolio assuming EBS/Haven will sell further loans (and further advances) up to the limits contained in the mortgage sale agreement. The agency has used these WAFF and WARR levels when modelling the transaction cash flows.

**Fitch Default Model Output (Dynamic Pool After Revolving Period)**

| Rating level (%) | WAFF[a] | WARR[b] | MVD[c] |
|---|---|---|---|
| AAA | 36.8 | 31.6 | 59.1 |
| AA | 30.8 | 35.6 | 54.8 |
| A | 24.8 | 39.5 | 50.5 |
| BBB | 18.8 | 43.5 | 46.2 |

Recovery time (3.5 years for 'AAAsf' rating scenario): Interest accrued on contractual rate for 3.5 years at 'AAAsf'
Recovery cost: Variable - 3%; Fixed - EUR18,500
[a] Weighted-average foreclosure frequency
[b] Weighted-average recovery rate
[c] Market value decline
Source: Fitch

## Code of Conduct on Mortgage Arrears (Mortgage Code)

The financial regulator has published the code of conduct on mortgage arrears, which took effect on 27 February 2009. The mortgage code covers mortgage lending activities to borrowers in respect to their principal private residence; therefore, lending secured against RIPs is outside the scope of the mortgage code. The mortgage code sets out what lenders must do when managing arrears cases; more specifically, the lender must explore alternative arrangements with the borrower, including arrears capitalisation, extension of loan term or changing mortgage type to reduce mortgage payments.

The lender cannot seek repossession of a property until all alternative arrangements with the borrower have been exhausted. In addition, the mortgage code states that the lender cannot commence repossession proceedings until at least twelve months after the borrower has entered into arrears. Even after the repossession proceedings have been initiated, the lender is expected to explore all possibilities of a repayment arrangement with the borrower. If such an arrangement is agreed with the borrower and the latter establishes a record of regular payments under the arrangement, the lender is expected to put the repossession proceedings on hold. In light of the above, the repossession proceedings can take longer than the typical one and a half years period. Fitch assumes a standard three-year

foreclosure period for Irish residential mortgages and has not made any additional stress in relation to the mortgage code. The agency will continue to monitor the impact of the mortgage code on this transaction.

The Irish financial regulator published a revised mortgage code, effective 1 January 2011. The revised mortgage code sets out in detail the responsibilities of Irish lenders regarding managing arrears cases. The restrictions on initiating legal proceedings still remain in place.

## Financial Structure and Cash Flow Modelling

At closing, the issuer issued three rated classes of mortgage-backed, fixed-rate notes.

The issuer applied the proceeds of the issue of the rated notes solely towards the purchase of the portfolio. The proceeds of the class Z loan provided by EBS were used to pay part of the purchase price that was not covered by the issue of the rated notes. EBS provided an additional subordinated loan to the issuer towards the funding of the initial cash reserve amount.

Interest on the rated notes is payable monthly in arrears on the 22 of each month, starting 22 February 2011.

Available funds will be applied to payments due under the notes according to a separate priority of payments.

### Credit Enhancement

#### *Subordination*

The rated class A1, A2, and A3 notes are supported by a subordinated class Z loan (25% of the total notes issued). The class Z PDL will be debited prior to drawings to the general reserve fund or prior to debiting the class A1, A2, and A3 PDLs.

#### *Reserve Fund*

A fully-funded reserve fund (1% of the total notes issued) provides credit enhancement to the rated notes. The reserve fund is non-amortising and gets replenished before the payment of interest on the class Z loan.

The reserve fund is available to help meet any deficit in available revenue receipts for payment of fees and interest due on the rated notes.

#### *Excess Spread*

To the extent available, excess spread, after meeting other senior expenses and interest on the relevant note tranche, will be available to replenish any debit balances that arise on the PDLs. However, over the course of the transaction, this may be eroded by delinquencies and defaulted loans in addition to prepayments, an effect that is compounded if higher-margin loans are affected.

Consequently, the agency has simulated potential margin compression when performing its cash flow analysis by conservatively assuming that the higher yielding loans default and prepay. The excess spread can also be affected adversely by the conversion of loans, which is mitigated by the condition that any conversion that remains in the portfolio will yield at least 2.5% p.a. Additionally, the servicer is obliged to maintain the standard variable rate (SVR) to at least 1.5%p.a.

### Principal to Pay Interest

If there is a shortfall in revenue funds to pay senior fees and interest on the rated notes, funds may be reallocated from principal receipts to cover the shortfall. The principal made available to cover these revenue deficits will be recorded on the PDL and is expected to be recouped from future revenue payments.

In its cash flow analysis, Fitch has modelled the principal draw mechanism, which is standard among Irish RMBS transactions.

### Notes Amortisation

During the revolving period, all principal receipts will be retained on the retained principal ledger to fund the purchase of new loans. After the revolving period, the transaction envisages sequential pay-down of notes, with class A1, class A2 and class A3 notes being paid down in that order.

The principal receipts available during a collection period, less any principal used to pay an interest shortfall on the notes, would be used to pay down principal on the notes outstanding.

**Key Parties**

**Issuer:** Mespil 1 RMBS Limited

**Originator/Seller:** EBS Building Society (EBS, rated 'BBB-'/Rating Watch Negative/'F3'), Haven Mortgages Limited

**Servicer:** EBS

**Trustee:** The Bank of New York Mellon, London Branch

**Account Bank:** Ulster Bank Ireland Limited (Ulster Bank, rated 'A+' Stable/'F1+')

**Subordinate Loan Provider:** EBS

**Principal Paying Agent:** The Bank of New York Mellon, London Branch

**Arranger:** J.P. Morgan

## Counterparty Risk

### Servicer

EBS (rated 'BBB-/Rating Watch Negative/F3') is the servicer to the EBS loans and Haven delegated the majority of servicing responsibilities to EBS at closing. Fitch performed an on-site operational review of EBS/Haven to assess, among other things, the lenders' origination and servicing capabilities. The agency recognises the importance of the servicing counterparty role for the transaction in terms of the underlying loan portfolio performance.

In common with other Irish RMBS transactions, no back-up servicer is appointed for this transaction. Upon a downgrade of EBS's Long-Term Issuer Default Rating (IDR) below 'BBB-', EBS is obliged to enter into a back-up servicing agreement within 60 days of the downgrade. With this arrangement, disruptions in the servicing of the portfolio are expected be minimised.

#### *Commingling Risk*

Payments made by borrowers will be credited into an existing collection account of EBS, held by Ulster Bank Ireland Limited (Ulster Bank, rated 'A+'/Stable/'F1+'); however, these funds will be commingled with funds received by other borrowers that do not form part of the mortgage portfolio. Notwithstanding, there is a daily payment from the collection account to the issuer account held by Ulster Bank in the name of the issuer.

Furthermore, EBS/Haven has declared a trust over the collection account, in favour of itself and the issuer and, as such, except for those funds to which EBS/Haven have a beneficial interest as sellers, these funds would not form the bankruptcy estate upon an insolvency event of EBS/Haven. The transaction legal opinion points out that the effectiveness of the trusts are subject to the ability of EBS/Haven and the issuer's ability to trace, in the relevant accounts, the assets that are subject to the trust.

To limit the counterparty credit risk of Ulster Bank, upon a downgrade below 'BBB-' or 'F2', the servicer will transfer the collections account to a suitably rated bank. This is compliant with Fitch's criteria on commingling risk (see "*Counterparty Criteria for Structured Finance Transactions*", published 22 October 2009 and available at www.fitchratings.com).

#### *Set-Off Risk*

Deposit set-off is minimal for this transaction. Firstly, Haven is not a deposit-taking institution; additionally, the loans in the Mespil portfolio were originated through the broker channel, resulting in the vast majority of borrowers not holding deposits with EBS. As at October 2010, the aggregate deposits held by EBS belonging to the borrowers in the portfolio stood at EUR0.8m, ie 0.08% of the portfolio. Therefore, deposit set-off risk is sized at 0.08% of the outstanding principal balance of notes at closing.

There are no loans in the portfolio made to the staff of EBS and Haven. The loan warranties in the mortgage sale agreement state that no borrower is an employee of the seller.

The total set-off amount Fitch assumed in its analysis is 0.08% of the principal

outstanding at closing. In its cash flow analysis, the agency assumed borrowers will exercise their set-off rights immediately after closing. This results in a 0.08% reduction in the collateral balance and a corresponding debit to the PDL, thus stressing the transaction upon the insolvency of the originator.

### Account Bank

Ulster Bank is the issuer and reserve account bank and it will be replaced, within 30 calendar days, should its Long-Term and Short-Term Rating fall below 'A' (or should it be placed on Rating Watch Negative while rated 'A') or 'F1'.

## Performance Analytics

On 9 December 2010, Fitch downgraded all three tranches from Emerald Mortgages No.4 Plc, originated by EBS Building Society.

Following the downgrade of Ireland's sovereign rating to 'BBB+'/Stable on 9 December 2010, the ratings of senior Irish structured finance tranches were capped at 'AAsf', five notches above Ireland's sovereign rating. The downgrades to the mezzanine and junior tranches were the result of a continued deterioration of asset performance and future expectations of high losses, due to continued house price depreciation.

As of the latest interest payment date in December 2010, loans three or more months in arrears increased to 4.6% of the outstanding collateral balance, from 3.0% a year ago (November 2009) for Emerald Mortgages No.4 Plc. Although these figures are comparable to other prime Irish RMBS transactions, the higher LTV profile of the pool is of concern, due to the higher probability of future default.

Even though arrears have increased, no loans have been foreclosed to date. This is a common theme across Irish RMBS, due to forbearance measures instigated by the Irish Government that are being adopted by all Irish lenders. The agency believes that ultimately the lender will either have to foreclose on some properties or restructure the loans. In either case, Fitch expects a loss to occur on the transaction.

## Related Research

| Publication[a] | |
|---|---|
| **General rating and structured finance criteria** | |
| Inside the Ratings: Comparing Structured Finance and Other Ratings | 14 July 2010 |
| Special-Purpose Vehicles in Structured Finance Transactions | 13 June 2006 |
| **Counterparty risk criteria** | |
| Counterparty criteria for Structured Finance Transactions | 22 October 2009 |
| Counterparty Criteria for Structured Finance Transactions: Derivative Addendum | 23 October 2009 |
| **Interest rate criteria** | |
| Interest Rate Risk in Structured Finance Transactions - Euribor | 1 November 2006 |
| Fitch Euribor Stresses | Monthly updated |
| **Country-specific criteria** | |
| EMEA Residential Mortgage Loss Criteria | 23 February 2010 |
| EMEA Residential Mortgage Loss Criteria Addendum - Ireland | 23 February 2010 |
| **Surveillance** | |
| European RMBS Surveillance: Post Issuance Reporting Standards | 19 November 2004 |
| Around the Houses - Quarterly European RMBS Performance Update | Quarterly |
| EMEA RMBS Q110 Update | 17 June 2010 |
| **Origination & servicing** | |
| European Residential Mortgage Originator Review Criteria | 9 July 2009 |
| Global Structured Finance Originator Evaluations | 3 December 2008 |
| Global Rating Criteria for Structured Finance Servicers | 16 August 2010 |

All the above research is available at www.fitchratings.com
[a] Criteria can be updated or amended: Readers should always make reference to the last criteria available at www.fitchratings.com
Source: Fitch

# Appendix A

## Transaction Comparison

| | Mespil |
|---|---|
| **Closing date** | **Dec 2010** |
| **Total issuance (EURm)** | **2,100.00** |
| **Rating (%)** | |
| AAA (%) | 76.0 |
| | |
| Initial reserve (% of initial balance) | 1.0 |
| Target reserve (% of current balance) | 1.0 |
| Liquidity | n.a. |
| | |
| **WAFF (%)** | |
| AAA | 36.6 |
| AA | 30.6 |
| A | 24.6 |
| BBB | 18.7 |
| BB | 12.7 |
| | |
| **WARR (%)** | |
| AAA | 31.6 |
| AA | 35.6 |
| A | 39.5 |
| BBB | 43.5 |
| BB | 47.3 |
| | |
| **Portfolio** | |
| Collateral balance (EUR) | 1,008.4 |
| Number of borrowers | 4,516 |
| Average current balance per borrower (EUR) | 223,294 |
| WA seasoning (months) | 18 |
| WA remaining term to maturity (months) | 352 |
| | |
| **(%)** | |
| WA interest rate | 3.7 |
| WA OLTV | 76.0 |
| WA DTI | 48.4 |
| Self-employed | 8.9 |
| Self-certified | 0.0 |
| RIP | 8.7 |
| Subsidised loans | 0.0 |
| WACLTV | 76.0 |
| WACLTV (indexed values) | 98.5 |
| WAOLTV >70%-80% | 18.9 |
| WAOLTV >80%-90% | 15.4 |
| WAOLTV >90%-100% | 27.1 |
| <30 days arrears | 0.0 |
| 30-60 days arrears | 0.0 |
| 60-90 days arrears | 0.0 |
| 90+ days in arrears | 0.0 |
| Interest only | 13.7 |
| Dublin | 35.1 |
| Illiquid properties | 6.6 |

Source: Transaction documents and Fitch

## Appendix B: Servicing and Origination

EBS (formerly Educational Building Society) had been established since 1935 and has become a key player in the Irish mortgage market; it has securitisation programmes of residential mortgages.

EBS has 100 outlets across Ireland, including 16 branches, 39 franchised agents and 45 agents and has been using a select group of intermediaries since 2005. The franchised agents are tied to EBS for all products, whereas the agents are only tied for mortgages and savings.

EBS's Broker business was established in July 2005 under the EBS brand. In early 2007, there were joint venture discussions with Britannia Building Society to launch a joint venture to establish a broker-only lender. In 2007, Britannia withdrew from the joint venture. Haven was set-up in December 2007 as a wholly-owned subsidiary of EBS. Haven has a 12.3% share of the Irish broker market.

### Origination

Originations through the intermediary channel pass through Haven, a wholly-owned subsidiary of EBS.

### Underwriting

Brokers input all the applicant's details via Haven's application forms. Once the applications are completed and back-up documentation collated, the forms and documents are sent to Haven's account manager (on-site). The account manager will assess the application and review the information provided. If the account manager is satisfied with the forms and documents, the application is forwarded to a centralised underwriting unit. The underwriting unit will perform all verification checks including calling the employer, checking the employer's business, checking the bank statements of the applicant, conducting Irish credit bureau checks and affordability calculations. Once the underwriter is satisfied with the application, an offer is made.

### Credit Authority

All loans must comply with the lending policy set out by EBS and approval mandates have been allocated to relevant members of staff to assess applications. Mandates are tiered and based on value, product type and risk. The level authorised is dependant on the individual underwriter's experience and knowledge, together with completion of pre-determined training requirements.

Mortgage loans to a borrower whose exposure to EBS is greater than EUR1,500,000 must be recommended by an underwriting manager (following referral from the underwriters) and approved by the Group CEO.

### Broker Performance Management

Haven conducts an annual appointment renewal process for every broker. The following terms are agreed annually: remuneration details; minimum required volumes; terms and conditions of appointment; and financial regulator appointment confirmation. In addition to the above, on an on-going basis, the account management team performs checks on the quality of the business introduced by every broker and assesses the broker's knowledge of Haven's products and processes.

### Property Valuation

Full valuations are completed for all loans via an approved panel of valuers. The valuation is typically instructed by the underwriter and the valuer must provide a full valuation for new purchases and remortgages, whereas a drive-by valuation is acceptable for further advances up to 90% LTV. Indexed valuations or automated valuation models are not utilised.

## Strengths and Concerns

Fitch has considered several strengths and concerns as part of the operational review and, among others, the main concerns are: (i) no documented limit on acceptable adverse credit limits (eg prior arrears) for underwriting; and (ii) no credit scorecard for underwriting.

In Fitch's view, strengths to consider of EBS/Haven's origination process include: (i) good IT infrastructure, resulting in streamlined origination and servicing processes; (ii) EBS having a robust underwriter monitoring regime, covered by branch and intermediary lending; and (iii) underwriters conduct manual verification of income. Additional employer calls are conducted pre-offer and pre-completion to ensure borrower is still in employment.

## Servicing

EBS will be responsible for the servicing of the mortgage loan portfolio.

Processing staff based in Dublin manage all general administration and arrears processing for the accounts. EBS is not a Fitch-rated servicer of residential mortgage loans. For more information on Fitch's servicer rating programme, see the report titled "*Global Rating Criteria for Structured Finance Servicers*", dated 13 August 2010.

## Primary Servicing

The arrears management currently performed by the group is fairly typical of market practices in Ireland.

The collection activity of loans up to three payments in arrears is standard for each account and all missed payments are subjected to a standard collection procedure.

Arrears management commences at the earliest opportunity, with unpaid direct debits triggering initial contact with the borrower by letter. This process is followed each month until telephone contact is made at two- to six-months past due. Once contact is established, EBS requests the borrower complete an income and expenditure form in order to fully understand the borrower's financial situation. EBS will consider the borrower's situation and may offer a restructuring of the loan (ie conversion to IO or reduction in the interest rate). EBS will offer an arrears capitalisation if the borrower has made six consecutive contractual mortgage payments.

## Special Servicing

Litigation is the last resort for Irish lenders. At six months down, if the borrower is not cooperating, legal action may be initiated. The mortgage code restricts lenders from initiating legal proceedings against cooperating borrowers within twelve months of their entering into arrears. The whole process can take up to three years, due to the length of time required to obtain orders for possession and the ability of the borrower to challenge repossession proceedings.

Following repossession, the property is marketed with a view to obtaining the best possible sale price; however, auction sales may be considered. Recovery of any shortfall in debt may be passed to external agents, depending on value and customer circumstances.

## Back-up Servicing

There is no named back-up servicer on this transaction.

# Appendix C: Transaction Overview

## Mespil 1 RMBS Limited

Ireland/RMBS

### Capital Structure

| Class | Rating | Size (%) | Size (EURm) | CE (%) | Interest rate (%) | PMT freq | Maturity | Margin | ISIN |
|---|---|---|---|---|---|---|---|---|---|
| A1 | AAsf | 15.0 | 150.1 | 26.0 | 2.5 | Monthly | August 2055 | n.a. | XS0562903038 |
| A2 | AAsf | 30.0 | 300.0 | 26.0 | 2.0 | Monthly | August 2055 | n.a. | XS0562903202 |
| A3 | AAsf | 30.0 | 300.0 | 26.0 | 1.75 | Monthly | August 2055 | n.a. | XS0562903467 |

| | |
|---|---|
| **Cash reserve** | 1.0 |
| **Liquidity** | n.a. |
| **First interest payment date** | Feb 2011 |
| **Call date** | Feb 2016 |
| **Swap** | n.a. |

Source: Transaction documents

### Key Information

| | |
|---|---|
| **Closing date** | December 2010 |
| **Country of assets** | Ireland |
| **Country of SPV** | Ireland |
| **Structure** | Pass-through |
| **Settlement** | |
| **Listing** | Irish Stock Exchange |
| **Analysts** | |
| Michael Greaney | +44 20 3530 1120 |
| Ketan Thaker | +44 20 3530 1392 |

| **Parties** | |
|---|---|
| **Seller/originator** | EBS Building Society/Haven Mortgages Limited |
| **Servicer** | EBS Building Society |
| **Arranger** | J.P. Morgan |
| **Joint lead managers** | |
| **Principal paying agent** | The Bank of New York Mellon |
| **Cash collection account provider** | Ulster Bank Ireland Limited |
| **Swap counterparty** | n.a. |
| **Cap counterparty** | n.a. |

Source: Transaction documents

### Summary

**Rating drivers**

- The sovereign rating of Ireland is 'BBB+'/Stable. Due to the economic stress in the Irish economy and concerns about the resulting stress in the Irish mortgage market. Fitch applied a rating cap of 'AAsf', five notches above the rating of Ireland.
- The interest rate risk between the fixed rate notes and the floating rate loans is unhedged. Fitch modelled the transaction cashflows using the standard interest rate stresses.
- The transaction has a one-year revolving period in which the seller can sell further loans to the issuer, subject to certain conditions. Fitch has stressed the expected loss of the mortgage portfolio up to the limits contained in the mortgage sale agreement.
- The mortgage portfolio contains loans originated through the broker channel. Historic arrears performance information shows that broker-originated loans have higher level of arrears compared to branch-originated loans. Fitch increased the probability of default for the broker-originated loans.
- 71% of the mortgage portfolio was originated between 2006-2008. These vintages have suffered the most during the economic downturn. Fitch increased the probability of default for the 2006-2008 vintages to account for the increase default expectations.

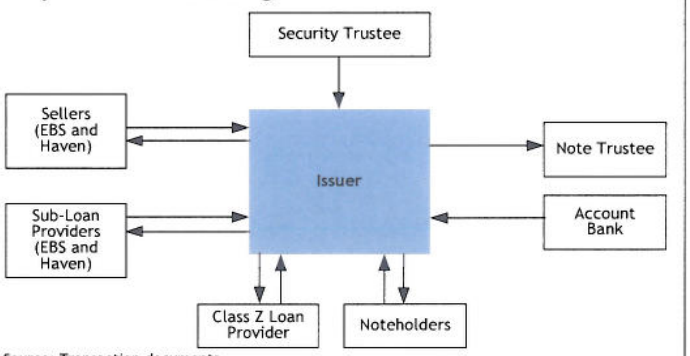
Source: Fitch

### Fitch Default Model Output

| Rating level | AAA | AA | A | BBB |
|---|---|---|---|---|
| WAFF (%) | 36.6 | 30.6 | 24.6 | 18.7 |
| WARR (%) | 31.6 | 35.6 | 39.5 | 43.5 |
| WALS (%) | 81.4 | 77.4 | 72.6 | 68.6 |
| WA MVD (%) | 59.1 | 54.8 | 50.5 | 46.2 |

Source: Fitch

### Simplified Structure Diagram




Source: Transaction documents

### Collateral Summary

**Provisional pool characteristics (as of 31 October 2010)**

| | | | |
|---|---|---|---|
| Original principal balance (EURm) | 1,008.4 | **Regional concentration (%)** | |
| Current principal balance (EURm) | 1,008.4 | Dublin | 35.1 |
| Average current loan per borrower (EURm) | 223,294 | Commuter region[a] | 21.7 |
| Number of borrowers | 4,516 | Other regions | 43.2 |
| Number of loans | 4,516 | | |
| Seasoning (years) | 1.5 | | |
| Loan-to-value (LTV) (%) | | | |
| WA OLTV | 76.0 | Loans in principal grace period (%) | |
| WA CLTV | 76.0 | Lien position | |
| | | First ranking | 100.00 |
| Mortgage characteristics | | | |
| Government subsidised (%) | 0.00 | Payments | |
| RIP (%) | 8.7 | Payment frequency | Monthly |
| | | Payment method | Direct debit |
| Interest rate type | | Performing loans (%) | 100.0 |
| Floating-rate loans (%) | 67.0 | WA DTI (%) | 48.4 |
| | | Employment status (% of self-employed) | 8.9 |
| WA interest rate (%) | 3.2 | | |

[a] Louth, Meath, Kildare, Wicklow
Source: Transaction documents

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