# Paragon Auto and Secured Finance (No. 1) PLC

**ABS — UK**

**CLOSING DATE:**
November 23, 2000

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## TRANSACTION IN BRIEF

| Class | Rating | Amount | Coupon |
|---|---|---|---|
| A | **Aaa** | €285,000,000 | 3 Month EURIBOR + 34 bps |
| B | **A2** | £16,580,000 | 3 Month LIBOR + 80 bps |
| C | **Baa2** | £9,750,000 | 3 Month LIBOR + 180 bps |

### Structure Summary

| | |
|---|---|
| Structure Type: | Senior/subordinate mixed receivable (Car Finance Contracts and Secured Loans) backed Notes with credit enhancement facility |
| Final Legal Maturity: | November 2031 |
| Note Payment Dates: | 15th day of February, May, August, and November, commencing on February 15th, 2001 |
| The Issuer: | Paragon Auto and Secured Finance (No. 1) PLC |
| Originator/Seller: | Paragon Personal Finance Limited (PPF), Paragon Car Finance Limited (PCF) |
| Transaction Bank Account: | National Westminster Bank Plc (**Aa2**, **Prime-1**) |
| Issuer Deposit Bank: | Société Générale (**Aa3**, **Prime-1**) |
| Servicer: | Paragon Finance PLC |
| Receivables Trustee: | Citicorp Trustee Company Limited |
| Interest Rate and Basis Swap: | Société Générale (**Aa3**, **Prime-1**) |
| Lead Manager: | Société Générale (**Aa3**, **Prime-1)** |

### Credit Support

| | |
|---|---|
| Cash Reserve: | 3% of Initial Note Balance |
| Over-Collateralisation: | 0% building up to 1.5% of Initial Balance |
| Subordinated Tranches: | 8.5% Class B, 5% Class C |

### Provisional Portfolio Summary

| | |
|---|---|
| As at: | 29 September 2000 |
| Contract Types: | Car Finance Contracts, Secured Loans |
| Number of Contracts: | 18,365 |
| Current Balance: | £152,367,060 |
| Contract Interest Types: | Fixed and floating interest rate |
| Collateral Type: | Secured Loans and Car Finance Contracts |

| | Car Finance Contracts | Secured Loans |
|---|---|---|
| Weighted Average Interest Rate: | 13.81% | 12.5% |
| Weighted Average Remaining Term: | 48 months | 9.9 years |
| Weighted Average Seasoning: | 4.7 months | 5.9 months |
| Weighted Average LTV | n/a | 84.5% |
| Average Current Balance Outstanding: | £6,657.22 | £11,527.37 |

## RATING OPINION

Moody's has assigned the following long-term ratings to the debt issuance of Paragon Auto and Secured Finance (No. 1) PLC ("PASF"):

**Aaa** to the €285,000,000 Class A Floating Rate Notes due 2031;
**A2** to the £16,580,000 Class B Floating Rate Notes due 2031; and
**Baa2** to the £9,750,000 Class C Floating Rate Notes due 2031

The rating of the Senior Notes is based upon:

- Moody's analysis of the quality and expected loss characteristics of the asset pool on which the Notes are secured;
- The selection of eligibility criteria for both types of loan contracts (secured loan and auto loan);
- The credit enhancement provided by Excess Spread, Over-Collateralisation, the Cash Reserve, and the Subordination of the Class B and Class C Notes;
- The benefit of an interest rate swap with Société Générale (**Aa3**, **Prime-1**), which hedges the interest rate risk between the fixed rate interest from the asset pool and the floating rate coupons on the Notes;
- The benefit of a swap with Société Générale (**Aa3**, **Prime-1**), which hedges the basis risk between LIBOR and EURIBOR payments of the Class A Notes and the exchange of currency;
- Moody's assessment of Paragon's operations, controls, and procedures for both underwriting and subsequent servicing of the asset pool; and
- Moody's assessment of the transaction's legal structure and tax analysis.

Moody's ratings of the Class B and Class C Notes is based on the same as that set out above for the Senior Notes, except for taking into account the subordinated positions in the transaction of each of the two classes of Notes.

The ratings of the Notes reflect the timely payment of interest and the ultimate payment of principal on the Notes on or before the legal final maturity.

## RATING SUMMARY

### Structure

The Issuer is a special purpose vehicle incorporated under the laws of England and is a wholly owned subsidiary of the Paragon Group of Companies. The activities of the Issuer are restricted to ensure that it is bankruptcy remote.

The Issuer will fund the purchase of the assets by issuing the Class A, Class B, and Class C Notes.

The Class A Notes pay quarterly coupons at a fixed spread over EURIBOR and the Class B and Class C Notes pay quarterly coupons at a fixed spread over LIBOR, with the first payment being made February 15th 2001.

The Issuer's beneficial interest in the English receivables will be an equitable interest only. No notification of the assignment and transfer of the receivables and collateral shall be made to the receivables' debtors. The Trustee will therefore need, via the power of attorney granted by Paragon, to give notice to obligors of the transfer of the receivables. In the case of an insolvency of Paragon, the Note Trustee will still be able to give notice to the borrowers requiring them to make payments directly to the Receivables Trustee's account.

In relation to the Scottish auto receivables (25.7% of provisional auto portfolio balance) the transfer of the receivables must be done using a legal perfection of assets, which could be subject to Stamp Duty — the risk being mitigated through an additional reserve provided specifically for this purpose. Paragon will apply for adjudication from Stamp Duty, seeking a Section 42 Finance Act 1930 intra group exemption.[1] If this application is adjudicated "Stamped without Duty" then the additional reserve can be removed.

1 See "An Overview of U.K. Stamp Duty and it's Impact on U.K. Securitization Transactions", *Moody's Investors Service*, Special Report August 10, 2000.

## Collateral

The mixed asset receivables pool consists of secured loans made to individuals and auto loans made to individuals, partnerships and corporate bodies in England, Wales, and Scotland. The ratio of auto loans to secured loans will at close be approximately 52%/48%, but may change during the four year revolving period. This volatility of asset mixture is however mitigated by a 75% cap on the level of auto loans, and a 50% cap on the level of secured loans, which can be sold to the transaction during the substitution period.

The assets included in the portfolio will comprise: the benefit of loans to individuals in the United Kingdom secured by second or subsequent-ranking charges over residential property in England, Wales and Scotland, together with all security relating to those loans. The assets also include the benefit of motor vehicle hire purchase agreements and motor vehicle conditional sale agreements; and the beneficial ownership of the vehicles that are concerned.

One of the weaknesses of this transaction, in relation to the assets, is the limited amount of performance data available, due to the fact that the Car Finance business has only been originating loans since 1997, and the Secured Loan business has only been originating loans since July of 1999. Arrears for both pools have been low, but this is based on limited experience. The level of enhancements available to the transaction however, mitigates these risks.

## Substitution

The criteria which must be met for substitution of further assets during the 4 year substitution period include:

1. During the four year substitution period, new receivables can only be added if there is no unremedied loss present on the Principal Deficiency Ledger;
2. If the Cash Reserve Account is fully funded;
3. If losses in the Secured Loans pool are less than 10% or, the amount of interest that is due to be generated by the pool divided by the actual amount of interest generated must be equal to/or greater than 95% (or such other percentages as may be agreed with Moody's from time to time);
4. If losses on the Car Finance Contracts are less than 4% or the amount of interest that is due to be generated by the pool divided by the actual amount of interest generated must be equal to/or greater than 96% (or such other percentages as may be agreed with Moody's from time to time);
5. The ratio of Car Finance Contracts to Secured Loans must remain within the respective caps (Car Finance Contracts maximum 75% of Outstanding Balance, and Secured Loans, maximum 50% of Outstanding Balance);
6. A minimum mortgage margin of 5% must be maintained for the entire portfolio of secured loans; and
7. A minimum margin over the swap rate of 5% must be achieved for any pool of substituted car finance assets.

These triggers assist in mitigating the risk that the volatility of the pool may worsen due to substitution. If such deterioration is detected, then the substitution period will end and the transaction will amortise.

## Call Option

The Issuer may redeem all of the Notes on, or after, any Interest Payment Date falling in November 2004 or upon which the principal amount of the Transaction Receivables is less than or equal to 20% of the initial principal amount outstanding of the receivables.

## Principal Paying Interest

The Issuer has the ability to use principal receipts to meet its senior expenses obligations and interest due under the Class A Notes (but not the Class B and/or Class C Notes). This provides substantial protection for investors in the Class A Notes against a gradual deterioration in the arrears performance of the portfolio. Moody's believes, however, that the fact that the Issuer is unable to use principal receipts to pay interest on the Class B or Class C Notes exposes the Class B and Class C Notes to greater liquidity risk.

## HEDGING

### Interest Rate Risk

On the Closing Date, the Issuer will enter into hedging arrangements with Société Générale as Swap Counterparty to hedge any Secured Loans which are fixed rate, capped rate or collared rate Loans and all Portfolio Car Finance Contracts that are acquired on the Closing Date. These asset pool cashflows are at fixed rates of interest, whereas the Notes pay fixed spreads over three month EURIBOR (for the Class A Notes) and three month LIBOR (for the Class B and Class C Notes). The fixed/floating interest rate mismatch is hedged by the Issuer entering into hedging arrangements which may consist of swaps, caps or floors with Société Générale, such that the Issuer will agree to pay amounts calculated by reference to a fixed rate based on the amortising Principal Balance of Receivables.

### Basis Risk

The Issuer will also enter into hedging arrangements with Société Générale to hedge the currency and interest rate exposure arising from the fact that subscription amounts for the Class A Notes will be paid by investors in Euro, but the consideration for the purchase by the Issuer of Portfolio Assets will be in Sterling. And further, payments from Obligors in relation to the Portfolio Assets will be in Sterling, but the payment obligations of the Issuer in relation to interest and principal on the Class A Notes will be denominated in Euro and, in the case of interest, calculated by reference to EURIBOR.

## CREDIT ENHANCEMENT

Investors in the Notes are protected from the effect of credit losses on the pool in a number of ways.

### Excess Spread

The first layer of protection for investors in the Notes is the Excess Spread in the transaction, which is the difference between:

1. The income receivable by the Issuer under the auto loans, and the secured loans, and its other investments and swap arrangements; and
2. The amounts of interest due by the Issuer on account of its various ongoing costs and expenses and under the Notes and swap arrangements.

The credit enhancement value of Excess Spread also depends on the timing of principal losses. Excess Spread is available on a "use it or lose it" basis and so, if not used to top up the Cash Reserve Account, to reduce the Principal Deficiencies Ledger or build up over-collateralisation, it is paid back to Paragon via the Subordinated Loan and other profit extraction mechanisms. This might occur before losses on the portfolio have shown through. The value of the Excess Spread was assessed by Moody's under a variety of adverse conditions, including high pre-payment scenarios.

### Cash Reserve Account/Over-Collateralisation

The second layer of protection which is available for Investors in the Notes is the Cash Reserve Account. On closing, Paragon will make a Subordinated Loan to the Issuer of an amount equal to 3% of the aggregate initial principal amount outstanding of the Notes to be issued.

This loan will be paid into a designated account ("Cash Reserve Account") to be used to provide on-going liquidity support, to meet senior expenses and to provide credit support to the transaction. Any amounts utilised will be replenished from future excess spread in the transaction.

On each Interest Payment Date, revenue of the Issuer in excess of the amounts required to pay or provide for priority payments will be applied to replenish the Cash Reserve Account to the Required Amount, and/or to build up the transaction's Over-Collateralisation (the second layer of Investor protection) to a level of 1.5% of the Initial Notes Balance.

## Principal Deficiency Ledger

If on any Interest Payment Date the Issuer has insufficient income to meet its Priority Expenses (which include Servicer's fees, Note Trustee, and Class A Note interest due on that date) it will use principal receipts to meet the deficiency and debit the amount to the Principal Deficiency Ledger.

For both Auto Loans and Secured Loans (the Receivables) 100% of accounts in arrears will be written off to the Principal Deficiency Ledger at twelve months' delinquency, if not previously written off.

To the extent that on any subsequent Interest Payment Date there is income available to the Issuer in excess of the amount then required to meet Priority Expenses, it will be applied in reducing or extinguishing any such debit.

## Principal and Interest Subordination

The Class A Notes rank first in point of security. The Class B Notes will be subordinated to the Class A Notes. The Class C Notes will be subordinated to the Class B Notes in point of security. Accordingly, upon enforcement of the security and after utilising the transaction's Over-Collateralisation and the transaction Reserve Account, losses will be borne first by the Class C Noteholders then by the Class B Noteholders and then by the Class A Noteholders.

### *Pro Rata B and C Note Interest Trigger*

The pro-rata paydown of the Class B and Class C Notes will be subject to triggers, including separate arrears triggers for secured and auto loans.

## VAT Grouping

In common with other Paragon transactions rated by Moody's, but unlike the vast majority of UK MBS transactions, the Issuer is grouped with the rest of the Paragon Group for VAT purposes. The VAT grouping means that services or goods provided between members of the VAT group are not subject to VAT (which would otherwise be payable on servicing fees); but, as a consequence, each member of the VAT group is jointly and severally liable for VAT liabilities of all other members of that group. A long standing arrangement is in place to mitigate this risk:

A Trust Account, held in the name of Morgan Guaranty Trust Company of New York (**Aa3**, **Prime-1**) ("MGT") as trustee with National Westminster Bank Plc (**Aa2**, **Prime-1**), can be used by any member of the VAT group to meet group VAT liabilities should PFPLC (which, as representative member, is primarily liable for group VAT) fail to do so. PFPLC must maintain a minimum balance in the Trust Account equal to the greater of (1) £120,000, (2) 1.2 times the actual VAT liability for the Paragon VAT Group in the last two accounting periods, or (3) 1.2 times the sum of the estimated VAT liabilities of the Paragon VAT Group for the current and next succeeding accounting periods.

If PFPLC fails to pay VAT due by it, or fails to maintain the minimum balance in the Trust Account), the Issuer will automatically be de-grouped; on a de-grouping, no new VAT liabilities will arise but any that exist remain. The VAT authority cannot prevent a company from degrouping, but it must be given 90 days' prior notice.

## SERVICER

Moody's believes that Paragon Finance PLC has a well-developed servicing business with a track record of successful collections and arrears management in the United Kingdom. There is no stand-by servicer in place, however the level of credit enhancement and liquidity provisions present in the transaction gives Moody's comfort that this risk is sufficiently mitigated.

Moody's will monitor the transaction and the ratings of the Notes on an ongoing basis until the Notes mature. The monitoring will include the review of the monthly servicing reports and other performance data including supporting ratings, together with discussions with the servicer and other parties, as Moody's considers appropriate.

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