July 2010

Repurchase Agreements – Benefits, Risks and Controls

A repurchase agreement (repo) is an agreement between two parties whereby one party sells the other a security at a specified price with a commitment to buy the security back at a fixed time and price. Maturities can vary from overnight to a year, with the longer-maturity repos commonly referred to as "term" repos.

BofA Global Capital Management typically enters into "tri-party" repos on behalf of its clients. In these arrangements, a custodian bank acts as an intermediary between the two parties and creates operational efficiencies by providing, among other things, standardized legal documentation, transaction settlement services and collateral segregation. Repos are widely used by the managers of money market funds because they generally offer three distinct benefits:

- Liquidity – Repos provide the ability to invest cash overnight, making them a critical component in the effort to manage liquidity. The size of the market and supply of repos provide for strong liquidity.
- Yield Advantage – Repos generally provide additional yield as compared to traditional money market instruments, such as Treasury bills, time deposits or agency discount notes. The yield advantage depends on such factors as the repo's maturity date and the credit quality of the repo's collateral.
- Flexibility – The principal amount of repos can be adjusted up or down as fund cash flows dictate, and transactions and can be conducted late in the day.

Repos generally are designed such that the fund takes possession of the collateral if a counterparty fails to meet its obligations under the repo. While counterparty selection and collateral requirements provide the fund protection, repos remain subject to counterparty risk.

If a counterparty defaults, a loss may be realized on the sale of the underlying security to the extent that the proceeds from the sale and accrued interest of the security are less than the resale price, including interest, provided in the repurchase agreement. Moreover, should a counterparty declare bankruptcy or become insolvent, a fund may incur delays and costs in selling the underlying security, or it may suffer a loss of principal and interest. This could occur, for example, if a fund is treated as an unsecured creditor and is required to return the underlying collateral to the counterparty or its assigns.

BofA Global Capital Management seeks to mitigate counterparty risk by providing credit and portfolio oversight through controls and reviews that include:

- Credit Review Process – BofA Global Capital Management's assessment of credit quality includes:
    - Counterparty Evaluations – All counterparties must be vetted and approved by the firm's credit review committee; if the counterparty is not on the approved list, BofA Global Capital Management will not execute a repurchase agreement with it (even if it posts strong collateral).

- Collateral Requirements – BofA Global Capital Management's collateral requirements are designed to protect fund investors should a counterparty default:
  - The value of the security must be equal to or greater than the value of the repo itself (up to 105% of the repo value depending on the collateral's credit quality).
  - Repo positions must have first claim and priority lien on the collateral, which is held by third party custodian banks.

- Operating Controls – BofA Global Capital Management conducts periodic reviews to verify that the requirements noted above are met and that the appropriate legal agreements are in place to protect a fund's interests in the collateral.

BofA Global Capital Management believes its credit review process, collateral requirements and operating controls are reasonably designed to manage counterparty risk associated with repos. As such, BofA Global Capital Management continues to believe that repos are an appropriate investment vehicle for the funds it manages.

BofA Advisors, LLC
100 Federal Street, Boston, MA 02110
www.bofacapital.com

INT-25/60607-0710 10/AR34M2T5