**BEFORE THE EXTERNAL REVIEW PANEL OF THE**
**DETERMINATIONS COMMITTEE OF THE**
**INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC.**

**DC ISSUE: 2009-100901**

**Has a Restructuring Credit Event occurred with respect to CEMEX, S.A.B. de C.V.?**

# BRIEF IN FAVOR OF THE "YES" ANSWER TO THE REVIEWABLE QUESTION


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## TABLE OF EXHIBITS

Pertinent excerpts from the following documents that were available to the Determinations Committee are included in the "Appendix of Exhibits to the Brief in Favor of the 'Yes' Answer to the Reviewable Question," submitted with this brief. Citations to these documents are in the form "(Ex. A at ___)," and the Exhibit designation for each referenced document is as set forth below.

| **Date** | **Document** | **Exhibit** |
|---|---|---|
| May 31, 2005 | Credit Agreement among Cemex, S.A.B. de C.V., L.C., as Borrower, Cemex Mexico, S.A.B. de C.V., L.C., Empresas Tolteca de Mexico, S.A. de C.V., L.C., as Guarantors, the several Lenders part thereto, and others (signature pages omitted); together with the Fifth Amendment to Credit Agreement dated January 22, 2009. | A |
| January 21, 2009 | Standard & Poor's Report | B |
| March 6, 2009 | Bloomberg Article, *Cemex Said to Delay $500 Million Bond Sale After Drop* | C |
| March 9, 2009 | CEMEX Press Release | D |
| March 10, 2009 | Fitch Report | E |
| March 10, 2009 | Standard & Poor's Report | F |
| April 2009 | Conditional Waiver and Extension Agreement, CEMEX, S.A.B de C.V. Form 20-F, and Amendment dated June 29, 2009 (signature pages redacted). | G |
| June 30, 2009 | Auditors' Statement, CEMEX, S.A.B de C.V. Form 20-F at F-2 | H |
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| Date | Document | Exhibit |
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| June 30, 2009 | CEMEX Press Release | J |
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| October 2009 | Bloomberg Screen Shots:<br>• CEMEX CDS Pricing<br>• CEMEX Equity (US) Pricing vs. SPX<br>• CEMEX Description of May 2005 Facility<br>• CEMEX Amendment History of May 2005 Facility | O |

## INTRODUCTION

On August 14, 2009, CEMEX, S.A.B. de C.V. ("Cemex") consummated a transaction meeting all of the criteria for a Restructuring Credit Event. Prior to that date, Cemex faced "unsustainable" challenges in meeting its debt obligations, the vast majority of which were scheduled to mature from 2009 to 2011. (Ex. M at 4).[1] In June 2009, Cemex's auditors had warned that, absent a successful restructuring of the company's debt, there was "substantial doubt about [Cemex's] ability to continue as a going concern." (Ex. I at 10). The two credit rating agencies covering Cemex had also downgraded it many notches below investment grade as a result of concerns about Cemex's deteriorating financial condition, its ability to repay near-term debts, and a cash-flow shortfall of between $1.2 and $2 billion.

Cemex spent much of the first half of 2009 seeking to stop the decay in its creditworthiness and financial condition by: *first*, attempting an unsuccessful $500 million debt offering that it abandoned on March 5, 2009; *second*, on March 9, 2009, engaging its lenders in extended negotiations to restructure its debt obligations; and *third,* in April 2009, securing an agreement, and later an extension of that agreement, to defer payments on various obligations of its subsidiary coming due during 2009. Finally, on August 14, 2009, Cemex consummated a restructuring to extend the maturity dates for approximately $15 billion in debt, including over 90% of Cemex's bank debt obligations on a consolidated basis (the "August 14 Transaction"). (Ex. L at 4, 19). The August 14 Transaction is a "Restructuring" under Section 4.7(a) of the 2003 ISDA Credit Derivatives Definitions,[2] because one or more of Cemex's Obligations were

[1] Relevant excerpts of the materials cited herein are annexed to the Appendix of Exhibits submitted with this brief.

[2] The 2003 ISDA Credit Derivatives Definitions (as published by the International Swaps and Derivatives Association, Inc. ("ISDA")), as supplemented by the 2009 ISDA Credit Derivatives Determinations Committees, Auction Settlement and Restructuring Supplement to the 2003 ISDA Credit Derivatives Definitions (the "2003

amended to effect a "postponement or other deferral of a date or dates for . . . the payment of principal or premium."

The August 14 Transaction does not fall within the exception set forth in Section 4.7(b)(iii) of the 2003 Definitions, which excludes restructurings that do "not directly or indirectly result from a deterioration in the creditworthiness or financial condition of the Reference Entity." Ten years ago, when the Restructuring definition first appeared in the 1999 Definitions,[3] the Practice Notes stated that Section 4.7(b)(iii) "was drafted to provide a limited exception" to the occurrence of a Restructuring Credit Event and that "in the vast majority of cases" "it will be clear" when this exception applies. *See* 1999 Definitions, at ix. While there may be cases where the applicability of the exception in Section 4.7(b)(iii) is not clear, this is not one of them. Cemex's extension of the dates for payment on its obligations was caused by a "deterioration in [its] creditworthiness or financial condition." 2003 Definitions § 4.7(b)(iii). An indirect causal connection would suffice, but the causal connection between the Cemex restructuring and Cemex's financial deterioration was direct and indisputable.

The External Review Panel should therefore answer the Reviewable Question in the affirmative, as that is the "better answer." Credit Derivatives Determinations Committees Rules ("DC Rules") § 4.6(c)(ii).

## BACKGROUND

Cemex is a holding company that, acting through its operating subsidiaries, is one of the three largest cement makers in the world. (Ex. N at S-1). Cemex issues or incurs debt directly at

(continued…)

Definitions"). Capitalized terms not defined herein, unless otherwise indicated herein, shall have the meanings ascribed to them in the 2003 Definitions.

[3] The 1999 ISDA Credit Derivatives Definitions (the "1999 Definitions") are the predecessor to the 2003 Definitions. The relevant provisions of the 1999 Restructuring definition were not changed by the 2003 Definitions.

the holding company level or through various operating subsidiaries, but has no significant assets of its own other than its ownership of stock in its subsidiaries. (*Id.* at S-22). As of December 31, 2008, Cemex had, on a consolidated basis, outstanding debt of approximately $18.78 billion. (Ex. I at 3, 124).

The market trades credit default swaps on Cemex itself and, accordingly, for purposes of this analysis, Cemex is the Reference Entity. Among Cemex's indebtedness is a syndicated credit facility, dated May 31, 2005, with aggregate commitments in the amount of $1.2 billion (the "May 2005 Facility") that is a direct obligation of Cemex and, as set forth in detail in Part I.C of this brief, satisfies the required category and characteristics of an "Obligation" of the Reference Entity under the 2003 Definitions (Physical Settlement Matrix, Latin America Corporate BL). (Ex. A). The May 2005 Facility, as well as other obligations of Cemex,[4] contain cross default provisions that, among other things, are triggered upon a payment default of *any* material indebtedness of Cemex or its subsidiaries. (Ex. A at 40-41). Accordingly, if Cemex, or a subsidiary of Cemex, had failed to pay obligations coming due in 2009, an event of default would have occurred and Cemex's lenders could have accelerated Cemex's obligations under the May 2005 Facility.

Against this backdrop, in early March 2009, Cemex indefinitely postponed its attempt to issue a bond offering. (Exs. C, F). A few days later, on March 9, 2009, Cemex announced that it was entering into discussions with its lenders to renegotiate its debt and extend debt maturities.

[4] Included among Cemex's outstanding debt obligations are the following debts that also qualify as "Obligations" for purposes of determining whether a Restructuring has occurred with respect to Cemex: (i) a revolving credit facility, dated as of June 6, 2005, with aggregate commitments in the amount of $700 million; (ii) a credit facility, dated as of January 27, 2009, with aggregate commitments of $437.5 million; (iii) Maturity Loan A, dated as of December 31, 2008, for which New Sunward Holding BV is the borrower and Cemex is the guarantor, with aggregate commitments of $525 million; (iv) Maturity Loan B, dated as of December 31, 2008, for which New Sunward Holding BV is the borrower and Cemex is the guarantor, with aggregate commitments of $525 million; and (v) a credit facility, dated as of June 27, 2005, for which New Sunward Holding BV is the borrower and Cemex is the guarantor, with aggregate commitments in the amount of $700 million. (Ex. A, Am. No. 5 to May 2005 Facility)).

(Exs. D, E). On April 16, 2009, Cemex, together with a wholly owned Cemex subsidiary, CEMEX Espana, S.A., entered into a Conditional Waiver and Extension Agreement (the "Extension Agreement") with its bank lenders, pursuant to which the lenders agreed to extend until June 24, 2009 all scheduled principal payment obligations—a total amount of approximately $1.116 billion. (Ex. G at 1, 64-65). In June 2009, Cemex sought and secured a further agreement with its lenders to defer the expiration of the Extension Agreement through July 31, 2009. (Ex. G). Then, on August 14, 2009, Cemex entered into the August 14 Transaction with its lenders, which extended until February 2014 the final maturity of a total of approximately $15 billion in outstanding debt including Cemex's obligations under the May 2005 Facility. (Ex. K; Ex. M at 1; Ex. O)

On October 9, 2009, ISDA was notified of a General Interest Question related to the August 14 Transaction: "Has a Restructuring Credit Event occurred with respect to CEMEX, S.A.B. de C.V.?" The Issue was accepted by two Convened DC Members and considered by a Convened DC Committee that voted on November 6, 2009, but was unable to achieve the requisite supermajority under Section 3.1(b) of the DC Rules. The issue was thereafter referred for External Review. Because neither Presented Position in the DC garnered more than 60% of the votes of the Convened DC Members, the Reviewable Question here will be decided on the basis of a majority vote of the members of the External Review Panel as to which Position is the "better answer." DC Rules § 4.6(d)(ii).

## ARGUMENT

### I. UNDER THE PLAIN LANGUAGE OF THE DEFINITION, A RESTRUCTURING CREDIT EVENT HAS OCCURRED WITH RESPECT TO CEMEX

Under the 2003 Definitions, a "Restructuring" is defined in pertinent part as, among other events, a "postponement or other deferral of a date or dates for either (A) the payment or accrual of interest or (B) the payment of principal or premium" with respect to "one or more Obligations." 2003 Definitions § 4.7(a)(iii). An event that meets the criteria of Section 4.7(a) is a Restructuring unless it fits within one of three exceptions, including that the event "does not directly or indirectly result from a deterioration in the creditworthiness or financial condition of the Reference Entity." 2003 Definitions § 4.7(b)(iii).

The two principal issues discussed by the DC with respect to the Reviewable Question were (1) whether Cemex's Obligations were modified to postpone the due dates for the payment of principal in a manner not provided for under the terms of the Obligations, or were discharged and replaced with new debt; and (2) if the exception in Section 4.7(b)(iii) is applicable because the restructuring of Cemex's Obligations did not result directly or indirectly from a deterioration in Cemex's creditworthiness or financial condition. The record is clear and unambiguous: (1) Cemex's Obligations were indeed amended, not discharged and replaced by the issuance of new obligations; and (2) the restructuring of its Obligations resulted "directly or indirectly" from a deterioration in its creditworthiness or financial condition. A Restructuring Credit Event has therefore occurred with respect to Cemex.

### A. The Payment of Principal on Cemex's Obligations Has Been Postponed

Cemex *postponed* the dates for the payment of principal under the May 2005 Facility and did not discharge and replace this Obligation with new debt. The May 2005 Facility, as amended by the August 14 Transaction, continues to be in full force and effect. Cemex has itself so stated repeatedly in its regulatory filings, which make clear that the August 14 Transaction "extended" the maturities on Cemex's "existing" facilities:

- "The financing agreement ***extends the maturities*** of approximately U.S.$15.0 billion in syndicated and bilateral bank and private placement obligations, providing for a semi-annual amortization schedule, with a final maturity of approximately U.S.$6.8 billion on February 14, 2014." (Ex. N at S-3, emphasis added).

- "***[O]ur existing bank facilities that are included in the financing agreement*** bear interest at either a base rate plus an applicable margin, a LIBOR rate plus an applicable margin or a Euribor rate plus an applicable margin." (*Id.* at S-16, emphasis added).

- "*Interest rate.* The base rates, LIBOR rates and Euribor ***rates applicable to our existing facilities remain in place***, and under the financing agreement the applicable margin for each facility is set at 4.5% per annum …." (*Id.* at S-86, emphasis added).

- "*Maturity*. The maturity of all our financing agreement facilities has been ***extended*** until February 14, 2014." (*Id.*, emphasis added).

- "We and certain of our subsidiaries were obligors as borrowers or guarantors under our various credit facilities and other indebtedness prior to the effectiveness of the financing agreement. ***These obligations continue to be in full force and effect under the financing agreement***." (*Id.* at S-85, emphasis added).

Cemex's August 14, 2009 press release announcing the financing agreement similarly referred to a "revised maturity schedule" and specified that it "extends" the maturities of approximately $15 billion of debt. (Ex. K).

Further, a June 29, 2009 amendment to the Extension Agreement, which extended the repayment dates for $1.116 billion of principal, also expressly contemplated a future "restructuring" of Cemex's obligations under its "existing facilities":

- The first page of the amendment refers to a "draft termsheet setting out the terms of a master override agreement in relation ***to the restructuring of the Existing Facilities*** (the 'Master Override Agreement') circulated to the Lenders (the 'Termsheet')." (Ex. G).

- The amendment defined the "Master Override Agreement" to "mean[] the master override agreement to be entered into between, *inter alia*, CEMEX Parent, CEMEX España, certain Lenders and any other relevant Financial Creditor ***in respect of the restructuring of the Existing Facilities*** and any other relevant facilities and financial accommodation provided by other Financial Creditors of the Group." (Ex. G at 3).

In a conference call announcing the August 14 Transaction, Cemex was also asked specifically whether the agreement created a new facility and repaid the old agreements, and it answered: "No." (Ex. M at 5). Cemex stated on that same call that the August 14 Transaction "*extends* the final maturities of $15 billion to February 2014" pursuant to a "*revised* maturity schedule." (Ex. M at 1, 4 (emphasis added)). Although Cemex's executives on the call referred to the

August 14 Transaction, without elaboration, as a "refinancing," what Cemex *labeled* the August 14 Transaction is irrelevant; what matters is what the August 14 Transaction *did*. And, as Cemex made clear in the Prospectus, in the Extension Agreement, and in announcing the August 14 Transaction, the August 14 Transaction extended the maturities of Cemex's existing facilities.

Cemex also disclosed that *all* of its lenders had agreed to the August 14 Transaction. (Ex. M at 5). Where a debtor issues or incurs new debt to pay off existing indebtedness, the consent of existing lenders whose debt is being repaid is, in most cases, not required. Only when that debt is to remain outstanding, but with amended repayment or security terms, is the consent of the lenders generally required. Accordingly, that Cemex obtained the approval of its lenders for the August 14 Transaction is further evidence that this Transaction effected a restructuring of Cemex's obligations under the May 2005 Facility, not a repayment of that facility.

The August 14 Transaction is therefore "a postponement or other deferral of a date or dates for . . . the payment of principal or premium" of an Obligation, rather than the issuance of new debt, and is therefore a "Restructuring" under Section 4.7(a). 2003 Definitions § 4.7(a)(iii).

### B. The Exception Provided for in Section 4.7(b)(iii) Does Not Apply.

The August 14 Transaction does not fit within the exception provided for in Section 4.7(b)(iii). Under the plain language of this provision, the occurrence of, agreement to, or announcement of an event that meets the criteria of Section 4.7(a) is a Restructuring unless it "does not directly or indirectly result from a deterioration in the creditworthiness or financial condition of the Reference Entity." 2003 Definitions § 4.7(b)(iii).

#### 1. Section 4.7(b)(iii) Is a Limited Exception

The definition of Restructuring was first formally adopted in the 1999 Definitions, and the exception set forth in Section 4.7(b)(iii) has remained unchanged since. The Introduction to the 1999 Definitions makes clear that Section 4.7(b)(iii) provides a "limited exception" to Section 4.7(a) and provides an instructive explanation of the intent underlying this exception:

> [Section 4.7(b)(iii)] should be read with its purpose in mind, namely to protect against triggering a Restructuring where a Reference Entity's credit quality has improved and it negotiates new terms with its lenders or where its credit quality has stayed the same but improving market conditions permit the negotiation of more favorable terms.

1999 Definitions, Practice Notes at viii ("Restructuring Credit Event"). The Practice Notes state further that "in the vast majority of cases" application of this exception will be straightforward because "it will be clear when the creditworthiness of a Reference Entity has improved or remained the same." *Id.* at viii-ix.

The use of the formulation "directly or indirectly," in particular, conveys that an event will *not* fall within the narrow exception provided by Section 4.7(b)(iii) so long as it can be said to result indirectly from a deterioration in the Reference Entity's creditworthiness or financial condition. The Practice Notes gave an example of just how the concept of "indirect" causation operates to limit the scope of the exception in this regard:

> [F]or example, the agreement to new terms on a distressed borrowing, even after long period of negotiations, would constitute a Restructuring under a credit derivative transaction in effect when such negotiations began despite any improvement in the creditworthiness of the Reference Entity while the new terms were being negotiated or as a result of the new, presumably more favorable, terms. In this case, the eventual agreement to new terms is best viewed as an indirect result of the original distressed situation and not as the negotiation of more favorable terms by a Reference Entity whose credit quality has improved.

*Id.* In this example from the Practice Notes, even though the new terms of a borrowing are preceded by an *improvement* in the Reference Entity's creditworthiness—brought about by the very fact that the distressed Reference Entity is re-negotiating its obligations—for purposes of applying the definition, the new terms are at least *indirectly* tied to a deterioration in the

Reference Entity's creditworthiness; and so, under Sections 4.7(a) and 4.7(b), a Restructuring Credit Event is triggered.

The use of the formulation "direct or indirect" frequently plays such a clarifying role in contracts and statutes. "Direct" causation conveys a comparatively rigorous concept of proximate causation. *See* BLACK'S LAW DICTIONARY 250 (9th ed. 2009) ("proximate cause" is "[a] cause that *directly* produces an event and without which the event would not have occurred") (emphasis added). But where, as in the definition of Restructuring, a causal link can also be established "indirectly," the requisite connection is much more readily established under New York law, which is the Relevant Governing Law here. *See* DC Rules §§ 2.1(c), 6. Indirect causation is a purposely broad notion that embraces not only proximate, or "direct," causation, but also a practical or reasonable causal link between an event and a result.[5]

The "direct or indirect" formulation in Section 4.7(b)(iii) thus provides important clarity to the market in applying the definition of Restructuring. The basic distinction that this provision makes is between amendments to credit agreements that result from the Reference Entity having *improved or unchanged* creditworthiness or financial condition, and those where the Reference Entity has restructured, either directly or indirectly, because of a deterioration in its creditworthiness or financial condition. Under the principles set out above, that is not a difficult

[5] *See, e.g.*, *Cerati v. Berrios*, 61 A.D.3d 915, 915 (2d Dep't 2009) ("'Proving that the defendant's violation was an 'indirect cause' [of an injury] does not require the same amount of proof as proximate cause in common-law negligence, but requires a practical or reasonable connection between the statutory or regulatory violation and the injury.'"); *O'Connell v. Kavanagh*, 231 A.D.2d 29, 30 (1st Dep't 1997) (construing provision for damages in the event that an "injury . . . occurs directly or indirectly" from a third party's conduct in violation of statute; "it is not necessary that the plaintiff show the same degree of proximate causal connection which we are accustomed to in the field of negligence" under this provision because the notion of "indirect" causation imposes liability where there is "any practical or reasonable connection between a violation and the injury"); *Gittelson v. Mutual Life Ins. Co. of N.Y.*, 266 A.D. 141, 142-46 (1st Dep't 1943) (construing provision in life insurance contract for double indemnity in the event that death results "directly or indirectly" from disease; this "exception is broader than the exceptions in [other policies] and is made so by the use of the word 'indirectly'"); *In re Gillespie*, 263 A.D. 175, 177-78 (3d Dep't 1942) (regulation providing that "persons or corporations shall not directly or indirectly" be subject to expense by reason of changing the route of a power line, "is a broad provision and indicates a clear purpose to include all items of expense or damage that might reasonably be charged to the change").

determination to make so long as there is at least a reasonable causal connection between an event listed in Section 4.7(a) and a deterioration in a Reference Entity's creditworthiness or financial condition.

### 2. Cemex's Restructuring Was a *Direct* Result of the Deterioration in its Creditworthiness or Financial Condition

The plain terms of Section 4.7(b)(iii), when considered in light of the clear statements in the Practice Notes as to its limited applicability, compel the conclusion that this exception is not applicable here. The restructuring by Cemex of its Obligations was *directly* caused by the deterioration in Cemex's creditworthiness or financial condition; and, under Section 4.7(b)(iii), even an "indirect" causal connection would suffice to make the August 14 Transaction a Restructuring. The following facts and circumstances show the linkage required by Section 4.7(b)(iii) and hence demonstrate the inapplicability of this exception:

***First***, Cemex's auditors stated that Cemex's ability to pay its existing debt obligations that matured in 2009 would depend upon successfully restructuring that debt. (Ex. H). In Cemex's 20-F for 2008, Cemex's auditors stated that, as of June 30, 2009, *there was substantial doubt about Cemex's ability to function as a "going concern" if Cemex did not successfully restructure its debt in 2009*:

> [T]he Company's ability to fulfill its short and long-term debt obligations that mature in 2009 is dependent on successfully completing their refinancing in 2009. This raises substantial doubt about the Company's ability to continue as a going concern.

(*Id.* at F-1.) The auditors further directly linked this threat to Cemex's creditworthiness and continuing existence to its deteriorating financial condition:

> During 2008 and continuing into 2009, CEMEX's liquidity position and operating performance is being negatively affected by adverse economic and industry conditions in several of its main operating segments brought on by the downturn in the global construction industry and the global credit market crisis. As of

> December 31, 2008, CEMEX had approximately Ps95,270 (US$6,934) of debt [in millions] (including the current portion of long-term debt) due in the following 12 months in accordance with the terms of the debt instruments. In addition, CEMEX had an excess of current liabilities over assets of approximately Ps84,542 (US$6,153) [also in millions]. These factors raise substantial doubt concerning CEMEX's ability to continue operating as a going concern. ***The ability of CEMEX to continue operating as a going concern is dependent upon its ability to complete the bank refinancing described in the following paragraphs or otherwise obtain additional debt or equity financial resources to pay CEMEX's obligations as they become due.***

(Ex. I at F-61 (emphasis added)). Cemex itself similarly stated in an SEC disclosure covering the period from November 2008 through June 2009 that, "[o]ur access to funds to meet our obligations is, in part, dependent on the ultimate outcome of the bank debt refinancing process" and repeated the auditors' qualification that there was "substantial doubt about [Cemex's] ability to continue as a going concern." (*Id.* at 10).

***Second***, Cemex stated in its 20-F filed on June 30, 2009 that it had entered into agreements with its lenders to postpone the due date for $1.116 billion in principal payment obligations that had been due between March 24, 2009 and July 31, 2009, "to give us time to negotiate a broader debt refinancing," but that "[w]e cannot provide assurance that we will be able to enter into a refinancing plan to replace the Conditional Waiver and Extension Agreement prior to July 31, 2009 or to extend the Conditional Waiver and Extension Agreement to a later date." (*Id.* at 3). Further, "[i]f the Conditional Waiver and Extension Agreement expires or terminates, and we are unable to pay the extended amounts and any accelerated amounts, this would trigger a payment default under the relevant bank facilities, which would trigger defaults under other debt of ours." (*Id.*) Cemex also stated that its revolving credit facilities had been fully drawn and that it could face liquidity problems and then "may not be able to comply with our upcoming principal payment maturities under our indebtedness." (*Id.* at 4).

***Third***, before Cemex entered into negotiations to restructure its debt, the two rating agencies that follow it—Fitch and Standard & Poor's ("S&P")—downgraded Cemex's credit ratings to below investment grade, thereby further limiting Cemex's access to funding to pay its debts. As Cemex disclosed in an SEC filing: "On October 31, 2008 and January 21, 2009, Fitch and S&P respectively downgraded our credit rating from BBB- (investment grade) to BB+ (below investment grade). On March 10, 2009, both agencies further downgraded our rating, S&P to B- and Fitch to B." (Ex. N at S-65). Accordingly, in a two-month period, Standard & Poor's had downgraded Cemex six notches (from BBB- to B-) and Fitch had downgraded it five (from BBB- to B). Cemex acknowledged that these ratings downgrades "***have materially and adversely affected*** and will continue to adversely affect ***the availability of financing to us and our subsidiaries and the terms on which we could refinance our debt***, including the imposition of more restrictive covenants and higher interest rates on our existing debt." (*Id.*) (emphasis added).

S&P explained that its downgrade in March 2009 reflected its "concern[] about timely refinancing of [Cemex's] bank loan maturities in 2009," based on S&P's estimate that "Cemex needs to meet a cash flow shortfall this year of about $1.2 billion to $2.0 billion." (Ex. F). Fitch similarly explained that its downgrade in March 2009 "underscores the challenges Cemex will face as it seeks to negotiate with banks in a manner that will allow it to meet its debt coming due over the next few months" and that, even if successful, Cemex's "risk will remain high until it reaches a broader agreement with the banks that will allow it to lengthen the maturity schedule of a significant portion of its debt that comes due in 2009, 2010, and 2011." (Ex. E).

Significantly, the rating agencies did not reverse their negative views of Cemex's creditworthiness until the company announced the August 14 Transaction. As Cemex disclosed in an SEC filing: "[O]n August 27, 2009 [S&P 'revised its outlook'] from developing to positive. Fitch also revised its outlook on August 17, 2009, from negative to stable." (Ex. N at S-65).

***Fourth***, certain key financial indicators confirm Cemex's financial deterioration during the relevant period preceding Cemex's restructuring. Cemex had indefinitely postponed a bond offering when it announced the start of restructuring discussions on March 9, 2009 (Exs. C, F), and its stock reached its lowest point on that day. (Ex. O). The spreads on Cemex's credit default swaps also peaked just two weeks after the announcement of the restructuring discussions and narrowed thereafter in anticipation of the consummation of a successful restructuring. (Ex. O). Further, from June 30, 2008 to June 30, 2009, Cemex's net operating income (after expenses) dropped almost 50%, its Earnings Per Share dropped from 0.43 to 0.11, and its comprehensive financing result deteriorated precipitously from a loss of Ps4,483 million to a loss of Ps8,874 million. (Ex. N at F-3).

***Fifth***, Cemex confirmed in an August 17, 2009 conference call that it had undertaken to restructure its debt to alleviate the deterioration to its creditworthiness and financial condition. Cemex stated during that call that cement volumes had dropped by almost 50% between 2006 and 2009 and that the company does not expect its U.S. EBITDA to recover to 2007 levels until 2015. (Ex. M at 3) In light of these and other factors, Cemex stated that "*[o]ur immediate priority is to strengthen our balance sheet*" and that the "objective" of the August 14 Transaction is to, *inter alia*, "recover our financial flexibility" and "our investment grade structure." (*Id.* at 9). As Cemex also explained, the August 14 Transaction was an "important milestone in our integrated strategy to rebuild our balance sheet" (*id.* at 1), and was undertaken with Cemex's back against the wall of *unsustainable amortization requirements* in 2009 to 2011:

> Prior to our refinancing agreement, we were facing unsustainable amortization requirements during 2009 to 2011. The new debt

> maturity profile . . . provides time and flexibility to deleverage our balance sheet as our markets, our performance and the financial environment recover.

(*Id.* at 4).

These, and other, facts available to the DC show that there is an indisputable and *direct* causal link between the deterioration in Cemex's creditworthiness and financial condition and the restructuring discussions that it announced in March 2009 and which consummated in the August 14 Transaction. And, under Section 4.7(b)(iii), all that would be necessary to avoid application of this exception is an indirect causal connection. Although there may be reasonable debate in some cases as to whether the "direct or indirect" standard has been satisfied, this is not one of them. Indeed, if this situation is not a Restructuring, there would effectively be *no* such Credit Event short of Bankruptcy or Failure to Pay, and that result is of course inconsistent with the provision for a separate Restructuring Credit Event under the 2003 Definitions.[6]

In sum, because the exception in Section 4.7(b)(iii) does not apply here, the External Reviewers should determine that a Restructuring Credit Event has occurred with respect to Cemex.

### C. All of the Other Criteria of the Definition Have Been Satisfied

As shown above, the August 14 Transaction (i) postponed the due dates for the payment of principal on an Obligation of the Reference Entity, Cemex; and (ii) this event does not fit within the exception in Section 4.7(b)(iii). None of the other criteria for a Restructuring Credit Event were disputed in the DC discussions, and they have all been satisfied with respect to the August 14 Transaction.

[6] The market clearly recognizes that Restructuring is a distinct Credit Event: for a given Reference Entity, Credit Default Swaps that contain a Restructuring provision typically are more expensive than those that do not.

### 1. All of the Pertinent Criteria for an "Obligation" Have Been Satisfied

The May 2005 Facility is a $1.2 billion "Loan" governed by a credit agreement and issued by Cemex. (Ex. A). It is "Not Subordinated," because Section 5.09 of the May 2005 Facility provides that Cemex's obligation under this facility must rank *pari passu* with Cemex's other senior, unsecured and unsubordinated debt. (*Id.* at 28-29). The "Not Sovereign Lender" characteristic is also satisfied because Cemex's obligations under the May 2005 Facility are not primarily owed to a Sovereign or Supranational organization, but to private banks (Ex. A); and the "Not Domestic Currency" characteristic has been satisfied because amounts borrowed under the May 2005 Facility are payable in U.S. dollars, yen, euros, or sterling. (*Id.* at 16). In addition, the May 2005 Transaction is governed by New York law (*id.* at 49), thus satisfying the "Not Domestic Law" characteristic, and the majority of the lenders under the May 2005 Facility are non-Mexican banks and the May 2005 Facility is denominated in a currency other than pesos (Ex. A), so the "Not Domestic Issuance" characteristic is satisfied.

### 2. The Remaining Criteria for a Restructuring Have Also Been Satisfied

The extension of the maturities of Cemex's obligations by the August 14 Transaction was not provided for under the terms of the May 2005 Facility. The August 14 Transaction was also agreed between Cemex, the Reference Entity, and a sufficient number of holders to bind all holders of this Obligation (here, all holders). (Ex. A, Exs. K-O.). The Multiple Holder Obligation is satisfied as well because, at the time of the August 14 Transaction, more than three lenders that were not affiliates of each other held Cemex's Obligations under the May 2005 Facility and amendments or waivers to extend payment terms require consent of each affected lender. (Ex. A at 46). The August 14 Transaction also occurred in relation to an aggregate amount of not less than the Default Requirement, *i.e.*, $10 million. It postponed the maturities of all but $1 billion of Cemex's bank debt, and the May 2005 Facility was fully drawn and in the amount of $1.2 billion. (Ex. A, Exs. K-O.) Accordingly, the August 14 Transaction occurred with respect to at least $200 million of Cemex's obligations under the May 2005 Facility. The August 14 Transaction also occurred after the Credit Event Backstop Date, because all final documentation had been signed and conditions precedent had been satisfied by August 14, 2009 (Exs. K-N), which was less than sixty days before the Credit Event Resolution Request Date.

## II. THE ARGUMENTS ADVANCED FOR WHY THIS EVENT IS NOT A RESTRUCTURING ARE NOT SUPPORTED BY THE PLAIN LANGUAGE OF THE DEFINITION AND THE FACTS

In the DC deliberations, the Convened DC Members who contended that no Restructuring Credit Event has occurred (the "No Position") argued that Cemex's restructuring of its Obligations purportedly did not result directly or indirectly from a deterioration in its creditworthiness or financial condition. This position cannot be squared with the plain language of the Restructuring definition or the relevant facts.

One argument was that Section 4.7(b)(iii) is "vague" and that a so-called "purposive approach" should therefore be followed by applying such factors as market expectations, "economic sense," and "the rational operation" of the credit derivatives market. But Section 4.7(b)(iii) is not vague as applied to the Cemex restructuring, for all of the reasons stated above. Moreover, the DC Rules do not sanction ignoring the language of the 2003 Definitions in deference to policy considerations, but expressly state that "*[e]ach DC Question shall be Resolved based on the provisions of the 2003 Definitions* (taking into consideration any amendments thereto contemplated in the relevant DC Question) or the provisions of such other documents as contemplated in the relevant DC Question." DC Rules § 2.5(a) (emphasis added).

In any event, a true "purposive" interpretation of the definition of Restructuring is perfectly aligned with the plain language of the definition and the proper application of it as set forth in Part I.B, above. Restructuring has been the subject of significant discussion by market participants, but the exception in Section 4.7(b)(iii) has not been revised since its formal introduction in the 1999 Definitions. Instead, the market has addressed concerns regarding the Restructuring Credit Event by focusing on the Deliverable Obligations in certain types of cases.[7] Section 4.7(a) of the Restructuring definition was also revised to impose a Multiple Holder requirement to assure that individual creditors could not manufacture a Restructuring. The market concluded that these changes were preferable to adopting a materiality threshold or imposing other changes that would entail an unworkable level of subjectivity for triggering a Restructuring Credit Event. Adopting the No Position would effectively alter the definition of Restructuring, however, and thereby override the considered judgment of the market on these issues for the last ten years.

The No Position purported to "derive" a standard for determining when a Restructuring has occurred by engrafting what it referred to as "concepts of 'proximity' and 'gravity'" onto Section 4.7(b)(iii). Neither of these concepts as put forward by the "No" Position has any support in the definition. The No Position's proximity notion that "there must be no intervening break in the chain of causation between the deterioration and the 4.7(a) event" would transform the "direct or indirect" language in Section 4.7(b) into a notion of strict proximate cause. As noted above, a proximate cause is a *direct* cause; but the definition makes clear that a Restructuring also occurs when a Section 4.7(a) event results "*indirectly*" from a deterioration in creditworthiness or financial condition of a Reference Entity. This notion of "proximity" invoked by the No Position would impermissibly read "indirectly" right out of the definition, make the scope of this exception less clear, and increase the likelihood of future disputes. The

[7] In the wake of the triggering of a Restructuring Credit Event with respect to Conseco in September 2000, for example, market participants decided not to amend the exceptions to Section 4.7(a) in Section 4.7(b)(iii), but instead to introduce Modified Restructuring and Modified Modified Restructuring to alter the Deliverable Obligation criteria for physical settlement.

notion that the deterioration in creditworthiness or financial condition must have "proximity in time to the Section 4.7(a) event" is also hopelessly vague. How close in time would an event have to be to be "proximate" in this sense? Section 4.7(b) does not provide an answer, nor does the No Position identify any basis in the text of the definition for providing an answer.

The No Position's "gravity" notion, *i.e.*, that an event must be "severely damaging to the Reference Entity's credit profile," is similarly vague and contrary to the plain language of the definition. Section 4.7(b)(iii) does not impose a "severe[]" threshold level of deterioration that must be met before this exception is applied. Indeed, when the definition of Restructuring was included in the 1999 Definitions, it was intended to eliminate the "subjective assessment of the impact of [the] adjustment on the terms of the Obligation, *including whether that impact was material*." 1999 Definitions at viii (emphasis added). This approach was adopted *precisely because* of the "created uncertainty which, in turn, gave rise to a certain level of disputes" under prior practice. *Id.* As noted above, the market has chosen in the ensuing decade to address perceived problems with the Restructuring Credit Event, not by amending the scope of the trigger in Section 4.7(a) or the exception in Section 4.7(b)(iii), but by limiting deliverables in certain types of cases and imposing the Multiple Holder Obligation requirement. The determination of the Auction Settlement Amount directly addresses the type of economic, market-based concepts that the No Position is trying to engraft onto Section 4.7(b)(iii).[8] Elastic notions of "gravity" are also addressed by the Default Requirement, not by Section 4.7(b)(iii).

Finally, when the No Position's concepts are applied to the facts of Cemex, their inconsistency with the definition of Restructuring is stark. On "proximity," the No Position was that Cemex showed clear credit deterioration before March 2009, when Cemex initiated

[8] For example, if the financial distress of a particular Reference Entity is not severe, that presumably will be reflected in a higher Auction price and, consequently, a lower settlement payment by protection sellers.

discussions with its lenders to reschedule its debt, but that "intervening events" purportedly reflect Cemex's improved creditworthiness before the August 14 Transaction. Even if true, that argument does not negate at least an *indirect* connection between the deterioration in Cemex's creditworthiness and its restructuring. Indeed, this is the *precise situation* addressed by the 1999 Practice Notes. Where a Reference Entity begins negotiations while it is under distress but then, "even after a long period of negotiations," there is "improvement in the creditworthiness of the Reference Entity while the new terms are being negotiated or as a result of the new, presumably more favorable terms," "***the eventual agreement to new terms is best viewed as an indirect result of the original distressed situation*** and not as the negotiation of more favorable terms by a Reference Entity whose credit quality has improved." 1999 Definitions at ix (emphasis added).

Moreover, the "intervening events" that the No Position seeks to rely upon for breaking the causal chain in fact demonstrate quite the opposite. As noted above, Cemex's share price and market capitalization reached their bottom on March 9, 2009, the day that Cemex announced it was entering into discussions to restructure its debt, and thereafter began to climb, reflecting the market's positive view of Cemex's undertaking to restructure its debt to avoid a default and continue as a going concern. Indeed, on the very day that Cemex announced the August 14 Transaction, Cemex admitted that it had entered into the agreement because it was facing "*unsustainable amortization requirements during 2009 to 2011*." (Ex. M at 4).

As for the No Position's notion that Cemex's restructuring did not occur in sufficiently "grave" circumstances, there is, once again, no such concept in Section 4.7(b) and no basis for reading it into the definition. But, even if there were, there cannot be any question that Cemex's restructuring was undertaken against a real threat to its survival. Not only did the company state when it announced the restructuring that it had faced unsustainable amortization requirements, but *Cemex's auditors gave it a going-concern qualification* that was expressly tied to Cemex's "ability to complete the bank refinancing." (*Id.*; Ex. I at F-61). There can hardly be a more clear statement that the restructuring was undertaken and negotiated while the company was under severe financial distress. Indeed, a going-concern qualification is not issued unless an auditor has "*substantial doubt* about the entity's ability to continue as a going concern" *after* investigating, *inter alia*, the company's existing debt and its plans to remedy the conditions that gave rise to the auditor's doubt. *See* AU §§ 341.02, 341.07 (emphasis added).

Accordingly, even if the Panel were to accept that the No Position's vague notions of "proximity" or "gravity" can be read into the definition of Restructuring—and, to repeat, there is no support for this interpretation and it would lead to considerable uncertainty in applying the definition—the Panel should nonetheless conclude that those criteria are met here. No matter what standard the External Reviewers apply, there can no serious dispute under Sections 4.7(a) and (b) that a Restructuring Credit Event has occurred with respect to Cemex.

## CONCLUSION

The External Review Panel should answer "yes" to the Reviewable Question, "Has a Restructuring Credit Event with respect to CEMEX, S.A.B. de C.V.?"

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Respectfully submitted,
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