

Thomson – Further Information Concerning the Cash Settlement Mechanics

Each of the three Thomson Auctions references at least one Loan as a Permissible Deliverable Obligation. As a result, it is possible that any market participant submitting a Physical Settlement Buy Request or a Limit Bid to purchase Deliverable Obligations in any of the Thomson Auctions may be required to take delivery of one or more Loans under a Representative Auction Settled Transaction (a **RAST**). Market participants should be aware that in the event Delivery of a Loan is not successful, Cash Settlement will apply under Section 9.3 of the Definitions, as amended in the definition of RAST in the Thomson AST. A summary of certain specific concerns relating to Cash Settlement in the context of the Thomson Auctions follows. Terms not defined herein have the meaning set out in the 2003 ISDA Credit Derivatives Definitions, as supplemented by the 2009 ISDA Credit Derivatives Determinations Committees, Auction Settlement and Restructuring Supplement to the 2003 ISDA Credit Derivatives Definitions (the **Definitions**) and the 2009 Thomson Credit Derivatives Auction Settlement Terms (the **Thomson AST**), as applicable.

Market participants need to be aware of the risks associated with the Cash Settlement of Loans in the auction process – and specifically the Thomson Auctions. Market participants should consider all of the risks involved in placing Physical Settlement Requests or Limit Orders in the Thomson Auctions and should ensure that they are aware of the circumstances where the Cash Settlement provisions may operate, including in an economically disadvantageous manner.

This summary primarily relates to Section 9.3 (*Partial Cash Settlement Due to Impossibility or Illegality or, in the case of a Deliverable Obligation which is a Loan, no Delivery*) and Section 9.8 (*Partial Cash Settlement Terms*) of the Definitions, as amended in the definition of RAST in the Thomson AST.

This is a necessary summary of certain provisions and is no substitute for reading the relevant contractual provisions of any specific Credit Derivative Transaction to which such provisions may relate.

Cash Settlement mechanics in the Credit Derivatives Auction Settlement Terms

- If a party to a RAST is unable to successfully Deliver a Loan within the specified timeframe to the other party, a dealer poll may be held to determine the value of the relevant Loan.
- Full Quotations are sought in respect of an amount of such Loan equal to the greater of (a) the Outstanding Amount (i.e. the outstanding principal balance of the Loan specified in the Notice of Physical Settlement) and (b) any applicable minimum transfer amount under the terms of the relevant Loan.
- Cash Settlement will only occur if the Relevant Buyer enters into an arms-length binding contract to sell the relevant amount of the Loan using a firm Full Quotation from the Dealer (including the Seller (or, in respect of a settlement chain, the ultimate Seller at the end of the relevant chain of RASTs)) providing such Full Quotation.
- Seller (or, in respect of a settlement chain, the ultimate Seller at the end of the relevant chain of RASTs) is treated as a Dealer and is permitted to provide a Full Quotation and is given a "last-look" in order to be the final party to provide a Full Quotation. This means that such a Seller who wishes to purchase the Loan will have an opportunity to do so by providing the highest Full Quotation.

Specific points to highlight relating to the Thomson Auctions

Revolving Loan Facility Agreement

- Under the terms of the EUR1,750,000,000 Multicurrency Revolving Loan Facility Agreement (as amended from time to time) entered into, *inter alios*, by Thomson on 5 July 2004 (the **Revolver**), a lender may assign its rights under the Revolver in an amount equal to the lesser of (a) its entire holding and (b) EUR5,000,000. As a result, unless a lender's holding is in an amount less than EUR5,000,000, the minimum transfer amount in respect of the Revolver will be EUR5,000,000. Please note the Revolver is a Permissible Deliverable Obligation in all three Thomson Auctions.
- **IMPACT:** Since the Quotation Amount Increment (being the increments in which any Physical Settlement Request or Limit Order must be made) is EUR1,000, there are a number of situations where a RAST could be formed pursuant to an Auction but where Buyer would be unable to Deliver the Revolver to Seller due to the minimum transfer amount restrictions (for example, a Physical Settlement Sell Request of EUR1,000 forming a RAST with a notional of EUR1,000 cannot be settled if the minimum transfer amount is EUR5,000,000 without Buyer under the RAST incurring a substantial loss since Buyer is not compensated for any amount of the Loan that is Delivered in excess of the notional of the RAST).
- **IMPACT:** This may also affect the ability of Seller (or, in respect of a settlement chain, the ultimate Seller at the end of the relevant chain of RASTs) to take advantage of its last-look, because to the extent that the amount of the Loan in respect of which Full Quotations are sought in the dealer poll exceeds the RAST notional, Seller will not recoup all of the amounts paid by Seller to purchase the Loan through the corresponding reduction of the Cash Settlement Amount payable by Seller. This may disadvantage Seller if its Full Quotation was in excess of the market value of the Loan. It is now critical that Seller considers the economic effect of having to purchase an amount of the Loan in excess of the RAST notional at the Full Quotation given pursuant to its last-look.
- **NOTE:** Even if the RAST notional is greater than EUR5,000,000, Cash Settlement may still apply if the Loan cannot be Delivered for other reasons, such as failure to secure consent.

Changes to the last-look mechanic

- Any market participant submitting a Physical Settlement Sell Request or Limit Offer of EUR5,000,000 could be matched with two different counterparties in the Auction, thereby forming two RASTs with a different Seller (or, in respect of a settlement chain, a different ultimate Seller at the end of each such chain of RASTs). Instead of requiring Buyer to conduct two separate dealer polls, each for EUR5,000,000, while also being prevented from using the highest Full Quotation in each dealer poll due to only having EUR5,000,000 to Deliver, the Thomson AST expands the definition of "Dealer" to include any additional party nominated by the Relevant Buyer (i.e. in addition, but not instead of, the existing five dealers required). This allows the Relevant Buyer to nominate Seller (or, in respect of a settlement chain, the ultimate Seller) at the end of any relevant chain of RASTs to provide a Full Quotation for the RAST, or each RAST in the chain, as applicable.
- This means that in a situation where Buyer's exposure of EUR5,000,000 has been split into two separate RASTs, for example, one with a notional amount of EUR2,000,000 and one with a notional amount of EUR3,000,000, the outcome under the Thomson AST would be that Buyer would continue to alternate between each Seller (or, in respect of a settlement chain, the ultimate Seller at the end of each relevant chain of RASTs), offering them each a last look, until one refused the option. Both RASTs, or each RAST in the

chain, as applicable, would then be settled at the same Cash Settlement Amount that results from the Full Quotation provided by whichever of the two Sellers provides the highest Full Quotation.

- Without this change in the Thomson AST, it is possible that Buyer would only have been able to cash settle one RAST (by entry into a binding commitment to sell EUR5,000,000 of the Revolver to a Dealer) and the other RAST would have fallen back to Section 9.10 (which would require Delivery of another Deliverable Obligation). In turn, each Seller at the end of each chain could bid above the dealer poll price in order to reduce the Cash Settlement Amount payable, resulting in Buyer potentially being inadequately compensated through the Cash Settlement mechanism.
- **IMPACT:** Please note that the Seller at the end of the chain now may face competition with respect to their last-look. This may mean that a Seller's ability to purchase the Revolver through the dealer poll at a price just above the price which would have otherwise been achieved in the dealer poll is reduced depending on interest from other Sellers designated by the Relevant Buyer exercising their last look.

Examples

We set out below some examples to show how the provisions relating to the Cash Settlement of Loans in the Thomson AST work in practice. Assume for the purposes of each of the examples below that the Auction Final Price = 80%.

Example One:

Buyer holds less than EUR5,000,000 of the Revolver (e.g. EUR2,000,000) and submits a Physical Settlement Sell Request or a Limit Offer for a notional amount of EUR2,000,000 specifying the Revolver as the Deliverable Obligation

- As the minimum transfer amount under the Revolver is the lesser of EUR5,000,000 and the relevant lender's holding, Buyer is able to Deliver EUR2,000,000 of the Revolver to Seller.

Example Two:

Buyer holds EUR5,000,000 of the Revolver and submits a Physical Settlement Sell Request or a Limit Offer for a notional amount equal to EUR2,000,000 specifying the Revolver as the Deliverable Obligation

- As the minimum transfer amount under the Revolver is the lesser of EUR5,000,000 and the relevant lender's holding, Buyer will not be able to Deliver EUR2,000,000 of the Revolver to Seller, since here Buyer's holding is equal to EUR5,000,000 and therefore the smallest amount of the Revolver that Buyer can transfer is EUR5,000,000.
- Unless Buyer is prepared to overdeliver, the fallback to Cash Settlement will apply and the amount of the Loan in respect of which Full Quotations would be sought in the dealer poll would be EUR5,000,000.
 - Assume the highest Full Quotation is 70%. Seller would pay 10% by way of Cash Settlement Amount (since the Auction Final Price is 80%) and, if Seller was the party with whom Buyer entered into a binding agreement to sell the Revolver, 70% for the Revolver.
 - If Buyer did not enter into a binding agreement to sell EUR5,000,000 of the Revolver to one of the Dealers providing a Full Quotation (including Seller), Section 9.10 would apply and Buyer would need to Deliver something else to Seller.

Example Three:

Buyer holds EUR5,000,000 of the Revolver and submits a Physical Settlement Sell Request or a Limit Offer for a notional amount of EUR5,000,000 specifying the Revolver as the Deliverable Obligation.

Buyer is paired with two separate counterparties in the Auction, forming RAST 1 with a notional amount of EUR2,000,000 with Seller A and RAST 2 with a notional amount of EUR3,000,000 with Seller B.

- As the minimum transfer amount under the Revolver is the lesser of EUR5,000,000 and the relevant lender's holding, Buyer is unable to Deliver the Revolver into either of the RASTs (unless Buyer is prepared to overdeliver).
- The fallback to Cash Settlement will apply and the amount of the Loan in respect of which Full Quotations would be sought in the dealer poll would be EUR5,000,000.
- Seller A and Seller B could each provide Full Quotations and Buyer would continue to give each a last look until either declined to provide a further Full Quotation.
 - If the highest Full Quotation is 70%, provided by Seller A, and Buyer enters into a binding agreement to sell EUR5,000,000 of the Revolver to Seller A, Seller A would pay 10% by way of Cash Settlement Amount and 70% for the Revolver. Seller B would be required to pay 10% by way of Cash Settlement Amount.
- If Buyer did not enter into a binding agreement to sell EUR5,000,000 of the Revolver to a Dealer (including either Seller) providing a Full Quotation, both RAST 1 and RAST 2 would settle in accordance with Section 9.10.