

Statement by the Japan Legal Sub-Committee

This statement is provided to (i) clarify certain points for guidance purposes and (ii) correct certain misunderstandings regarding the relationship between the Revitalisation ADR process and credit derivatives and does not constitute definitive legal advice. It is not a determination of, and does not bind, the Japan DC, nor does it suggest that a Credit Event has occurred with respect to any particular entity. In particular, please note that under the Credit Derivatives Determinations Committees Rules (the Rules), the Japan DC may not deliberate the occurrence of a Credit Event until it approves the existence of "Publicly Available Information" (as defined in the Credit Derivatives Definitions). Any such determination made will then depend on the specific set of factual circumstances which apply. This statement should not be relied upon by any party and none of ISDA, the Japan DC, the Japan Legal Sub-Committee, Allen & Overy Gaikokuho Kyodo Jigyo Horitsu Jimusho (Allen & Overy) or Gaikokuho Kyodo-Jigyo Horitsu Jimusho Linklaters (Linklaters) undertake any duty of care or shall otherwise be liable to any interested person. As such, any such interested person should take their own legal advice when considering the issues below.

Following the recent submission to ISDA of various hypothetical fact patterns relating to the Business Revitalisation ADR Procedure in Japan under the Act on Special Measures Concerning the Revitalisation of Industrial Activities and the Innovation of Industrial Activities of Japan (Act No. 131 of 1999, as amended) (the **Revitalisation ADR process**) for the purposes of being considered by the Japan DC, the Japan DC formed a legal sub-committee (the **Japan Legal Sub-Committee**) to discuss further and analyse the legal issues involved, as they relate to the credit derivatives market as a whole. In doing so, the Japan DC noted that the Credit Derivatives Determinations Committees established pursuant to the 2009 ISDA Credit Derivatives Determinations Committees and Auction Settlement CDS Protocol are primarily designed to make contractual determinations with respect to specific factual circumstances that have already occurred and, therefore, should generally not be viewed as a forum for the discussion of hypothetical queries. Accordingly, the Japan DC has dismissed the questions presented.

While taking into account the general view noted above, given the relatively recent introduction of the Revitalisation ADR process in Japan, the Japan Legal Sub-Committee met on 17 December 2009 and subsequently, and engaged in substantive discussions regarding the interaction between the Revitalisation ADR process with respect to a Reference Entity and the definition of the Restructuring Credit Event as set out in Section 4.7 of 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**). Terms used but not defined herein shall have the meaning given to such terms in the Definitions.

Certain key aspects of the definition of Restructuring were discussed as they relate to the Revitalisation ADR process. As part of this discussion, the views of Allen & Overy and Linklaters were sought. Allen & Overy and Linklaters advised the Japan Legal Sub-Committee that:

- **At what time would agreement of creditors participating in a Revitalisation ADR Process actually occur?** If there were to be a unanimous vote by all the creditors participating in the Revitalisation ADR process to approve the proposed revitalisation plan in accordance with the relevant laws and regulations with respect to the Revitalisation ADR process, all creditors participating in such process would generally be bound at that point in time to a contractual agreement to put into effect the terms contemplated by the revitalisation plan even if additional procedural steps are required to be taken by such creditor in order to do so (such as amendments to the relevant underlying documentation). In other words, the point in time when contractual agreement is reached would generally be the passing of the relevant resolution rather than any subsequent implementation of the revitalisation plan. However, the

relevant laws and regulations with respect to the Revitalisation ADR process also do not provide any specific format for such a resolution to be publicised, and thus such resolution may or may not result in the existence of Publicly Available Information, depending on how or whether such resolution is made public.

- **Unanimity required by the Revitalisation ADR process.** The agreement of all the creditors participating in the Revitalisation ADR process is required in order to approve and agree on a revitalisation plan under the Revitalisation ADR process. In that sense, a single vote in favour of the revitalisation plan by one participating creditor does not of itself result in a binding agreement between such creditor and the debtor. As a result, there would not be the possibility that, pursuant to and within the Revitalisation ADR process, certain creditors who are participating in the Revitalisation ADR process could agree to restructure some portion of the debt outstanding while other such creditors refused.

In addition to the above, the Japan Legal Sub-Committee noted that market participants should also be aware that even if all of the elements required by Section 4.7 occur, that the Japan DC could only make a determination if:

- the request was submitted together with sufficient Publicly Available Information. The definition of Publicly Available Information is set out in Section 3.5 of the Definitions and, despite its name, can include information which is not truly "public" in its nature, for example, information received from or published by an agent in respect of the relevant obligation; and
- the Japan DC has received sufficient factual information that would satisfy it that all of the elements of the Restructuring definition have been met, such as:
 - (a) the occurrence of, agreement to or announcement of a relevant event, as set out in Section 4.7(a)(i) to (v) of the Definitions (for example, the occurrence of a postponement or other deferral of a date or dates for the payment of principal or premium);
 - (b) the relevant event occurs, is agreed or is announced with respect to one or more Obligations (i.e. obligations of the Reference Entity directly or indirectly pursuant to a Qualifying Guarantee which satisfy the relevant Obligation Category and Obligation Characteristics);
 - (c) the relevant event is not expressly provided for under the terms of the Obligation in effect as of the later of (i) the Credit Event Backstop Date and (ii) the date as of which such Obligation is issued or incurred;
 - (d) the relevant event is agreed between the Reference Entity and a sufficient number of holders of such Obligation to bind all holders of the Obligation (if the relevant event has not otherwise occurred in a form that binds all holders of such Obligation nor been announced by the Reference Entity in a form that binds all holders of such Obligation);
 - (e) the relevant event occurs, is agreed or is announced in relation to an aggregate amount of not less than the Default Requirement;
 - (f) Section 4.7(b)(iii) of the Definitions requires that the relevant event that constitutes a Restructuring as set out in Section 4.7(a)(i) to (v) directly or indirectly results from a deterioration in the creditworthiness or financial condition of the Reference Entity. Although

the point was made that it is generally a requirement for a Revitalisation ADR process involving the reduction of principal that it is difficult for the debtor to conduct its business mainly because of its excessive debts, the Japan Legal Sub-Committee notes that this element of the Restructuring definition must be analysed on a case-by-case basis, relying on the information available to the Japan DC at that time. Whilst the commencement of a Revitalisation ADR process is perhaps likely to occur in circumstances where the financial condition or creditworthiness of the Reference Entity has deteriorated, Section 4.7(b)(iii) requires a factual analysis with respect to causality;

- (g) the occurrence of, agreement to or announcement of the relevant event in Section 4.7(a)(i) to (v) does not occur due to an administrative adjustment, accounting adjustment or tax adjustment; and
- (h) evidence that the Credit Event occurred after the Credit Event Backstop Date.

It is important for market participants to note that any information submitted to the Japan DC for its consideration in relation to the above determinations is submitted on the basis that such market participant will be deemed to represent and warrant that such information has been disclosed and can be made public without violating any law, agreement or understanding regarding the confidentiality of such information. As such, information which cannot be made public (for example, private information) cannot be submitted to a DC in order to assist it in making the above determinations.

In instances where a sufficient number of voting members on the Japan DC believe that the requirements of the Restructuring definition have been met in relation to a Revitalisation ADR process, the Japan DC could Resolve that a Restructuring Credit Event had occurred with respect to the relevant Reference Entity – but again, only based on information validly provided to ISDA.