SUBMISSION TO EXTERNAL REVIEW PANEL ON BEHALF OF "NO" POSITION

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I. BACKGROUND

The credit default swap ("CDS") is the principal instrument used by financial institutions to manage credit risk – the risk that a debtor will default on its obligations and creditors will suffer a loss as a result. A CDS is a contract in which a buyer of credit default protection (the protection buyer) agrees to pay an upfront fee and/or a periodic fee (the "spread") to a seller of credit default protection (the protection seller) on a reference entity (the debtor) for the life of the contract or until a defined credit event, such as bankruptcy, has occurred. In exchange, the protection seller agrees that upon the occurrence of a credit event, it will pay the protection buyer an amount equal to the difference between the par value of the reference entity's qualifying debt obligations (such as bonds or loans) and the market value of those debt obligations, as determined at auction (or, in certain instances, will accept delivery of the reference entity's debt obligations and pay the par value thereof).

CDSs have become widely-used instruments that serve critical risk management and other functions. As the size and significance of the CDS market have grown, it has become increasingly important that the market operate in standard, predictable ways that are consistent with the reasonable commercial expectations of the parties. The ongoing development of the documentation for standard CDSs, including the adoption of the ISDA Determinations Committee process for deciding whether credit events have occurred, has been a key part of the evolution of the market toward this goal.

For the type of CDS in question in this dispute ("Relevant Transactions"), the relevant Reference Entity is CEMEX, S.A.B. de C.V. ("CEMEX") and the underlying documentation is a confirmation incorporating the ISDA Physical Settlement Matrix with a Transaction Type of "Latin American Corporate BL." As such, the Relevant Transactions incorporate the 2003 ISDA Credit Derivatives Definitions, as supplemented by the 2009 ISDA Credit Derivatives

Determinations Committees, Auction Settlement and Restructuring Supplement thereto (published on July 14, 2009) (collectively, the "Definitions").

CEMEX is a global building materials company founded in Mexico in 1906 with annual revenues of approximately $18 billion. Although CEMEX has multiple, legally distinct subsidiaries, only CEMEX, the parent holding company, is the Reference Entity in the Relevant Transactions. Like most corporations, CEMEX and its subsidiaries experienced financial difficulties, including liquidity pressure and deteriorating operating performance, in 2008 and early 2009 as a result of global recessionary conditions. It was against this backdrop that CEMEX's independent auditors, for the audit period ended December 31, 2008, expressed concern regarding the company's ability to service its long-term debt obligations in certain circumstances.

The auditors' opinion, however, did not take into account initiatives CEMEX implemented in early 2009 to improve its financial position, including: (1) reduction of operating costs (generating $900 million in annual savings), (2) cuts in capital expenditures (to $650 million in 2009 from $2.2 billion in 2008), and (3) the sale of certain business assets (including its Australian operations for approximately $1.7 billion). CEMEX's liquidity position and operating performance improved materially in the second quarter of 2009 ("Q2"). Its consolidated revenue increased by 14% from $3.66 billion in the first quarter ("Q1") to $4.188 billion in Q2, its EBITDA increased by 14% from $712 million in Q1 to $812 million in Q2, and its cash holdings jumped 27% from $768 million in Q1 to $978 million in Q2. CEMEX Mexico's ("Mexico") operations (the principal business and immediate subsidiary of the reference entity) held up well during 2009, with Mexican cement volumes "not substantially hit by economic recession." (*See* attached Tab 1.)

By June of 2009, the financial markets took notice. CEMEX's equity shares (as represented by its U.S. ADRs) rose from $3.87 in March of 2009 to $11.34 in mid-June 2009, an increase of 193%. CEMEX's bond yields declined from 30% in March of 2009 to less than 15% in June of 2009, and to 11% by early August 2009, significantly lower than the average yield for Latin American B-rated credit at the time. And of particular import, CEMEX's CDS spreads decreased significantly during this period from 1500 basis points in March 2009, to 800 basis points by May 2009, and to less than 600 basis points by early August 2009. The narrowing of CEMEX's yields and spreads indicates that the credit markets concluded that the risk of a CEMEX default was significantly lower by June of 2009 than in March of 2009, and even lower in August of 2009.

Against this backdrop of *improved* liquidity and operating performance, reduced risk of default, and as part of its strategic long-term plan to re-direct resources towards its core business, CEMEX set out to refinance its debt to add increased financial flexibility. To this end, the CEMEX group reached an agreement on August 17, 2009 (the "Refinancing Agreement") with its lenders to refinance $15 billion of its debt.

II. THIS DISPUTE

A. Standard of Review

The Reviewable Question is whether or not CEMEX's Refinancing Agreement constitutes a Restructuring Credit Event under Section 4.7 of the Definitions for the Relevant Transactions. The Determinations Committee previously found by a 9 to 6 vote that the Refinancing Agreement did not constitute a Restructuring Credit Event. This Panel's review of the decision can be reversed only if the majority of this Panel determines that another Presented Position is "the better answer." (Determinations Committee Rules §§ 4.6(c) and (d)(ii), *see* Tab 3.)

In answering the Reviewable Question, this Panel should interpret the relevant terms of the Definitions in a manner that is consistent with market practice and expectations (discussed below), as well as the principles of New York law that a court would be expected to apply if it were addressing this question.[1] In such a dispute, the party seeking to establish that a Restructuring Credit Event has occurred with respect to CEMEX would bear the burden of doing so. *See, e.g., Needham v. Candie's Inc.*, 2002 U.S. Dist. LEXIS 15144, at *8 (S.D.N.Y. Aug. 19, 2002) ("Where there is a condition precedent to performance, the party seeking to enforce the contractual obligation bears the burden of proving that the condition has been satisfied.") (citing *The Rachmari Corp. v. 9 East 96th St. Apartment Corp.*, 211 A.D.2d 262, 269 (1st Dep't 1995)).

Indeed, the terms of the Relevant Transactions place the burden of proof squarely on the party seeking the declaration of a Credit Event. Specifically, the Definitions require that in order for a CDS to be settled as a result of a Credit Event, the relevant Determinations Committee must make an affirmative determination that a Credit Event has occurred. (Definitions § 1.8(a)(ii), *see* Tab 2.) Additionally, under the Definitions, in the case of a Credit Event that is a Restructuring, it is typically required that a party wishing to settle the related CDS provide a Credit Event Notice that describes the purported Credit Event "in reasonable detail."[2] (*See id.*, *see also* Definitions § 3.3, *see generally id.* Art. III., *see* Tab 2.) The Determinations Committee decision must be supported by Publicly Available Information that "reasonably confirms . . . facts relevant to the determination that the Credit Event...has occurred" or, in the event that a protection buyer is the sole source of information, on a certification that a Credit Event has occurred. (*Id.* §§ 3.5(a) and (b), Tab 2.) Determinations Committee members are further

[1] Under Determinations Committee Rule 4.6(e), the Reviewable Question is to be interpreted in accordance with New York law.

[2] In other contexts where the Determinations Committee does not act, settlement of a CDS requires that the relevant party provide such a Credit Event Notice.

required to base their vote on information that is "either public or can be published by" the relevant Determinations Committee. (Determinations Committee Rule § 2.5(a), Tab 3.)

B. Summary of Argument

As discussed below, there are at least two independent reasons why CEMEX's Refinancing Agreement does not qualify as a Restructuring Credit Event under the Relevant Transactions. *First*, the available evidence does not demonstrate that CEMEX's refinancing took the form of any of the events enumerated in Section 4.7(a) of the Definitions. Available information suggests strongly that CEMEX's financing activity took the form of a refinancing, which involves the undertaking of a new obligation, the proceeds of which satisfy the old obligation, rather than a Restructuring, which under Section 4.7 is an event that modifies, but leaves in place, an existing obligation.

Second, the evidence before the Determinations Committee does not reasonably confirm that CEMEX's refinancing, even if had taken the form of one of the Section 4.7(a) events, resulted from a deterioration in CEMEX's creditworthiness or financial condition, as required by Section 4.7(b)(iii) of the Definitions. To the contrary, during the period leading up to the refinancing, CEMEX's financial condition was improving. Indeed, as discussed below, CEMEX appears to have been fully capable of satisfying its near-term debt obligations from existing cash and cash flow, even in the absence of the Refinancing Agreement.

III. THE REFERENCE ENTITY'S REFINANCING DOES NOT QUALIFY AS A RESTRUCTURING UNDER SECTION 4.7(a) OF THE DEFINITIONS

Based upon publicly available descriptions, CEMEX's Refinancing Agreement does not appear to qualify as one of the events enumerated in Section 4.7(a) of the Definition of "Restructuring." (*See* Tab 4.) That provision defines a Restructuring as a modification to an existing obligation and specifies the particular modifications that qualify:

(a) 'Restructuring' means that, with respect to one or more Obligations and in relation to an aggregate amount of not less than the Default Requirement, any one or more of the following events occurs in a form that binds all holders of such Obligation, is agreed between the Reference Entity or a Governmental Authority and a sufficient number of holders of such Obligation to bind all holders of the Obligation or is announced (or otherwise decreed) by a Reference Entity or a Governmental Authority in a form that binds all holders of such Obligation, and such event is not expressly provided for under the terms of such 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:

(i) a reduction in the rate or amount of interest payable or the amount of scheduled interest accruals;

(ii) a reduction in the amount of principal or premium payable at maturity or at scheduled redemption dates;

(iii) 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;

(iv) a change in the ranking of payment of any Obligation, causing the Subordination of such Obligation to any other Obligation; or

(v) any change in the currency or composition of any payment of interest or principal to any currency which is not a Permitted Currency. (*See* Tab 4.)

As an initial matter, a party seeking to establish that a Restructuring Credit Event has occurred must identify a specific Obligation of the Reference Entity, and demonstrate that the terms of the Obligation were modified in at least one of the ways set forth in Section 4.7(a). This showing cannot be made with respect to CEMEX. In the documents submitted to the Determinations Committee, the only Obligation identified was CEMEX's $1.2 billion revolving loan (the "Revolver"). And there is no clear indication that the Revolver was modified in a manner covered by Section 4.7(a) as part of the Refinancing Agreement or otherwise. The transaction documents for the Refinancing Agreement are not publicly available and there have been no other documents presented to the Determinations Committee that demonstrate that the Revolver was included in the Refinancing Agreement or that the terms of the Revolver were otherwise modified in any of the ways set forth in Section 4.7(a). Market participants, therefore, have been left to guess or infer that such a modification has occurred. Such speculation cannot serve to reasonably confirm that a Credit Event has taken place, as the Definitions require.

Moreover, CEMEX's Refinancing Agreement does not qualify as a Restructuring under this section because it appears to have taken the form of a refinancing through which existing financial obligations were repaid and replaced by new facilities. By the terms of Section 4.7(a), in order for a Restructuring to occur, one of the enumerated events must occur "with respect to one or more Obligations" in a manner that "binds all holders of the Obligation." In other words, a particular existing Obligation must be the subject of one of the enumerated types of modifications (i.e., the restructured Obligation must remain in place). Where an Obligation is repaid in full, and lenders extend new debt to the Reference Entity on different terms, an event within the meaning of Section 4.7(a) has not occurred with respect to the original Obligation, and there is no "Restructuring."

This principle, which is generally understood and accepted among credit derivatives market participants, is further supported by a significant change that was made when the Credit Derivatives Definitions were modified in 2003. In the prior version of the Definitions (adopted in 1999), a Restructuring was defined to include an "Obligation Exchange," which was defined as the "mandatory transfer . . . of any securities, obligations or assets to holders of Obligations in exchange for such Obligations." (*See* Tab 5.) Obligation Exchanges were generally understood to encompass a variety of transactions, including refinancing through which obligations are repaid and new debt is extended. When the Definitions were modified in 2003, an Obligation Exchange was eliminated as a form of Restructuring, making plain the intent to exclude refinancing from the definition of Restructuring.

Here, CEMEX repeatedly characterized the August 2009 financing activity as a refinancing that led to the creation of a new facility. When the Refinancing Agreement was under negotiation, for example, a June 30, 2009 press release entitled "CEMEX presents plan to refinance bank debt" explained that the "key component of the proposed refinancing plan is a revised maturity schedule on a new facility encompassing U.S. $14.5 billion in bank debt...." (June 30, 2009 Press Release (emphasis added), *see* Tab 6); *see also id.* ("'CEMEX is working to finalize the terms of a comprehensive refinancing plan with all our banks....'" (quoting L. Zambrano).) In a July 29, 2009 conference call, Rodrigo Treviño, CEMEX's Chief Financial Officer, similarly explained that the "new facility" would provide for a revised maturity schedule. (July 29, 2009 Conference Call (emphasis added), p. 7., *see* Tab 12.) During the same call, Héctor Medina, Executive Vice-President, Finance & Legal, explained that creditors "representing more than 90% of the debt is proposed to be refinanced have given us the indication that they would support the refinancing plan."

Once the Refinancing Agreement was in place, CEMEX continued to describe it as a "refinancing" with new terms and covenants. On August 17, 2009, Lorenzo Zambrano, CEMEX's Chief Executive Officer, thanked the financial institutions for working closely with CEMEX to "build a refinancing agreement that is in their interest as well as the interest of the rest of our CEMEX stakeholders." (August 17, 2009 Conference Call, *see* Tab 7.) As described in a PowerPoint presentation that day, CEMEX further explained that "50+ banks joined the Refinancing Agreement with its respective syndicated facility participation and/or bilateral loan[s]." (Company Presentation dated August 17, 2009, p. 21., *see* Tab 1.)

The terms of the August 2009 agreement also suggest that it was a refinancing, rather than a restructuring. Typically, a refinancing is characterized by the maintenance of the principal amount, but on new and different terms. A restructuring, however, usually occurs in the context of significant distress and therefore often involves acceptance by the creditors of some forgiveness of principal or interest payments or other less favorable terms. Indeed, sub-sections

(i) through (v) of the Restructuring definition identify conditions less favorable to the creditors, including decreased interest rates and amount of principal, subordination of ranking, or change to a nonstandard currency.

In contrast, the CEMEX transaction bears the hallmarks of a refinancing. For example, creditors did not take any principal haircut in connection with the August 2009 transaction, nor does it appear that the interest rate was decreased. Improved covenants and a security package favorable to the creditors also were included. (*See* August 17, 2009 Conference Call, *see* Tab 7.) The extensive changes suggest that the refinancing was effected through new loans rather than an amendment of the existing facilities and that creditors experienced no economic impairment as a result of the refinancing.

From time to time, CEMEX employees used ambiguous language to describe the Refinancing Agreement as "revising" or otherwise modifying certain terms applicable to the original loans. The August 17, 2009 conference call announcing the Refinancing Agreement referred to a "revised maturity schedule" and specified that the Refinancing Agreement "extends" the maturities of approximately $15 billion of obligations. In this context, however, such language appears to be used colloquially for the purpose of comparing the terms of the new and old facilities rather than memorializing the form CEMEX's financing activity took. At a minimum, such language – clearly subject to different interpretations – does not "reasonably confirm" that the form of CEMEX's refinancing constituted a Restructuring, particularly because CEMEX repeatedly described what it did as a "refinancing" that led to the creation of a "new facility."

Even viewing the contrary arguments in the most favorable light, however, the most that can be said is that it is not clear from the information available to the Determinations Committee (and therefore to this Panel) what CEMEX did. Such an ambiguous record cannot serve to "reasonably confirm" that an event described in Section 4.7(a) had occurred. The specific elements set forth in the definitions of Credit Events, together with the requirement to obtain Publicly Available Information confirming them, set a high standard for a determination that a Credit Event has occurred. This is appropriate given the significant consequences that follow from such a determination. A more relaxed standard would encourage parties to evaluate whether a particular Reference Entity's financing activity constituted a Restructuring before all relevant facts are known and place undue reliance on a few statements that are ambiguous at best.

A more relaxed approach also invites uncertainty and unpredictability that would be detrimental to the efficiency of the credit protection markets and the ability to hedge risk. If sufficient Publicly Available Information is not available, the appropriate course of action is to refrain from declaring that a Credit Event has occurred. Accordingly, because a party seeking to establish that a Restructuring Credit Event occurred with respect to CEMEX cannot point to Publicly Available Information "reasonably confirming" that the requirements of 4.7(a) are satisfied, a "Yes" answer is not the "better position."

IV. NO RESTRUCTURING CREDIT EVENT HAS OCCURRED BECAUSE IT CANNOT BE SHOWN THAT THE REFERENCE ENTITY'S REFINANCING RESULTED DIRECTLY OR INDIRECTLY FROM A DETERIORATION IN ITS CREDITWORTHINESS OR FINANCIAL CONDITION

Even if a party could establish that a Restructuring as defined in Section 4.7(a) had occurred with respect to CEMEX, Section 4.7(b)(iii) places two important limitations on the application of Section 4.7(a), each of which precludes a finding of a Credit Event here. Section 4.7(b)(iii) provides:

> (b) Notwithstanding the provisions of Section 4.7(a), none of the following shall constitute a Restructuring:
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> * * *

> (iii) the occurrence of, agreement to or announcement of any of the events described in Section 4.7(a)(i) to (v) in circumstances where such event does not directly or indirectly result from a deterioration in the creditworthiness or financial condition of the Reference Entity. (*See* Tab 4.)

As discussed below, there can be no finding of a Restructuring with respect to CEMEX because (1) its financial condition at the time of the August 2009 refinancing was not deteriorating and, indeed, was improving in several critical areas, and (2) even if CEMEX had experienced a deterioration in credit in the past, the August 2009 financing was not caused by any such deterioration.

A. Consistent With Market Expectations, Section 4.7(b)(iii) Should Be Interpreted Narrowly

Section 4.7(b)(iii) has been recognized by market participants as being somewhat vague and difficult to apply.[3] It seems clear, though, that the credit deterioration must be material and that this deterioration must be the cause of and not merely occur contemporaneously with one of the 4.7(a) events. In light of underlying principles of law, the purposes of CDSs and the expectations of the parties, there must be significant deterioration which necessitates a restructuring in order to avoid an imminent default or bankruptcy or similar loss event for creditors.

Absent more specific guidance from the Definitions themselves, general legal principles of causation are relevant. The concepts of proximity and gravity, drawn from the New York common-law view of causation, support the requirement of a close causal connection between the credit deterioration and the Restructuring. With regard to proximity, intervening events and the passage of time are typically found to break the causal chain between any two events: in this case, between the decline in creditworthiness or financial condition and a later restructuring. (14

[3] See, e.g., Letter from ISDA and London Investment Banking Association to the Basel Committee on Banking Supervision, October 2, 2002. (*See* Tab 11.)

N.Y. Prac., New York Law of Torts § 8:14; Restatement (Second) of Torts § 433 (1965), Comment on Clause (c).) The concept of gravity requires consideration of the consequences to the entity of a failure to enter into the restructuring and the presence or absence of other alternatives. Causation may exist where it can be shown that the failure to enter into a restructuring would have been substantially likely to result in an imminent default and/or bankruptcy. Where the entity had other meaningful alternatives (as in CEMEX's case), however, causation cannot be demonstrated clearly.

Interpreting the language of 4.7(b)(iii) in this manner is also consistent with its purpose in the context of CDS.[4] *See, e.g, Glassalum Int'l Corp. v. Albany Ins. Co.*, 2005 U.S. Dist. LEXIS 9767, at *16-17 (S.D.N.Y. May 23, 2005) (courts should interpret contracts in a manner that is consistent with contract purpose) (citing *Sunrise Mall Assocs. v. Import Alley of Sunrise Mall, Inc.*, 621 N.Y.S.2d 662, 663 (2d Dep't 1995).) As noted above, the purpose of a CDS is to protect against the risk that a Reference Entity will default on its obligations and cause a loss to creditors. In accomplishing this purpose, the Definitions provide for six standard potential credit events that the parties can select as triggers for credit protection: (1) Bankruptcy, (2) Obligation Acceleration, (3) Obligation Default, (4) Failure to Pay, (5) Repudiation/Moratorium, and (6) Restructuring. All six are designed to compensate protection buyers in situations where there is an actual or imminent default, or expected loss, on the Reference Entity's debt obligations. To wit, a Bankruptcy Credit Event occurs if a Reference Entity becomes subject to an insolvency filing or analogous event. An Obligation Acceleration Credit Event occurs if a Reference Entity's debt obligation becomes due and payable prior to the maturity date as a result of the

[4] The approach taken by the Determinations Committee in certain other matters, including as to the definition of "Qualifying Policy" for the purpose of establishing the list of Deliverable Obligations for the Syncora Guarantee Inc. Auction, is consistent with a purposive approach intended to be consistent with market expectations. *See Nomura Int'l v. Credit Suisse First Boston Int'l*, (2003) EWHC 160. (applying purposive interpretation to CDS).

occurrence of a default, event of default, or other similar condition. A Failure to Pay Credit Event occurs if a Reference Entity fails to make an interest or principal payment when it comes due. A Repudiation/Moratorium Credit Event occurs if a Reference Entity repudiates or rejects its debt obligations or declares a suspension on debt obligation payments.

The Restructuring Credit Event should be construed similarly. It was included in the Definitions as a Credit Event to accommodate and is of principal importance in markets that do not have a concept or practice of reorganizations and restructuring of debt obligations within a bankruptcy proceeding, such as under Chapter 11 of the U.S. Bankruptcy Code.[5] Regulators and others arguing for its use in these jurisdictions are thus seeking to ensure its application for the purpose of providing protection in the context of "distressed" restructurings; that is, restructurings that are alternatives to bankruptcy or a default on the relevant obligations. The requirement that the Restructuring result from a deterioration in creditworthiness or financial condition should be read in light of this purpose.

Accordingly, a Restructuring Credit Event should be declared only in situations where financing activities result from a deterioration in creditworthiness that is akin to, and not appreciably less than, a bankruptcy or outright default. *Perreca v. Gluck*, 295 F.3d 215, 224 (2nd Cir. 2002) ("provisions of a contract be read together as a harmonious whole, if possible") (citations omitted). In other words, a Restructuring Credit Event should arise only in situations in which a creditor's investment is seriously impaired but the borrower is not subject to a formal insolvency proceeding, actual default, or other "hard" credit event that is expected to cause creditors to suffer a loss.

[5] This is one reason that participants in the North American credit derivatives market have moved away from using the Restructuring Credit Event.

Any other approach based on some unspecified and less severe decline in creditworthiness or financial condition would create significant uncertainty for market participants as to whether a Restructuring Credit Event occurred. There are several reasons why such an approach would be unacceptable. *First*, a broad interpretation runs the risk of technical Restructuring Credit Events on countless healthy corporations that refinance or amend credit terms, especially during recessionary macroeconomic periods when most corporations display evidence of credit deterioration. *Second*, a broad interpretation would be inconsistent with the other five defined Credit Events, each of which applies in similar, easily identifiable circumstances. This inconsistency would eviscerate the certainty and reliability necessary to price credit risk and undermine the efficient operations of the CDS market. *Third*, a broad interpretation would permit the declaration of technical Restructuring Credit Events that would have the effect of depriving protection buyers of their expected hedge. In many instances, buyers pay significant upfront premiums for long-term protection. Allowing the declaration of a Credit Event in instances of only mild distress where the reference entity's bonds are still trading at or close to par (i.e., with high "recovery rates") would allow sellers of protection to terminate the CDS and settle with small cash settlement payments, while pocketing the large premium. This would turn the CDS market into a highly technical gaming system and seriously impair market participants' ability to adequately manage credit risk. *Fourth*, a broad interpretation could provide an additional reason for market participants to exclude Restructuring protection from future transactions because of the additional uncertainty involved in whether it can be triggered and the likely increase in the cost of credit protection (or greater difficulty in accurately pricing credit risk) as a result.

A narrow interpretation is also consistent with the expectations of most market participants who, in general, have only been prepared to declare a Restructuring Credit Event in circumstances where the Reference Entity faces significant financial distress.[6] Indeed, earlier this year, market participants considered the scope of Section 4.7(b)(iii) with respect to Liz Claiborne, another company that refinanced its obligations in the context of the financial upheaval of late 2008 and early 2009. The market's evident conclusion in that case that no Restructuring occurred provides both guidance as to how the question should be viewed here and a reminder that the credit markets do not expect Restructuring Credit Events to be declared in situations not involving serious financial distress.

In January 2009, Liz Claiborne had been operating at a loss for several quarters, had only $41.5 million in available cash and had $408.9 drawn on its $750 million revolver. By its terms, the revolver was scheduled to be paid in full in October 2009. With few apparent options remaining, Liz Claiborne entered into an agreement to refinance the obligation. Shortly thereafter, market participants on a public ISDA market call took up the question of whether this refinancing qualified as a Restructuring Credit Event. The analysis set forth in that call, and apparently accepted by market participants thereafter (insofar as we are unaware of anyone attempting to declare a Credit Event), suggested that Section 4.7(b)(iii) precluded a finding of a Restructuring Credit Event because, despite a ratings downgrade and a recent financial report suggesting that the company's available revenue was well below the level necessary to support repayment of the revolver, the loan's maturity was still nine months away and it was possible that the company could have generated sufficient earnings or otherwise raised cash to pay the

[6] Market participants have urged a narrow interpretation of the Restructuring Credit Event in other contexts to avoid the technical and opportunistic triggering of swaps without a clear indication that the restructuring resulted from the reference entity's deterioration in its creditworthiness. For example, in August of 2002, numerous market participants, including a group of protection sellers, expressed concern that some parties had argued that a Restructuring event occurred with respect to Xerox, where there had been improvement in Xerox's financial condition, and in the price of Xerox's debt and stock, during the months leading up to the event. It appears that market participants generally concluded that the event was not a restructuring because of the lack of causal connection. (Letter from ISDA and London Investment Banking Association to the Basel Committee on Banking Supervision, October 2, 2002, *see* Tab 11.)

revolver without the benefit of a Refinancing. The Liz Claiborne analysis has been referenced in numerous articles and presentations since then and has played a role in shaping market expectations as to the proper interpretation of the Restructuring definition.

This analysis is consistent with the view that under Section 4.7(b)(iii) it is not enough to show that a Section 4.7(a) Restructuring and a deterioration occurred concurrently. Rather, it must be established that the Section 4.7(a) Restructuring was caused by the deterioration. In this situation, there was not enough evidence to conclude that Liz Claiborne could not have refinanced or repaid the revolver in the absence of the Restructuring. As discussed below, the Liz Claiborne case provides important guidance as to the expectations of market participants in circumstances like that of Cemex.

B. CEMEX's Refinancing Agreement Did Not Constitute A Restructuring Because CEMEX's Financial Outlook Was Improving And Its Creditors Did Not Face An Imminent Risk of Loss

A careful review of CEMEX's financial condition at the time of its August 2009 refinancing reveals that CEMEX was substantially more stable than Liz Claiborne was when it undertook its refinancing, had experienced improvement in key financial metrics since Q1 2009, and would have been able to satisfy its near and medium-term obligations even in the absence of the August 2009 refinancing. Thus, it cannot be said that CEMEX's creditors faced at the time the type of loss protected by CDSs.

As discussed in greater detail in Section I, CEMEX and its subsidiaries experienced financial difficulties in 2008 and early 2009 as a result of the global recessionary conditions at the time. It was in the context of those difficulties that CEMEX's auditors issued a "going concern" opinion with respect to the consolidated CEMEX group.[7] Recognizing that CEMEX

[7] Corporations often continue to operate after receiving a going concern opinion. For example, Las Vegas Sands, the Las Vegas-based casino operator, continued to operate after receiving a going concern opinion, and its auditors withdrew their going concern opinion following a public equity offering. Exide Technologies, a manufacturer of

itself had various financing options, however, the auditor qualified its opinion by noting that CEMEX needed to either refinance its debt "or otherwise obtain additional debt or equity financial resources to pay CEMEX's obligations as they came due." (CEMEX, Annual Report (Form 20-F), at F-61 (June 30, 2009), *see* Tab 9). In other words, the auditor recognized that CEMEX's options were not limited to a Restructuring and that the opinion did not take into account CEMEX's plans to avail themselves of those options.

As the general macroeconomic outlook, along with CEMEX's fortunes, improved beginning in Q2 2009, CEMEX took a number of steps to improve its performance and financial condition. These steps included a reduction of operating and capital costs, the sale of non-core assets and receivables, and the issuance of Certificados Bursatiles de Corto Plazo. Combined with sharp increases in revenue and EBITDA from Q1 to Q2, CEMEX's actions resulted in a brighter outlook.

CEMEX's equity shares (as represented by its U.S. ADRs) rose from $3.87 per ADR in March of 2009 to $11.34 per ADR by mid-June 2009, an increase of 193%. Its bond yields declined from 30% in March 2009 to less than 15% in June 2009, and to 11% in early August 2009. CDS spreads plummeted from over 1500 basis points to less than 600 basis points in the same period.[8] Indeed, by mid-June 2009, CEMEX's equity market value had increased to nearly $10 billion from its low of $3.3 billion on March 9, 2009. This improvement opened the door to

lead-acid batteries, similarly had a going concern opinion withdrawn after monetizing certain assets and realigning its workforce. Gruma, Inc., a leading producer of corn and wheat flower, returned to profitability less than a year after receiving a going concern opinion from its auditors. There is no reason to believe that CEMEX will not accomplish the same. Its auditors only expressed doubt about CEMEX's ability to continue as a going concern in the event that it could not secure additional capital through, for example, asset sales or other mechanisms. But CEMEX in fact did raise capital by securitizing MXN $2.2 billion of its accounts receivables in July 2009, selling CEMEX Australia for A$2.02 billion, and issuing securities in the form of Certificados Bursatiles de Corto Plazo. Cemex's equity market value by June 2009 was almost $10 billion, providing an additional avenue of raising equity proceeds (which in fact the Company did undertake in September 2009, raising $1.8 billion).

[8] By way of comparison, on August 17, 2008, the "on the run" spread quote for the very widely traded Markit CDX High Yield Index of 100 non-investment grade names was 881 basis points.

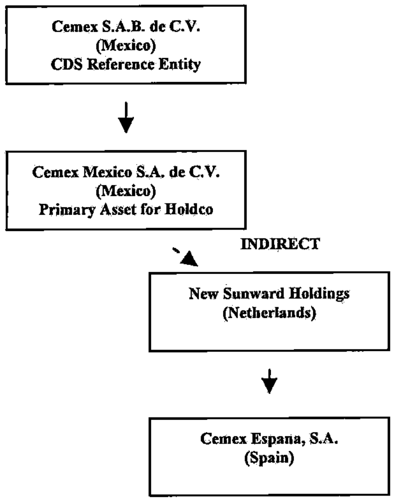
various financing options, including allowing the company to issue Certificados Bursatiles de Corto Plazo. During this period, CEMEX also demonstrated a continuing ability to raise funds in other ways, including the successful securitization of MXN $2.2 billion of accounts receivables and the sale of CEMEX Australia for A$2.02 billion. These improvements in financial condition were viewed favorably by rating agency Fitch, which changed its outlook on CEMEX to "Watch Evolving" on June 15, 2009. In short, CEMEX's financial condition meaningfully improved between March and August 2009, with improved operations, profitability and capital structure.

Against this backdrop of an improving financial condition, there is no basis to conclude that CEMEX's creditors faced the imminent prospect of suffering the type of loss against which CDSs protect. For this independent reason, a "Yes" answer is not a "better position."

C. <u>CEMEX's Refinancing Agreement Did Not Result From A Deterioration In Creditworthiness Or Financial Condition</u>

Even if CEMEX's creditworthiness and financial condition were viewed as having deteriorated at a relevant time, there is insufficient evidence to conclude that the refinancing resulted from that deterioration. Significantly, as a result of its improving financial condition, the company had sufficient free cash flow to satisfy its 2009 and 2010 debt obligations even without entering into the Refinancing Agreement. The Refinancing Agreement was not needed to avoid imminent default, insolvency or other serious loss to creditors of the reference entity.

As shown in the chart below, CEMEX is a holding company with three main subsidiaries, organized as follows:



Although the consolidated CEMEX group carried significant debt, less than 30% of that debt was carried by CEMEX. The remainder was incurred by New Sunward ("NS") and CEMEX España ("España"), with España responsible for the vast majority. CEMEX itself did not guarantee, and therefore was not responsible for, any of the España debt. Mexico, on the other hand, was a wholly-owned subsidiary of CEMEX that generated free cash flow that was available to service CEMEX debt. Thus, in evaluating CEMEX's ability to satisfy its debt obligations, it is necessary and appropriate to focus solely on the obligations of CEMEX and the ability of CEMEX Mexico to service those obligations.

Based on available information, it appears that prior to the Refinancing Agreement, only $623 million of the debt residing in CEMEX was to come due in 2009. At the time, the free cash flow from Mexico alone was sufficient to pay these obligations.[9] This could be accomplished without accessing cash from any other CEMEX subsidiary or drawing down cash reserves running between approximately $700 and $900 million over the first two quarters of 2009.

[9] Even during the worst of the downturn, CEMEX generated positive free cash flow and its forecast for full year 2009 is a substantial $1.6 billion.

Perhaps the strongest indicator that CEMEX had sufficient cash on hand during the period preceding the Refinancing is its decision to pay $98 million of interest on perpetual bond securities due on June 30, 2009 even though it had the option to defer the payments without any event of default. If CEMEX had truly been in distress, it would have deferred these payments, as it had the option to do so under the terms of the perpetual securities. And if creditors had believed that CEMEX faced an imminent default, they would have demanded that CEMEX defer the payments and use the $98 million in cash to satisfy debt obligations. They did not.

These facts all strongly suggest that CEMEX entered into the August 2009 refinancing to take advantage of the cooperation of its creditors and to position itself for an upturn in its sector, not because it faced an imminent default. This is precisely what CEMEX has explained:

- CEMEX described the financing as enabling it to "take advantage of a potential upturn in the business cycle in core markets" and allowing it to conduct "planned asset divestitures more efficiently." (September 22, 2009 Equity Prospectus at S-5., *see* Tab 10)
- Describing the role of the Refinancing in the context of its overall strategy, CEMEX stated that "combined with the divestment of non-strategic assets, ongoing cost-reduction initiatives, and the ability to access the capital markets, CEMEX expects that, when completed, the financing will contribute to a significant strengthening of the company's capital structure." (2009 Second Quarter Results, p. 4., *see* Tab 8.)
- CEMEX's CEO described the financing as "an important milestone in our integrated strategy to rebuild our balance sheet, reinforce our business model and take advantage of the coming recovery of the global economy" and concluded that he was "confident that the cumulative effect of our efforts will allow us to regain our financial flexibility and eventually our investment-grade capital structure." (August 17, 2009 Conference Call, *see* Tab 7.)

Looking at both the intervening events and CEMEX's own view of the refinancing as part of its business strategy, the available public evidence does not demonstrate, even indirectly, the causal link necessary to trigger a Restructuring Credit Event in this matter. Accordingly, a "Yes" answer is not the "better position" and this Panel should not overturn the views of the majority of the Determinations Committee.

Dated: New York, New York
November 25, 2009

Shearman & Sterling LLP

By: ____________________

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Advocate for the Convened DC Members who Favor a "No" Answer to the Reviewable Question