Minutes of the Tenth Meeting of the Working Group on Distributions of Securitized Products

1. Date
October 2, 2008 (Thursday) 15:00 to 17:00

2. Place
JSDA Conference Room

3. Participants
As stated in Appendix 1

4. Agenda
(1) Scope of securitized products (continued)
(2) Unified Information Disclosure Format (provisional name) (UIDF)
- Survey results
- Practical application of UIDF (including consistency with legal disclosure items)
- Consideration of CMBS originated by banks
- Treatment of information that cannot be included in UIDF
- Rules for periodic revision of UIDF after its introduction

5. Summary of Proceedings

(1) Scope of securitized products (continued)

A. On "Products which are deemed that the transactions are practically the transfer of specific assets"

The WG Chair said that "Products which are deemed that the transactions are practically the transfer of specific assets" should be excluded from the scope of the JSDA's self-regulatory rules. He raised if there are any products other than trust beneficiary rights among marketable securities covered by the JSDA's self-regulatory rules which falls into this criteria.

In response, a WG member expressed the opinion that "Products which are deemed that the transactions are practically the transfer of specific assets" means assets which are entrusted; therefore there probably were not any such products among the Paragraph 1 marketable securities covered by the JSDA's self-regulatory rules.

The Secretariat stated that if trust beneficiary rights were the only "Products which are deemed that the transactions are practically the transfer of specific assets", then there is no need to create a rule to remove products from coverage by the JSDA's self-regulatory rules when the products were outside the scope of the JSDA's self-regulatory rules. Therefore the Secretariat would remove them from the draft self-regulatory rules. However, to clarify the treatment of trust beneficiary rights, they would be included in the Q&A pamphlet. When the Secretariat asked whether the WG members were in agreement with these changes, they approved them.

B. On "Products for which the location and nature of specific risk is (including the risk arising from underlying assets of said securitized product) clear, and it is possible for investors to recognize such risk"

The WG Chair posed for discussion the issue of whether the three examples in the current proposal were also appropriate in the case of "Products for which the location and nature of specific risk is

(included the risk arising from underlying assets of said securitized product) clear, and it is possible for investors to recognize such risk."

There were no particular opinions on this issue and the examples in the current proposals were approved.

Next, a WG member gave the following explanation of securitized products that are deemed "Products for which the location and nature of specific risk is (included the risk arising from underlying assets of said securitized product) clear, and it is possible for investors to recognize such risk." under cases where guarantee is attached to such securitized products.

- I would like to propose that for cases where the location of the risk is clear as the result of having guarantees etc. to the products, the scope for said securitized products be limited to products that are deemed to be equivalent to securities, etc. issued by the entity providing the guarantees, etc. I make this proposal because even though the credit risk is guaranteed, the securitized product also is exposed to risk other than credit risk. For example, the product is exposed to risk of change in the maturity date, and if the location and nature of this risk is not clear, then I don't believe that the product should be removed from the scope of the self-regulatory rules.

It was decided to continue the discussion on the treatment of securitized products with guarantees at the next WG meeting.

C. On "Products for which fund managers have investigated and analyzed the investment and details of investment management of said product and are required under related laws and ordinances to report to customers on the investment and details of investment management of said product"

A WG member expressed the following opinion.

- The current proposal reads as if it was only written for domestic products. It is possible that it will apply to overseas investment trusts or investment companies. Therefore, I think that it should be revised so it can be read as being for both types of products. However, since we will not necessarily be able to determine whether fund managers and others are required to report to customers under laws and ordinances, I suggest that a clause such as "or stipulated by contracts, etc." should be inserted into the proposal.

In response, several other WG members voiced the following opinions.

- Under the self-regulatory rules, domestic and overseas products should receive the same treatment.
- If a clause such as "or stipulated by contracts, etc." is included, the proposal will apply to a very broad range of products, for example trusts that submit asset reports to customers based on contracts, weakening the substance of the self-regulatory rules. Therefore, we need to be cautious how we make the revision.

While it was recognized by the Working Group that the proposal should clearly include overseas products, it was decided to take up the discussion again at the next meeting.

D. Q&A pamphlet on treatment of structured bonds or notes

A WG member stated that he would like to see the proposal on the Q&A pamphlet revised to say that they would like to have the JSDA create a channel to handle cases where JSDA member firms can not make decisions on their own. This request was approved.

(2) Unified Information Disclosure Format (provisional name) (UIDF)

A. Survey results

Using the document included as Appendix 5, the Secretariat gave an explanation of the results of the survey of originators.

The WG Chair commented that there were not a lot of items for which many originators expressed problems with providing information. He said that going forward, the WG would put the results out for public comment and it was possible that more opinions could be gathered from originators that did not participate in the origination survey, but at this point it did not seem unrealistic that the Common Information Item List could be used in the self-regulatory rules.

The WG Deputy Chair gave the opinion that compared with CMBS; there was a gap in the level of information provided for RMBS, ABS, and CLOs. Therefore, it might be necessary to discuss whether each level proposed in current draft was indeed appropriate for each product at the next meeting.

The WG Chair stated that, including that point, he wanted to bring the discussion of the UIDF to a conclusion at the next meeting with full reference to the results of the survey of the originators.

B. Practical application of UIDF (including consistency with legal disclosure items)

The WG Chair made the following statements.

- The information items of the Common Information Item List and the statutory required disclosure items were mostly compatible.
- At this time, all companies have administrative processes in place to communicate this information by asset type. Therefore, if the UIDF were to be introduced in future, it probably would not place such a large additional burden on the companies.

WG members expressed the following opinions on this issue.

- (Regarding information communication following the distribution of a securitized product for which statutory disclosure applies) There are cases where the distributor not only provides written documentation appropriate for the format for statutory disclosure requirements, but also provides voluntarily publicly announced information by the issuer at the same time. If these products are to be the target of self-regulatory rules, at the very least the reporting format should conform to the format of the statutory disclosure requirements from the point of view of maintaining the distributor's options and avoiding increasing the administrative burden. In addition, information not related to statutory disclosure and voluntarily made public should not be made obligatory.
- (Regarding information communication following the distribution of a securitized product for which statutory disclosure applies) The administrative burden would be reduced if information vendors were used. To prevent disclosure to the wrong people, passwords could be used.
- In deciding how to use the UIDF in practical terms, we are going to have to base our approach on the actual systems being currently used by each firm. Therefore, we are going to have to accept a certain degree of originality in each company's system.
- From the point of view of producing documents to communicate information, let's suppose that we decided to fill in the Common Information Item List in a format consistent with the statutory disclosure requirements. We would have to find the items on the Common Information Item List that are not on the statutory disclosure item list and fill them in—this is a large amount of administrative work. Moreover, from the standpoint of distributing products, if we are asked by a customer where an item on the Common Information Item List is stated, having them all on one

document facilitates explanation. Therefore, I think that communication of the Common Information Item List should be done using an independent document.
- Particularly with the communication of information after the distribution of the product, in most cases there are many companies giving out the information. The distributors cannot control to what degree these multiple companies are going to communicate the information. If the distributors are going to be regulated in this aspect, the regulation should be limited to areas that the distributors can control.

C. Consideration of CMBS originated by banks

The current CMBS Common Information Item List targets originators that are mainly securities firms that have made non-recourse loans with the intention of securitizing them. The products have also been created based on the assumption that the servicer will be a specialist company different from the originator. In view of this background, in recognition of the issue of non-recourse loans made by banks, etc., without the intention of loans being later securitized, hearings were held with Japanese commercial banks to determine whether there would be any problems in such circumstances.

Representatives of commercial banks participating in the hearings had the following opinions.
- It would not be difficult to provide information on the items in "A." However, since we have the obligation to keep information confidential, whether the counterparty to whom we are providing information is a distributor or an investor, the disclosure of information should be based on confidentiality agreements. This applies for all of the items on the Common Information Item List.
- For "Actual principal and interest DSCR" in "B-2. Performance of Underlying Loans," while it is not impossible to provide information, it is difficult in some cases because banks are not constantly monitoring the products.
- For "Net sales price" in "B-3 (1). Special Items Report (Interim report on subject loans)," if the meaning of "net" is the sales price less the necessary expenses for the sale, it is possible that providing information will be difficult on a case by case basis because we don't know just how much detail we can get from borrowers.
- For "Date added to servicer watch list" in "B-3(2). Watch List (Interim report on subject loans)," in case when we are both the originator and the servicer, we cannot be sure that we can provide a servicing report with a complete servicer watch list. Therefore, this item may not always be applicable.
- Under "Reserve information" in "B-5.Information on Reserves (interim report on subject loans)," there are the items "name of reserve account" and "balance of reserve account." When a bank is the originator, it is also often the financial institution where the account is opened. Therefore, there are cases where the material received from the borrower during the period does not contain a waterfall report, making it difficult to provide this information.
- In "C-1. Performance Report on Collateralized Properties (Point of issue disclosure and interim reports)," there are cash flow related items (effective gross income, net operating income, net cash flow) that can only be comprehended at the trust calculation level. In such cases, we would like you to introduce treatment methods that we can comply with under those conditions.
- In "Collateral Evaluation" of "B-1. Basic Information on Underlying Loans (point of issue disclosure and interim reports)," while we can disclose appraisal value and other information, we cannot disclose the actual evaluation made by the lender.
- We would like to see self-regulatory rules with some degree of flexibility, where in some cases allowances can be made for situations in which we cannot provide the information.
- At the present time, there is not really an adequate system in place for originating CMBS. What should be done and to what extent and whether or not it can be done will depend not only on to what degree information can be obtained from customers, but also what kind of administrative

system can be set up within the banks.

A representative from CMSA gave the following opinion
- The “Net sales price” in B-3 that was pointed out is a Level 2 item (Useful items that should be considered for reporting in most cases) and therefore it is expected that there will be cases where it will be impossible to get the information.
- Overall, we don’t feel there is anything unreasonable about the comments that have been made.

The WG Chair asked whether banks would also act as servicers if they became originators of CMBS in the future, or whether they would outsource the servicing activity to others regardless if the servicer is an affiliate of the bank or not. One of the representatives of the commercial banks present gave the following response.
- Both cases are possible. Banks will probably deal with each case in accordance with the specifics, trying to balance the added administrative burden and reduction of risk by keeping servicing in-house with the cost of outsourcing.

D. Treatment of information that cannot be included in UIDF

The WG Chair posed for discussion the issue of how information that cannot be included in the UIDF was to be treated.

The WG members gave the following opinions.
- There is no real necessity for making rules. As came out in the discussions on setting up procedure, the intention is to put it into some kind of written format, but in essence we need to communicate the information that should be communicated.
- Within the Common Information Item List there is the “Others” category, for which we got many “cannot comply with” responses in the survey of the originators. Even if we removed the “Others” item from the list, it would not mean that only the items on the Common Information Item List need to be communicated in all cases. What is important is content not form. Isn’t what we are talking about here the same thing?

E. Rules for periodic revision of UIDF after its introduction

The WG Chair said that one possible proposal for dealing with this issue was to revise the UIDF annually after its introduction to take into account changes in economic conditions and new products, etc. To do that, meetings to collect information and exchange opinion would be held semi-annually or quarterly. The WG Chair asked what members thought of this idea.

The WG members had the following opinions.
- We will also require a revision of the set up of the procedure I think, but because it will take time to make employees thoroughly aware of the process within companies, in practical terms a revision once a year is the most we can do.
- Because we also face the issue of dealing with originators and investors, I have my doubts of whether making an annual revision is necessary.

The WG Chair said that there also was the issue of what type of meeting body should be used to conduct the revisions, and asked whether the Secretariat had any ideas. The Secretariat said that one possible proposal was to set up a standing WG under the Financial Instruments Committee and carrying out discussions within that WG if necessary. However, since the setting up of such a standing WG would be completely up to the Financial Instruments Committee, if the Working Group felt that they wanted to go in that direction, the JSDA Secretariat would have to consult the Financial Instruments Committee about it.

The WG Chair made the following proposal, which was approved.

- An annual meeting would be held to revise the UIDF. Quarterly meetings would be held to collect information and exchange opinions.
- The above meetings would be held by a standing WG established under the Financial Instruments Committee.
- The Secretariat would consult the Financial Instruments Committee about the above WG.
- The issue of the frequency of revisions of the set up of the procedure following introduction would be discussed at a later date.

(End of document).