

Article Title: ARCHIVE | Legal Criteria: Japanese Asset Isolation And Special-Purpose Entity Criteria--Structured Finance Data: (EDITOR'S NOTE: — This article is no longer current. It was superseded by "Structured Finance: Asset Isolation And Special-Purpose Entity Methodology," published on March 29, 2017. ) 1. This article describes S&P; Global Ratings' methodology and assumptions for assessing legal risks in Japanese structured finance transactions. This update supplements and should be read in conjunction with the global criteria titled "Asset Isolation And Special-Purpose Entity Criteria--Structured Finance," published May 7, 2013 (hereafter referred to as the "AISPE criteria"). This article is related to our criteria article "Principles Of Credit Ratings," which we published on Feb. 16, 2011. 2. [This paragraph has been deleted.] SCOPE OF THE CRITERIA 3. These criteria apply to all Japanese structured finance transactions that look to incorporate asset isolation and/or the insolvency remoteness of special-purpose entities (SPE) used in securitization transactions. The criteria consider key issues for the Japanese market and should be read in conjunction with the AISPE criteria. These criteria may be modified or supplemented to the extent that S&P; Global Ratings publishes asset-specific criteria that discuss asset isolation or the insolvency remoteness of SPEs. 4. For the purposes of this article, the terms "insolvency remote" and "insolvency remoteness" are used interchangeably with the terms "bankruptcy remote" and "bankruptcy remoteness," respectively. SUMMARY OF CRITERIA UPDATE 5. These updated criteria provide the market with a description of how we consider legal risks that could affect our assessment of the creditworthiness of Japanese structured finance debt issues. In Japan, S&P; Global Ratings will apply the criteria set out in the AISPE criteria article, with some limited adjustments outlined herein to reflect their application in Japan. 6. In Japan, S&P; Global Ratings applies the same criteria as those set out in "Multiple-Use Special-Purpose Entity Criteria--Structured Finance," published May 7, 2013. 7. In the past, we published certain articles discussing methodologies and assumptions related to how we assess legal risks in the context of our structured finance ratings for specific jurisdictions or asset types. The criteria contained herein do not constitute a departure from our existing views. Rather, following the release of the AISPE criteria, this article provides an updated description of the framework for how we assess legal risks in Japanese structured finance transactions. The criteria, as set out in this article, are not intended to be read as prescriptive but rather as general criteria that guide us when we consider legal issues we view as relevant to the credit analysis of Japanese structured finance securities. 8. [This paragraph has been deleted.] 9. [This paragraph has been deleted.] METHODOLOGY AND ASSUMPTIONS 10. The AISPE criteria provide the market with a description of how we consider legal risks that may affect our assessment of the creditworthiness of structured finance debt issues. That article focuses on a discussion of the below topics. Asset isolation in securitization The insolvency remoteness of SPEs 11. The AISPE criteria article also discusses related legal issues that could affect insolvency remoteness: clawback risk, setoff risk, and tax risk. In addition, that article discusses challenge risk in securitizations and sources of comfort on legal issues. 12. In Japan, S&P; Global Ratings will apply the AISPE criteria with some limited adjustments outlined herein to reflect their application in Japan. Asset Isolation 13. We consider that, as a general matter, Japanese law will support a transfer of assets from an originator to a transferee such that the transferred assets will not be treated as part of the originator's (or former owner's) estate, which has become subject to an insolvency proceeding. 14. Legal counsel for Japanese transactions typically provide legal opinions that confirm a true sale ("baibai" or "joto"), subject to qualifications and assumptions generally accepted by the market. The opinions confirm, to the extent possible, that the transfer of assets from an originator to an issuer SPE would not be deemed a secured transaction in the event of an originator bankruptcy, provided that perfection formalities are completed and S&P; Global Ratings considers the perfection formalities to be relatively minimal and in line with international precedents. Insolvency Remoteness Of SPEs 15. S&P; Global Ratings' criteria for insolvency remoteness are globally consistent, although their application may vary in detail between jurisdictions. Parties to Japanese securitization transactions typically use several types of SPEs, including: stock companies ("kabushiki kaisha"; KK), limited liability companies ("godo kaisha"; GK), limited liability companies established for securitization purposes ("tokutei mokuteki kaisha"; TMK), general incorporated associations ("ippan shadan hojin"; ISH), trusts ("shintaku"), and Tokyo branches of overseas SPEs, including Cayman special purpose companies (Cayman SPC) and Delaware limited liability companies. 16. S&P; Global Ratings considers each of

these types of entities to be capable of being insolvency remote as discussed in these criteria and subject to the relevant transaction documentation reflecting the elements of insolvency remoteness explained in paragraphs 13-35 of the AISPE criteria: Restrictions on objects and powers; Debt limitations; Independent directors; Restrictions on mergers or reorganization; Limitations on amendments to organizational documents; Separateness; and Security interests over assets. 17. The AISPE criteria also consider the role that the entity undertakes in the relevant transaction, including whether it is a borrower or issuer SPE, or a parent SPE. In Japan, for example, borrower-level SPEs in commercial mortgage-backed securities (CMBS) pool transactions are generally assessed in line with the U.S. CMBS practice-level criteria ("Assessing Borrower-Level Special-Purpose Entities In U.S. CMBS Pools: Methodology And Assumptions," published Nov. 16, 2010). 18. The stock or equities of an issuer KK, GK, or TMK may be held by an ISH or Cayman SPC whose ordinary shares are held by, for example, a charitable trust. In this way, the issuer may be treated as an orphaned special-purpose company (SPC) in line with our AISPE criteria. An ISH is typically not used as the issuer because under Japanese law it may not pay interest on its foundation debts ("kikin") or issue any shares or membership interests. 19. Japan's Trust Law and Bankruptcy Law were revised in 2007 to increase the effectiveness of Japanese trusts as SPEs, including in the context of securitization transactions. In particular, the Trust Law makes it clear that trust assets do not form part of a trustee's bankruptcy estate and provides for the court appointment of a trust property administrator ("shintakuzaisan kanrisha") if required. It is also important that the transaction documentation contain elements that mitigate the risk of a trust's termination during the life of a transaction. If an asset-backed loan (ABL) is advanced to the trust SPE, it is also important to consider the effectiveness of priority between the ABL and the trust's beneficial interests, as well as any incentive for the ABL lender to file a petition to commence an insolvency proceeding with respect to the entrusted assets. 20. Similarly to other jurisdictions, insolvency remoteness is also usually supported in Japan through contractual provisions such as nonpetition clauses, undertakings from specified persons such as directors not to file for insolvency of the SPE, and limited recourse clauses. There is some doubt as to whether limited recourse clauses will be implemented in an obligor's insolvency proceedings, and there is an argument that a Japanese court may accept a petition made contrary to a nonpetition undertaking. Accordingly, transaction parties in Japanese securitizations typically take further measures to reduce the incentive for creditors and other specified parties to file for insolvency, including security in favor of investors and subordination agreements that prioritize payments to investors. Related Legal Issues 21. As noted in the AISPE criteria (see especially ¶¶ 36-43), we may identify related legal issues that may affect our assessment of asset isolation or the insolvency remoteness of SPEs. The sections below discuss some of these legal issues in the context of Japan's legal system. Clawback risk ("hinin" and "sagai kou torikeshi") 22. Trustees in Japanese insolvency proceedings have the power to avoid certain transactions, a typical feature of insolvency law regimes. Japanese insolvency laws were amended in 2004, however, to make it clear that a sale of real estate by an insolvent entity at a fair market price would not be open to challenge provided that the proceeds of the sale were not to be concealed or gifted to another person. 23. Any analysis of clawback risk is necessarily qualitative, because the court's analysis would be fact-based and usually has the benefit of hindsight. Parties to Japanese securitizations, however, typically structure the transactions to minimize the risk that the transfer of any assets will be subject to such a challenge. Comfort On Legal Issues 24. Courts in Japan have not yet fully analyzed or expressed a view on certain legal issues relevant to securitization, including, for example, the status of executory contracts in the context of securitizations of lease receivables. The Japanese securitization market is mature, however, and issues that the courts have not analyzed are often the subject of general consensus among market participants and their legal counsel such that appropriate legal opinions are typically available to transaction parties, including opinions relating to taxation. Appendix: Summary Of Historic Changes To The Article 25. These criteria became effective on the original publication date of this article on Aug. 21, 2013. At that time, this article fully superseded the following criteria: "Eligibility Of New SPV Entities In Japan Structured Finance Market," published June 26, 2006; "Bankruptcy Remoteness Of Special-Purpose Vehicles In Japanese Securitization Transactions," published Oct. 17, 2006; and "Bankruptcy Remoteness Of Trusts In Japan," published April 24, 2008. It also partially superseded "Rating Methodology For Japan Business Securitization,"

published July 4, 2006.) 26. We republished the article following our periodic review completed on June 23, 2016. As a result of our review, we deleted outdated sections that previously appeared in paragraphs 2, 5, and 6 related to the initial publication of the article, and which were no longer relevant, and made minor editorial updates throughout the article. RELATED CRITERIA AND RESEARCH Asset Isolation And Special-Purpose Entity Criteria--Structured Finance, May 7, 2013 Guarantee Criteria--Structured Finance, May 7, 2013 Multiple-Use Special-Purpose Entity Criteria--Structured Finance, May 7, 2013 Principles Of Credit Ratings, Feb. 16, 2011 Assessing Borrower-Level Special-Purpose Entities In U.S. CMBS Pools: Methodology And Assumptions, Nov. 16, 2010 Debt Recovery For Creditors And The Law Of Insolvency In Japan, Feb. 28, 2008 These criteria represent the specific application of fundamental principles that define credit risk and ratings opinions. Their use is determined by issuer- or issue-specific attributes as well as S&P; Global Ratings' assessment of the credit and, if applicable, structural risks for a given issuer or issue rating. Methodology and assumptions may change from time to time as a result of market and economic conditions, issuer- or issue-specific factors, or new empirical evidence that would affect our credit judgment.