FundsTalk

April 2012

Hot Topics Corner

On March 22nd, Kramer Levin's Private Equity and Hedge Fund practice group hosted a panel discussion on the SEC's increased scrutiny of valuation and fee allocation practices of asset managers. Russell Pinilis, Barry Berke and Thomas Balliett identified potential areas of exposure to an SEC inquiry and proposed methods for compliance.

The SEC is investigating the valuation methodologies that funds use in stated returns for fund raising purposes. The SEC's interest in fund performance data signifies the importance of clients to review their compliance and valuation policies.

The panelists advised how to prepare for a potential SEC inquiry and shared the significance of applying consistent asset valuation methodologies and investor reporting. A well-documented, reasoned and consistent form of valuation across marketing materials and security filings is key. Fund sponsors are encouraged to carefully review their compliance policies and procedures to confirm that each is reasonably designed and evenly applied in a manner that is consistent with the legal obligations and fiduciary duties of such sponsors to their clients. These policies can evidence compliance with the securities laws.

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Editors

If you have any questions or would like more information concerning any of these topics, please contact one of the authors or:

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CLO 2012 Update

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After years of being lumped together with CDO transactions collateralized by sub-prime RMBS and other poorly performing ABS, the CLO market appears to have differentiated itself and rebounded strongly. In 2011, 28 new CLO transactions totaling $12.5 billion closed, more than three times the total in 2010. Thousands of vintage CLO classes previously downgraded were upgraded by the rating agencies in 2011. In the first quarter of 2012, the market saw new CLOs totaling over $5 billion by American Money Management Corp., Credit Suisse Asset Management, The Carlyle Group, ING Alternative Asset Management, Onex Credit Partners, Octagon Credit Investors, Invesco Senior Secured Management, Apollo Credit Management, LCM Asset Management, Ares Management, Babson Capital Management, Symphony Asset Management and others. Market participants believe that 2012 could see up to $20 billion in primary broadly syndicated CLO transactions as well as substantial growth in private bespoke CLO transactions. Below are some key issues for the CLO market in 2012.

Risk Retention

In March 2011, federal agencies jointly issued proposed risk retention rules that could impact the CLO market. The proposed rules include a footnote that identifies the collateral manager of a CLO as the sponsor required to retain a 5% credit risk in the securitized assets. Characterizing the collateral manager as a sponsor will likely have an adverse impact on the viability of the CLO market, particularly more broadly syndicated CLOs, as few collateral managers have the resources or the inclination to hold such a level of non-hedged credit risk. Market participants argue that (i) the footnote is inconsistent with a plain reading of the proposed rules' definition of "sponsor"; (ii) requiring CLOs and collateral managers to observe risk retention requirements is outside the scope of the Dodd-Frank Act's mandate; (iii) "skin in the game" was directed at parties engaged in an "originate to distribute" model that is not applicable to collateral managers;

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Effective Collateral Protection for Swaps

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In the Lehman Brothers collapse, numerous market participants trading derivatives lost substantial amounts of initial margin they had posted to Lehman as a counterparty to secure their swaps. Initial margin, an amount of liquid collateral protecting Lehman against adverse price movements arising from the volatility of a particular trade and counterparty credit risk, was usually commingled with Lehman's own funds and rehypothecated. In the bankruptcy, trading counterparties were essentially left with a mere general unsecured claim for a corresponding amount. No regulator was to blame; swaps were largely unregulated.

Congress subsequently passed the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") with its promise to regulate the entire derivatives market and protect market participants by, amongst other things, imposing regulatory requirements regarding margin segregation for both cleared and uncleared swaps. Under Dodd-Frank, funds posted in connection with cleared swaps would have to be segregated and segregation would be optional (for most end-users) for funds posted in connection with uncleared swaps.

This update provides an overview of regulatory requirements regarding collateral protection under Dodd-Frank for both uncleared and cleared swaps as well as related industry initiatives.

Uncleared Swaps

Last year, the Commodities Future Trading Commission (the "CFTC") and other regulators proposed regulations affecting collateral posted in connection with uncleared swaps. The regulations, which are expected to be finalized later this year, would impose strict margin requirements and force swap dealers to collect initial and variation margin from many counterparties that may not currently post any collateral. In addition, for uncleared swaps between swap dealers and major swap participants, the proposed rules would require all initial margin to be held by an independent, third-party custodian. For all other uncleared swaps, initial margin segregation would not be mandatory and swap dealers would only be required to offer their counterparty the option to have initial margin held in a segregated account with an independent, third-party custodian.

Market participants opting to have their initial margin segregated may use the sample initial margin segregation terms and provisions published by ISDA (the "Segregation Provisions") in negotiating their collateral segregation arrangements. The purpose of the Segregation Provisions is to provide market participants with a menu of suggested provisions that they can incorporate in their collateral segregation arrangements and further customize to meet their needs. The Segregation Provisions are intended to be used in the context of a tri-party custody arrangement amongst a pledgor, a secured party and an unaffiliated custodian. They address a number of issues related to the release of collateral, including (i) which of the end-user or the secured dealer may secure exclusive access to the collateral and upon the occurrence of which events; (ii) actions that the moving party needs to take in order to obtain exclusive rights to, and release of, the collateral; (iii) timing of the collateral release by the custodian; and (iv) available dispute rights in the event that the end-user or the dealer opposes the actions taken by the other party.

While the Segregation Provisions are a step in the right direction, they do not entirely eliminate counterparty credit risk; market participants have merely replaced the credit risk of their swap counterparty with that of the custodian. Hopefully, the latter will prove to be better.

> Market participants should carefully structure their uncleared swaps collateral segregation arrangements in a manner that suits their risk tolerance and business needs.

Cleared Swaps

With respect to cleared swaps, earlier this year, the CFTC adopted its final rules under Dodd-Frank regarding the protection of cleared swap collateral and favored the so-called legal segregation with operational commingling model (the "LSOC model").

Under the LSOC model, clearinghouses and futures commission merchants clearing swaps on behalf of customers must segregate customer collateral from their own property. They may keep cleared swap collateral

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of all customers together pre-bankruptcy, in a separate account, though they must identify the property of each individual customer on their books and records and update that information at least once each business day.

The LSOC model is a departure from the current rules applicable to futures where, in the event of a double-default (when a default by a customer forces its clearing member to default), the clearinghouse is permitted to use non-defaulting customer collateral to meet such a loss and, therefore, non-defaulting customers of the defaulting clearing member would be exposed to loss due to so-called "fellow customer risk." Under the LSOC model, in the event of a double-default, the clearinghouse, to satisfy amounts owed to it, may only access the collateral posted by the defaulting customer, and not the collateral posted by the other (non-defaulting) customers, thereby mitigating fellow customer risk.

However, the CFTC recognized that the LSOC model provides limited protection from operational risk (i.e., the risk that a clearing member fails to properly segregate cleared swaps customer collateral) as well as investment risk (i.e., the risk that a clearing member experiences losses on its investment of cleared swaps customer collateral, which it cannot cover using its capital). In such a case, customers would share pro rata in any remaining cleared swap collateral. The paradox is that market participants may find themselves less protected in collateral arrangements for cleared swaps than for uncleared swaps assuming they enter into and properly negotiate tri-party custody agreements for uncleared swaps.

Conclusion

Market participants should carefully structure their uncleared swaps collateral segregation arrangements in a manner that suits their risk tolerance and business needs. In particular, they should make sure that the documentation accurately reflects the business deal with their counterparty and their understanding of how, when, and to whom the collateral should be released.

The Segregation Provisions provide a good starting point to identify the main issues to be addressed and how they can be resolved — though further customization will often be necessary — and they also help level the playing field for swap participants when facing dealers by enabling a constructive discussion with market-driven solutions for these complex issues.

For cleared swaps, market participants need to understand what segregation really means and how their property will be treated in a bankruptcy or liquidation context. They should identify deficiencies in the regulatory framework and design risk mitigation strategies, where available, to address those gaps and understand their costs and limits. ■

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(iv) through subordinate and/or incentive fee structures, collateral managers already have "skin in the game"; and (v) CLOs have performed well and structures have held up throughout the crisis and imposing risk retention requirements in CLOs would damage a vibrant market for no credible policy reason. Industry comment letters are asking for clarity that CLOs are not subject to the risk retention rules or, alternatively, safe harbor provisions for CLOs and/or an expansion of the definition of a "qualifying commercial loan" exempt from risk retention. Given the vast dissatisfaction with the proposed rules, it is expected that the agencies will re-propose rules some time during 2012 with final rules in 2013. For CLOs, if applicable, the risk retention rules will be effective two years after the final rules are published.

In addition, Article 122a of the European Union Capital Requirements Directive requires credit institutions regulated in the European Economic Area investing in securitization transactions (including CLOs) to ensure that the originator, sponsor or original lender retain a 5% economic interest in the securitized assets. Article 122a appears to have limited the marketability of CLOs to European institutional investors.

Volcker Rule

In October 2011, federal agencies jointly issued proposed rules to implement the Volcker Rule which prohibits and restricts banking entities from engaging in proprietary trading and having certain interests in hedge funds and private equity funds. Hedge Funds and private equity

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funds are covered under the proposed rules by reference to Sections 3(c)(1) and (7) of the Investment Company Act. While it is true that most hedge funds or private equity funds utilize these exemptions, so do many other securitization vehicles, including CLO issuers. If prohibitions on banking entity sponsorship and ownership contained in the Volcker NPR were to apply to CLOs, CLOs would be prohibited from engaging in tasks central to their existence, such as holding cash received from the sale or repayment of loans, investing in short-term debt instruments, or containing investment baskets for other types of debt securities like high-yield bonds. Further, most balance sheet CLOs would not be permissible and traditional warehousing arrangements may not be possible. This result appears to be in conflict with the stated rule of construction that there be no limit or restriction on the ability of banking entities to sell or securitize loans. Market participants are hopeful that the final Volcker Rule will (i) exempt all securitization vehicles and (ii) expand and clarify the definition of which "loan securitizations" are exempt from the Volcker Rule. The Volcker Rule will become effective on July 21, 2012, whether or not any rules are approved; however, banks will be given until July 21, 2014, to comply with the Volcker Rule and the FRB has additional discretion to extend the implementation period.

Third Party Due Diligence

In June 2011, the SEC issued proposed Rule 15Ga-2 and amendments to Form ABS-15G, which would require the issuer or underwriter of a rated asset-based security (whether registered or not) to disclose, in the new Form ABS-15G, the identity of the securitizer and the findings and conclusions of any third-party performing "due diligence services" and the resulting "due diligence report." The SEC also proposed a new Rule 17g-10 and Form ABS Due Diligence-15E which requires third party "due diligence providers" to provide rating agencies with a written certification that includes a summary of the findings and conclusions of such due diligence. As many of the activities of a collateral manager could be considered "due diligence services," depending on the final rules, a collateral manager could be treated as a third party "due diligence provider." Final rules are expected during 2012.

Re-Proposal of Regulation AB II

In July 2011, the SEC re-proposed disclosure rules to address public comments and resolve a number of the discrepancies between the Dodd-Frank Act and prior proposed rules. A key open issue is the highly controversial proposal requiring public-style disclosure in private offerings that rely on exemptions from the registration requirements of the Securities Act of 1933 (such as Rule 144A and Regulation D). Under such proposal, an issuer would be required to provide to any investor, upon request, the same information that would be made available to investors in a registered public ABS offering, including ongoing reports, updated asset by asset data and periodic reports. The failure to provide such information to investors could bring about an enforcement action by the SEC.

FATCA

The Foreign Account Tax Compliance Act ("FATCA") was enacted to combat tax evasion by U.S. persons holding investments in offshore accounts. The IRS recently published proposed regulations on FATCA which are expected to be finalized before the end of 2012. FATCA requires foreign financial institutions ("FFIs") to report to the IRS certain information about financial accounts held by U.S. taxpayers or by foreign entities in which U.S. taxpayers hold a substantial ownership interest. If an FFI does not enter into an agreement with the IRS to report such information (an "FFI Agreement"), the FFI will be a deemed a non-Participating FFI ("non-PFFI"). U.S. persons making payments to a non-PFFI generally will be required to deduct and withhold 30% of the payments and remit such amount to the IRS. Unless a grandfathering provision applies (generally, for obligations (other than equity) issued or entered into before January 1, 2013), beginning on January 1, 2014, U.S. persons making payments to a CLO issuer generally will be required to withhold unless such CLO issuer has an FFI Agreement in place with the IRS which qualifies it as a Participating FFI ("PFFI") or the CLO issuer is otherwise deemed to be compliant with FATCA. An FFI Agreement (a form of agreement has not yet been introduced by the IRS) will generally require the CLO issuer to (i) obtain information regarding its debt and equity holders and perform diligence to determine which accounts are U.S. accounts; (ii) annually report to the IRS information regarding its U.S. accounts; (iii) beginning in 2017, deduct and withhold 30% of "pass-through payments" made to non-PFFIs and investors who fail to comply with reasonable requests for necessary information; (iv) comply with requests by the IRS for additional information regarding any of its U.S. accounts; (v) obtain a waiver of any privacy protections

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under foreign law regarding any of its U.S. accounts or close such account; and (vi) adopt written policies and procedures governing its FATCA compliance, conduct periodic internal compliance reviews and periodically certify to the IRS that it is in compliance with FATCA. It is anticipated that CLO issuers will be able to begin applying to the IRS for PFFI status as of January 1, 2013. A CLO issuer must enter into an FFI Agreement with the IRS by June 30, 2013 to ensure that it will be identified as a PFFI by the IRS in sufficient time to allow U.S. withholding agents to verify the CLO issuer's PFFI status and refrain from FATCA withholding which begins on January 1, 2014. A CLO issuer that enters into an FFI Agreement after June 30, 2013 might not be identified as a PFFI by the IRS in time to prevent FATCA withholding by U.S. payors beginning on January 1, 2014.

IRC Section 457A

As part of the Emergency Economic Stabilization Act, Section 457A was added to the Internal Revenue Code in 2008. That section generally requires fund managers who receive deferred compensation from offshore entities to include such compensation in taxable income when such compensation is no longer subject to a "substantial risk of forfeiture." Compensation under Section 457A is subject to "substantial risk of forfeiture" only if it is conditioned upon the future performance of substantial services. If the amount of compensation is not determinable when no longer subject to a risk of forfeiture, then the manager is subject to an interest charge on the income when it is determinable, plus a penalty equal to 20% of the compensation. Subordinate management fees and incentive management fees are generally not determinable until they are paid in accordance with the priority of payments and also arguably are not subject to "substantial risk of forfeiture." As a result, collateral managers could find that such subordinate management fees and incentive fees may be subject to an interest charge and a 20% penalty. Collateral managers should consider this possible tax when structuring their fee arrangements.

Investment Adviser Registration and Reporting

Effective July 2011, the Dodd-Frank Act repealed the commonly used "private adviser exemption." Subject to certain exemptions that few collateral managers will be in a position to utilize, non-registered collateral managers must be registered with the SEC by March 30, 2012 (initial applications for registration on Form ADV should have been filed with the SEC by February 14, 2012). Registered investment advisers must adopt a written compliance program and are subject to specific regulatory restrictions in key operational areas, including advertising and marketing, custody of client assets, books and records, cross trades and principal trades, and client solicitations.

Most registered investment advisers to private funds will also be required to file Form PF, which reports detailed information about the assets advisers manage. Form PF filings will be due in August 2012 for the largest advisers, and in 2013 for most smaller advisers.

While, for purposes of Form ADV, CDOs and CLOs are considered "private funds" and all their assets must be included in calculating "regulatory assets under management," Form PF separates private funds into seven categories of which "securitized asset fund" would appear to include CDOs and CLOs. This allows CDOs and CLOs to comply with the lower reporting threshold of annual, aggregated reporting in contrast to managers of large hedge funds who must report quarterly and include more detailed portfolio-level information on a fund by fund basis. Form PF is filed electronically, and is not publicly available, although it may be shared by regulators and will be provided to the FSOC.

Structure and Document Changes

Compared to older transactions, new CLOs appear to be less complex and less levered, have better defined and more investor-directed eligibility criteria and shorter reinvestment periods. In addition, as the financial crisis unfolded, it became apparent that CLO transaction documents were not always flexible enough or did not contemplate some of the situations that arose. Expect to see changes in documents to affirmatively deal with, among other things, (i) the *Concord Real Estate CDO* scenario where junior notes were submitted for cancellation to cure OC tests, (ii) the *Black Diamond CLO* issues relating to trade settlements and reinvestment periods, (iii) the *Zing VII CDO* issues related to bankruptcy remoteness, non-petition clauses and rights to object to involuntary bankruptcy, (iv) how "amend to extend" transactions should be treated in the context of reinvestment criteria and reinvestment periods, (v) timing of rating agency confirmations, (vi) informational requirements under FATCA and (vii) tax issues arising in connection with exchange workouts of loans. ■

Mine Control and Mind Control: How a Special Committee with a "Controlled Mindset" Approved Overpaying for a Mining Company Bought from a Controlling Stockholder

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In a recent opinion issued by the Delaware Court of Chancery, *In re Peru*, the Court awarded $1.26 billion in damages to address a failed special committee process in a related party purchase of a business from a controlling stockholder. The case provides some key take-aways on forming a "well-functioning" special committee when considering a related party transaction.

Facts

Grupo Mexico, the majority stockholder of Southern Peru, an NYSE-listed mining company, approached Southern Peru with a proposition: purchase Grupo Mexico's non-publicly traded mining company (Minera) for $3.1 billion of Southern Peru stock. Southern Peru set up a special committee with the mandate to evaluate the transaction. The committee engaged Goldman Sachs as a financial advisor. Based on its initial analysis, Goldman Sachs set a value for Minera at approximately $1.7 billion — $1.4 billion less than the initial value proposed by Grupo Mexico. Troubled by this outcome, the committee sought to employ other valuation methodologies to gain greater confidence with the transaction.

Instead of using a straight valuation of Southern Peru and Minera, which would have valued Minera based on its performance and Southern Peru's stock consideration based on its market value, the committee adopted a "relative valuation" approach. The committee justified this approach in part by concluding that Southern Peru's publicly traded stock was overvalued. In conducting this valuation, the committee approved "topping up" the value of Minera in a number of respects. First, the committee applied Southern Peru's EBITDA multiples to Minera even though Southern Peru was a market-tested public company that was thriving and nearly debt-free while Minera was privately held and in distress. The committee also optimized the projected results for Minera by engaging a mining consultant to update life-of-mine plans and projections (which was not done for Southern Peru). Southern Peru ended up beating EBITDA projections by 135%, while the projections used for Minera were much closer to actual performance. To further decrease the value of Southern Peru's stock, Southern Peru issued a $100 million special dividend, the majority of which went to Grupo Mexico as the controlling stockholder. All of this had the effect of making the value of the "give" look closer to the value of the "get."

The committee included one director (Harold Handelsman) who was an employee of a large stockholder (Cero). Cero was, at that time, negotiating with Southern Peru (i.e. Grupo Mexico as the controlling stockholder) for registration rights on its Southern Peru stock. Handelsman was leading these negotiations on behalf of Cero, and registration rights were granted on the same day that the committee approved the transaction (with Handelsman abstaining at the last minute due to a perceived conflict of interest). In exchange for its registration rights, Cero agreed to vote its shares in favor of the transaction if it was recommended by the committee.

Deal Terms

The committee and Grupo Mexico ultimately agreed to a deal at a fixed purchase price of 67 million shares of Southern Peru stock with a market value at signing of $3.1 billion, conditioned on a two-thirds vote of the stockholders. At that time, Southern Peru had two large minority stockholders, either one of which, voting with Grupo Mexico to approve the transaction, would satisfy the two-thirds requirement. One of these stockholders, Cero, was obligated to vote its shares in accordance with the recommendation of the committee. The other stockholder (Phelps Dodge) was granted registration rights in exchange for its expression of "current intent" to vote in favor of the merger. Although the value of Southern Peru's stock increased substantially over the next several months, the committee did not revisit its initial recommendation. When all was said and done, Southern Peru purchased Minera for approximately $3.75 billion (more than $500 million above the initial asking price).

Transaction is Challenged

A stockholder sued to challenge the transaction as being unfair to Southern Peru's minority stockholders. In its lengthy 100-page opinion, the Court concluded that the committee was not "well-functioning" and that the transaction was decidedly unfair, granting $1.26 billion in damages to Southern Peru.

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The Court's opinion offers some key take-aways described below on the ingredients for a "well-functioning" special committee when considering a transaction with a controlling stockholder:

Key Take-aways

A Special Committee Must Be Clearly Empowered to Negotiate and Ultimately Prepared to Reject the Transaction. In this case, the mandate of the committee was unclear, creating a reluctance to negotiate. The Court stressed that the committee exhibited a "controlled mindset" where the focus was on "finding a way to get the terms of the [deal] structure proposed by Grupo Mexico to make sense, rather than aggressively testing the assumption that the Merger was a good idea in the first place." As a result, the committee took "strenuous efforts to justify a transaction at the level originally demanded by the Controlling Stockholder" despite the value of Minera being worth far less than $3.1 billion.

Key Take-away: A special committee must clearly have the power to negotiate and must also be prepared to reject the transaction. The Court also suggested that a special committee should be empowered to propose strategic alternatives. It seems that this would be part of the consideration of a special committee that is empowered to negotiate a transaction, and it is not clear that there needs to be an explicit empowerment to pursue alternatives.

Consider Indirect Conflicts of Committee Members. While the Court refrained from finding that this was "the kind of self-dealing interest that would deem Handelsman interested in the Merger," the Court did note that the negotiation for registration rights had the undeniable effect of making Handelsman reluctant to just say no — saying no meant no liquidity for his employer.

Key Take-away: Boards should ensure that special committee members will not receive, directly or indirectly, benefits from approving the transaction beyond those received by minority holders.

Consider Changed Circumstances. The Court was critical of the committee for treating the deal as a foregone conclusion at the time of signing despite having negotiated for the ability to change its recommendation if its fiduciary duties so required. By the time of the stockholder vote, Southern Peru's stock price increased substantially, causing Southern Peru to pay an additional $500 million.

Key Take-away: The Court suggested that the failure of a special committee to reassess a recommendation in light of significant changed circumstances could influence the "entire fairness" analysis in a related party transaction.

Greece Restructures

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Terms restructuring Greece's 206 billion euros of sovereign debt, which faced likely and imminent default, were formally approved by the necessary 2/3 majority of bondholders on March 9. What now?

First, let's quickly review how the restructuring — which seemed practically impossible, albeit politically imperative, just a few months ago — came about. The original bonds were, for the most part, governed by Greek law, and contained terms requiring unanimous approval for changes in bondholder rights.

The restructuring terms involved the exchange of the outstanding bonds for (1) new Greek bonds having a face value equal to 31.5% of the original principal amount (and reduced future interest payments), (2) FESF securities having a two-year maturity and a face value of 15% of the original principal amount, and (3) Greek GDP-linked

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securities in a notional amount equal to the face value of the new Greek bonds issued to each bondholder.

Since it seemed clear that 100% of the bondholders would not agree to a 53.5% nominal haircut (and net present value losses of about 74%, taking into account the reduced future interest payments) — even if the alternative was Greek default and, as a result, perhaps an even greater haircut — to ensure approval on February 23, 2012 the Greek government retroactively inserted in Greek-governed bonds (i.e., 95.7% of the outstanding, the others are subject to foreign law), via law 4050/2012, collective action clauses ("CAC") reducing the approval threshold from 100% to just 75%.

This hat trick enabled Greece to avoid defaulting (for now) while at the same time reducing its ultimate payment obligation (74%!) with less than the originally-contracted unanimous approval. It's true that inserting the CAC in a manner which led to all of the bondholders' payment rights being reduced constituted sufficient basis for a Restructuring Credit Event to be declared by the ISDA Credit Derivatives Determinations Committee and thus a CDS auction (which took place on March 19, 2012). However, neither the CAC itself nor the declaration of a Restructuring Credit Event constitutes a payment default for purposes of cross-default clauses, and thus (again, for now), it seems that a wide scale acceleration/default of Greece's outstanding debt has been averted.

One could argue that inserting a CAC is unfair, although in essence it simply democratizes bondholder decisions, allowing a majority to rule. (Emerging markets have included CACs in their sovereign debt for a while, and current EU proposals foresee doing so as a matter of course in euro government bonds issued after 2013.)

More significant from a legal standpoint is the retroactive effect of the law, which can easily be seen to constitute a prohibited taking of private property, both under the Greek constitution and the European Convention on Human Rights. Accordingly, it seems that litigation contesting the constitutionality of the retroactive CAC insertion by Greece is possible, if not likely.

Article 17 of the Greek constitution is clear: "*No one shall be deprived of his property except for the public benefit which must be duly proven, when and as specified by statute and always following full compensation corresponding to the value of the expropriated property.*" Although the CAC insertion could be argued to have been "for the public benefit," in the sense that it was necessary to avert the certain disaster that would have been caused by a massive Greek default, by its terms the restructuring involved less than "full compensation." That said, since the constitutionality of the 4050/2012 law will be judged by Greek courts, a finding in favor of dissenting bondholders might be hard to obtain, regardless of the merit of their position.

At the European level, the law is just as clear: the European Convention on Human Rights (article 1 of Protocol No. 1) states "*Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.*" Although Europe's interests are aligned with Greece in this regard, there seems a slightly better chance that the validity of the retroactive law might be found wanting by the European Court of Human Rights.

The new bonds and securities issued as part of the restructuring exchange will be subject to English law, which would not allow a retroactive insertion of a CAC clause, so one would hope that this issue will not repeat itself for the new Greek debt. Whether Greece could pull another rabbit out of its hat — e.g., by making it illegal to repay amounts under the new securities — merits close consideration by those exposed to such debt. ■

Practice Areas

This publication is a collaboration of the following practice areas:

- Capital Markets
- Claims Trading and Distressed Investment Advice
- Corporate
- Corporate Restructuring and Bankruptcy
- Electronic Discovery
- Employment Law
- Executive Compensation
- Financial Services/ Investment Management
- Intellectual Property
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- Mergers and Acquisitions/ Joint Ventures
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- Securitization
- Swaps & Derivatives
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