CREDIT DERIVATIVES DETERMINATIONS COMMITTEE FOR THE AMERICAS

MEETING STATEMENT OCTOBER 1, 2024

This Meeting Statement is not binding with respect to any other determination of any Credit Derivatives Determinations Committee, nor does it preclude any other Credit Derivatives Determinations Committee, or any member of such committee, from making a different determination when resolving a similar question in the future, including any question that relates to similar facts. Furthermore, the discussion summarized below is not, and does not purport to be, an exhaustive list of factors that each member of the Credit Derivatives Determinations Committee for the Americas considered.

Prior to the publication on September 20, 2024 of the Final List of Deliverable Obligations for the Avon Products, Inc. (**Avon**) Auction (the **Avon Final List**), the Credit Derivatives Determinations Committee for the Americas (the **Americas DC**) received a challenge by the U.S. special situations trading desk of Barclays Bank plc and certain other Eligible Market Participants (the **Challenge Submission**) relating to the exclusion from the Initial List of Deliverable Obligations for the Avon Auction (the **Avon Initial List**) of the USD 405,000,000 promissory note dated May 17, 2022 and payable by Avon to the order of Natura & Co UK Holdings Plc (**Natura**) (the **Promissory Note)**[1]. The Challenge Submission was submitted pursuant to Rule 3.3(d) of the DC Rules and published on the DC Secretary Website pursuant to the DC Rules[2]. No response to the Challenge Submission was received by the DC Secretary prior to the deadline for Response Submissions.

After reviewing the material submitted in connection with the Challenge Submission, the Americas DC Resolved the Challenge Submission and determined that the Promissory Note should be excluded from the Avon Final List. The Americas DC is publishing this statement (the **Meeting Statement**) in relation to its decision to exclude the Promissory Note from the Avon Final List and to address the positions presented by the Challenge Submission. This Meeting Statement should be read in conjunction with the Americas DC's meeting statement dated September 12, 2024 (the **Initial Meeting Statement**), which was published in relation to the publication of the Avon Initial List[3].

For the purposes of this Meeting Statement, the Americas DC refers to:

(a) the 2014 ISDA Credit Derivatives Definitions, as published by the International Swaps and Derivatives Association, Inc. (**ISDA**) (the **2014 Definitions**); and

(b) the Credit Derivatives Determinations Committees Rules, as published by DC Administration Services Inc. on behalf of ISDA (as amended as of the date hereof, the **DC Rules**).

Each capitalized term used and not otherwise defined herein has the meaning given to such term in the 2014 Definitions, the DC Rules or the Promissory Note, as applicable.

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1 See Avon Form 8-K dated May 17, 2022 at Exhibit 4.1, available here.

2 *Available at*, https://www.cdsdeterminationscommittees.org/documents/2024/09/avon-products-inc-challenge-submission.pdf/?preview=true

3 *Available at*, https://www.cdsdeterminationscommittees.org/documents/2024/09/americas-dc-meeting-statement-september-12-2024.pdf/?preview=true

For the purposes of this Meeting Statement, the Transaction Type of the relevant Credit Derivative Transaction is North American Corporate / Standard North American Corporate, as defined in the Credit Derivatives Physical Settlement Matrix (the **Relevant Transaction Type**).

1. DETERMINING DELIVERABILITY OF THE REVIEWED OBLIGATIONS

1.1 Under Section 3.2(a) of the 2014 Definitions, the term "Deliverable Obligation" is defined, in relevant part, to include "any obligation of the Reference Entity (either directly or as provider of a Relevant Guarantee) determined pursuant to the method described in Section 3.14 (*Method for Determining Deliverable Obligations*) of the 2014 Definitions".

1.2 Section 3.14 of the 2014 Definitions provides, in relevant part, that a "Deliverable Obligation" is defined as "each obligation of the Reference Entity described by the Deliverable Obligation Category […] having each of the Deliverable Obligation Characteristics, if any, specified in the related Confirmation".

2. DELIVERABLE OBLIGATION CATEGORY FOR THE RELEVANT TRANSACTION TYPE

2.1 The relevant Deliverable Obligation Category, as set out in the Credit Derivatives Physical Settlement Matrix for the Relevant Transaction Type, is "Bond or Loan". "Bond or Loan" is a sub-category of "Borrowed Money" and means "any obligation that is either a Bond or a Loan". Section 3.13(a)(vi) of the 2014 Definitions.

2.2 Under Section 3.13(a)(ii) of the 2014 Definitions, "Borrowed Money" means "any obligation (excluding an obligation under a revolving credit arrangement for which there are no outstanding, unpaid drawings in respect of principal) for the payment or repayment of borrowed money (which term shall include, without limitation, deposits and reimbursement obligations arising from drawings pursuant to letters of credit)".

2.3 A "Bond" is defined to include "any obligation of a type included in the "Borrowed Money" Obligation Category that is in the form of, or represented by, a bond, note (other than notes delivered pursuant to Loans), certificated debt security or other debt security and shall not include any other type of Borrowed Money". Section 3.13(a)(iv) of the 2014 Definitions.

2.4 A "Loan" is defined to include "any obligation of a type included in the "Borrowed Money" Obligation Category that is documented by a term loan agreement, revolving loan agreement or other similar credit agreement and shall not include any other type of Borrowed Money". Section 3.13(a)(v) of the 2014 Definitions.

3. DELIVERABILITY OF THE PROMISSORY NOTE

As set out in further detail below, the Americas DC considered the positions set out in the Challenge Submission with respect to the "Loan" and "Bond" Deliverable Obligation Categories.

3.1 Deliverable Obligation Category

(a) Loan

With respect to the "Loan" Deliverable Obligation Category, the Americas DC considered the positions presented in the Challenge Submission in favor of treating the Promissory Note as a "Loan".

Among other arguments, the Challenge Submission highlighted that Avon publicly disclosed the Promissory Note in its financial statements as an inter-affiliate "loan".[4]

Further, the Challenge Submission asserted that the Promissory Note contained the "key terms of the loan to Avon"[5] and that the Promissory Note should therefore qualify as a "Loan" under the 2014 Definitions.

After considering these positions, the Americas DC remained of the view that the 2014 Definitions expressly require that a "Loan" be "**documented by** a term loan agreement, revolving loan agreement or other similar credit agreement" (emphasis added). This documentation requirement led the Americas DC to consider whether the Promissory Note contains the elements typically present in a "term loan agreement" or "similar credit agreement".[6]

As noted in the Initial Meeting Statement, the Promissory Note is not bilaterally executed, and, other than as set out in Section 5 (Conditions Precedent), does not contain any mechanics for effecting a borrowing (e.g., provisions setting out the method pursuant to which Avon drew and Natura disbursed funds). Fundamentally, the Promissory Note presupposes, but does not itself represent, an obligation of Natura to provide an extension of credit, a feature common to standard "term loan" agreements.

Furthermore, notwithstanding the Challenge Submission's assertion that the covenants included within the Promissory Note "are as restrictive, or perhaps more restrictive, than are typically found in credit agreements"[7], certain members of the Americas DC continued to view the covenants and other contractual provisions of the Promissory Note as minimal and not in line with what would typically be seen in a credit facility, a factor that such members viewed as weighing against treating the Promissory Note as a "Loan".

The Americas DC further noted that while Avon's financial statement disclosure was relevant in determining Avon's accounting treatment of the transaction and Avon and Natura's transactional intent, such disclosure was not dispositive in making a determination as to whether the Promissory Note constituted a "Loan" as defined in the 2014 Definitions. Even if the Promissory Note were considered to be a "loan", the Americas DC felt that the Challenge Submission did not sufficiently address whether the Promissory Note satisfied the common sense meaning of the terms "term loan agreement, revolving loan agreement or other similar credit agreement" embedded in the definition of "Loan", as understood in the market.

In light of the above, the requisite number of members of the Americas DC did not conclude that the Promissory Note was a "Loan".

(b) Bond

The Americas DC noted in its Initial Meeting Statement that the 2014 Definitions do not describe how the concepts of "a bond, note (other than notes delivered pursuant to Loans),

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4 Challenge Submission at p 8. See also Avon Form 10-Q dated August 12, 2022 at p 13 (describing "[l]oans from affiliates of Natura &Co Holding" including "408.4 outstanding under a Promissory Note with Avon Products, Inc. with a maturity date of May 17, 2029"), available here. See also *id*. at p 27 and 42 (describing inter-affiliate "loans").

5 Challenge Submission at p 9.

6 The Promissory Note on its face does not contain a commitment or similar concept found in "revolving" credit facilities; the discussion here therefore focuses on the "term loan agreement" concept.

7 Challenge Submission at p 8, FN 5.

certificated debt security or other debt security" should be interpreted for purposes of the definition of "Bond".

A Supermajority of the Americas DC interpreted the definition of "Bond" in the 2014 Definitions, by virtue of the use of the phrase "***or other debt security***", to mean that the items listed ahead of that phrase in the definition, namely a "bond, note…certificated debt security", should be read as limited to types of "debt security".

While certain DC members supported the argument set forth within the Challenge Submission,[8] a Supermajority of the Americas DC found that use of the term, "**other** debt security" (emphasis added), would not make any sense unless the enumerated items that precede the term are debt securities. Specifically, these members expressed the view that the interpretation set out in the Challenge Submission appears to read the word "other" out of the definition, rendering the word meaningless.[9] Such an interpretation should therefore be disfavored in line with general principles of contract interpretation.[10]

As a result, the Americas DC determined that the fact the Promissory Note is a type of "note" is not dispositive as to the determination of whether or not the Promissory Note is a "Bond". The Americas DC did not agree with the view expressed within the Challenge Submission that a "note" is *per se* a "Bond".

(i) Application of the *Reves* test

In the absence of further definitional guidance within the 2014 Definitions, the Americas DC considered a number of sources of meaning for the term "debt security" or "security", including the U.S. federal securities laws, Article 8 of the Uniform Commercial Code (**UCC**), as adopted by the state New York, and the U.S. federal Bankruptcy Code.

In connection with its review, the Americas DC considered the conceptual framework set out in *Reves vs Ernst & Young*, 494 U.S. 56 (1990) to be appropriate for considering CDS market participants' "reasonable expectations" with respect to the meaning of "debt security" under the 2014 Definitions.[11] Members of the Americas DC took the view that given the types of entities generally involved in the credit derivatives markets and those entities' expectations around the types of products that could be delivered into a credit derivative transaction a New York court would consider U.S. Supreme Court guidance in the context of the securities laws in determining whether the Promissory Note constitutes a "debt security" and therefore a "Bond".[12] The Americas DC therefore did not agree with

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8 *See* Challenge Submission at p 4.

9 *See e.g. Nat'l Football League v. Vigilant Ins. Co*., 36 A.D.3d 207, 212 (1st Dep't 2006), where a New York court reversed a motion to dismiss grant in favor of an insurer based on their argument that the general term in an insurance contract limited the preceding specifics. There are other cases from outside New York that apply this same canon and same logic. *See e.g. Safe Food & Fertilizer v. E.P.A.*, 350 F.3d 1263, 1269 (D.C. Cir. 2003), on reh'g in part, 365 F.3d 46 (D.C. Cir. 2004) ("This reading is also sensible, as well as consistent with the 'reverse ejusdem generis' principle occasionally invoked by this court, under which 'the phrase 'A, B, or any other C' indicates that A is a subset of C.'").

10 *See e.g. Galli v. Metz*, 973 F.2d 145, 149 (2d Cir. 1992)("Under New York law an interpretation of a contract that has the effect of rendering at least one clause superfluous or meaningless […] is not preferred and will be avoided if possible.") *See also Givati v. Air Techniques Inc.*, 104 A.D.3d 644, 645, 960 N.Y.S.2d 196 ("a court should not read a contract so as to render any term, phrase, or provision meaningless or superfluous").

11 The Committee has identified a case in the United States District Court, Northern District of California – *Shaper v Zadek*, 557 F.Supp.3d 969 (2021) – where the Court applied the *Reves* test to a promissory note. Further, the Americas DC notes that certain bankruptcy courts have also considered *Reves* in analyzing whether an instrument is a "security" for purposes of the Bankruptcy Code. *See, e.g., Bakst v. Bank Leumi, USA (In re D.I.T., Inc.)*, 561 B.R. 793 (Bankr. S.D. Fla. 2016).

12 *See, e.g*., *Kirschner v. JP Morgan Chase Bank, N.A.*, 79 F.4th 290 (2nd Cir. August 24, 2023) (applying the Reves test when considering whether loan participation "notes" were securities for purposes of New York state-law securities claims).

the argument put forth by the drafters of the Challenge Submission that it was incorrect to consider *Reves* in making its determination.[13]

In connection with the *Reves* analysis, the Challenge Submission noted facts pointing towards the Promissory Note constituting a "security", including the fact that the Promissory Note was labeled as a "note" (which certain DC Members considered relevant to the question of "transactional purpose" and the *Reves* presumption).

The drafters of the Challenge Submission also argued that the absence of an active plan of distribution to investors "does not insulate an investment product […] from the securities laws."[14] The Challenge Submission, and certain Americas DC Members, took the view that the Promissory Note did not bear a resemblance to one of the enumerated categories in *Reves*.[15]

As noted in the Initial Statement, in considering the *Reves* factors and the definition of "debt security" generally, the Americas DC took into account a variety of facts available in public filings as well as the terms of the Promissory Note itself. Among the factors considered, the Americas DC noted the inter-affiliate nature of the Promissory Note (relevant to the question of "plan of distribution" and "reasonable expectations of the investing public"); the Promissory Note's definition of the obligation that Avon is required to pay with respect to principal and interest as a "Loan" (relevant to the question of "transactional purpose"); Avon's treatment of the Promissory Note in its own regulatory filings as a "loan" (relevant to the question of "transactional purpose" and "reasonable expectations of the investing public"); and the fact that the Promissory Note was not initially marketed or sold to market participants as a security (relevant to the question of "plan of distribution" and "reasonable expectations of the investing public").

A Supermajority of the Americas DC took the view that the argument raised by the Challenge Submission did not adequately address the "plan of distribution" or "transactional purposes" factors. While certain members of the Americas DC agreed with the Challenge Submission's analysis of the *Reves* factors, a Supermajority of the Americas DC determined that the information available to it (in the form of the Promissory Note itself, as well as Avon's public filings) was sufficient to rebut the *Reves* presumption that the Promissory Note was a "security", and therefore concluded that the Promissory Note was not a "Bond".

(ii) Application of the NYUCC

The Challenge Submission asserted that the Promissory Note qualifies as a security, pursuant to Section 8-102(a)(15) of New York State's Uniform Commercial Code (**NYUCC**), by relying on the New York Court of appeals' Majority judgement in *Highland Capital Management LP v. Schneider,* 8 N.Y.3d 406 (2007).

Certain DC Members viewed the NYUCC analysis to be germane to questions of the treatment of purchases and sales (and taking security over) debt securities, but did not believe the NYUCC would necessarily constitute the appropriate body of law for

[13] *See* Challenge Submission at p 4.
[14] *Id.* at p 6.
[15] *Id.* at p 7.

interpreting the CDS contract or for determining CDS market participants' "reasonable expectations" of the defined term "debt security".

Furthermore, even if the NYUCC were to apply, certain DC Members disagreed with the view that the Promissory Note would constitute a "security" for purposes of the NYUCC. As the Challenge Submission noted, under Section 8-102(a)(15)(i) of the NYUCC, to qualify as a security, a promissory note must be "in registered form".[16] A note is in registered form where it (i) specifies a person entitled to the security and (ii) a transfer of the security may be registered upon books maintained for that purpose by or on behalf of the issuer, or the security certificate so states.[17]

With respect to the second limb of this definition, the Challenge Submission focused on the decision in *Highland Capital Management LP v. Schneider*, 8 N.Y.3d 406 (2007). The *Highland Capital* majority opinion held that for purposes of this aspect of the "transferability test", the "proper inquiry is whether the notes *could have been* registered on transfer books for this purpose at the time it issued notes, not whether they were registered on transfer books at the time of the litigation"[18] (emphasis added).

Certain members of the Americas DC pointed to the fact that the *Highland Capital* Majority's interpretation of this second limb has been subject to much criticism,[19] and that crucially, the NYUCC has since been amended to overturn the *Highland Capital* decision. As amended Section 8-103(h) of the NYUCC specifically states that the registrability requirement of the definition of "registered form" will not be satisfied merely because the issuer (1) maintains records of the owner thereof for a purpose other than registration of transfer; or (2) could but does not, maintain books for the purpose of registration of transfer.[20]

Additionally, the 2010 amendments to Articles 8 and 9 of the UCC added a paragraph to Comment 13 to Section 8-102, clarifying that the *Highland Capital* decision was unsupported by the statutory test, stating that "[c]ontrary to the holding in [*Highland Capital*], the registrability requirement in the definition of 'registered form,' and its parallel in the definition of 'security,' are satisfied only if books are maintained by or on behalf of the issuer for the purpose of registration of transfer, including the determination of rights under Section 8-207(a) […] It is not sufficient that the issuer records ownership, or records transfers thereof, for other purposes. Nor is it sufficient that the issuer, while not in fact maintaining books for the purpose of registration of transfer, could do so, for such is always the case."[21]

The Americas DC noted that there was no evidence, based on the available facts, that Avon maintained the requisite books for registration of the Promissory Note. Further, certain members of the Americas DC considered it unlikely that Avon would have

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16 NYUCC § 8-102(a)(15)(i).

17 NYUCC § 8-102(a)(13).

18 *Highland Capital* at 414.

19 The Permanent Editorial Board of the UCC (the **PEB**) has issued a commentary on the *Highland Capital* case, outlining its reasoning behind the 2010 amendments, where it stated explicitly that it agreed with the dissenting opinion in *Highland Capital*, noting that "[i]f an issuer of obligations not in bearer form does not maintain books on which transfer of those obligations may be registered, those obligations do not satisfy the registrability criterion and those obligations are not "securities."" See PEB Commentary No. 18 (July 2014). *See also* the New York City Bar's Committee on Commercial Law and Uniform State Laws' "Report on Article 9 of the Uniform Commercial Code" (June 2011), at 6 *available at* https://www2.nycbar.org/pdf/report/uploads/20072118-ReportonArticle9oftheUniformCommercialCode.pdf. (stating that the result in *Highland Capital* was universally acknowledged as wrong).

20 NYUCC § 8-103(h).

21 ULA UCC § 8-102.

maintained such books based on the fact that Avon itself had described the Promissory Note as a "loan" within its filed financial statements.[22] The requisite number of members of the Americas DC therefore did not agree that the Promissory Note was in "registered form", and therefore could satisfy the "transferability test".

Separately, with respect to the "functionality test", the *Highland Capital* court held that to satisfy the functional requirement, an instrument must be "of a type in or traded on securities exchanges or securities markets."[23] The Challenge Submission concluded that "[i]nstruments like the Promissory Note are traded over-the-counter"[24] without providing any further detail or evidence to support such conclusion. Certain members of the Americas DC did not agree with this conclusion, as they did not believe that the Promissory Note, or instruments like the Promissory Note, were traded on securities exchanges or markets.

4. APPLICABILITY OF THE SEARS ER DECISION

4.1 The Challenge Submission argued that when applying the 2014 Definitions, the Americas DC should have regard to the December 21, 2018 Decision and Analysis of the External Review Panel of the U.S. Determinations Committee in connection with the Sears Credit Event (DC issue 2018101502) (the **Sears ER Decision**).[25] As described in the Challenge Submission, in reaching the Sears ER Decision, the External Reviewers were of the view that the Deliverable Obligation provisions of the 2014 Definitions should be read to "expand the scope and usefulness of the CDS product".[26] The Challenge Submission, therefore suggested that it was not necessary for the Americas DC to decide whether the Promissory Note is either a "Bond" or a "Loan", and instead proposed that the "Bond or Loan" Deliverable Obligation Category "should be interpreted to encompass any instrument that is a "Bond" or "Loan" or anything in between."[27]

4.2 After considering the argument put forth by the Challenge Submission, the Americas DC did not reach an agreement as to whether the view of the External Reviewers in the Sears ER Decision should apply here. While certain Americas DC members were of the view that the quoted statements from the Sears ER Decision should serve as a guidepost for the Americas DC members in their consideration of the deliverability of instruments presented to the Americas DC, others did not agree with approaching the Sears ER Decision as relevant or binding precedent.

4.3 Furthermore, even if the view of the External Reviewers in the Sears ER Decision were to apply, the Americas DC felt that the Challenge Submission's interpretation of "Bond or Loan" was contrary to the express wording of the 2014 Definitions, which references the stand-alone definitions of "Bond" and

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22 *See* Section 2.1 of the Promissory Note.
23 *Highland Capital* at 415.
24 Challenge Submission at p 6.
25 *Id* at p 2.
26 *Id.* at 11.
27 *Id.*

"Loan", which each specifically state that their meaning should "not include any other type of Borrowed Money".[28]

5. CONCLUSION

5.1 Section 3.3(e) of the DC Rule provides that "[t]he Convened DC shall Resolve each Challenge Submission and/ or Response Submission that is validly submitted pursuant to Section 3.3(d) (*Challenging Potential Deliverable Obligations*) by a Supermajority."

5.2 On the basis of the factors described above, a Supermajority of the Americas DC did not Resolve to include the Promissory Note on the Avon Final List of Deliverable Obligations for the Avon Auction.

[28] Section 3.13(a) of the 2014 Definitions.