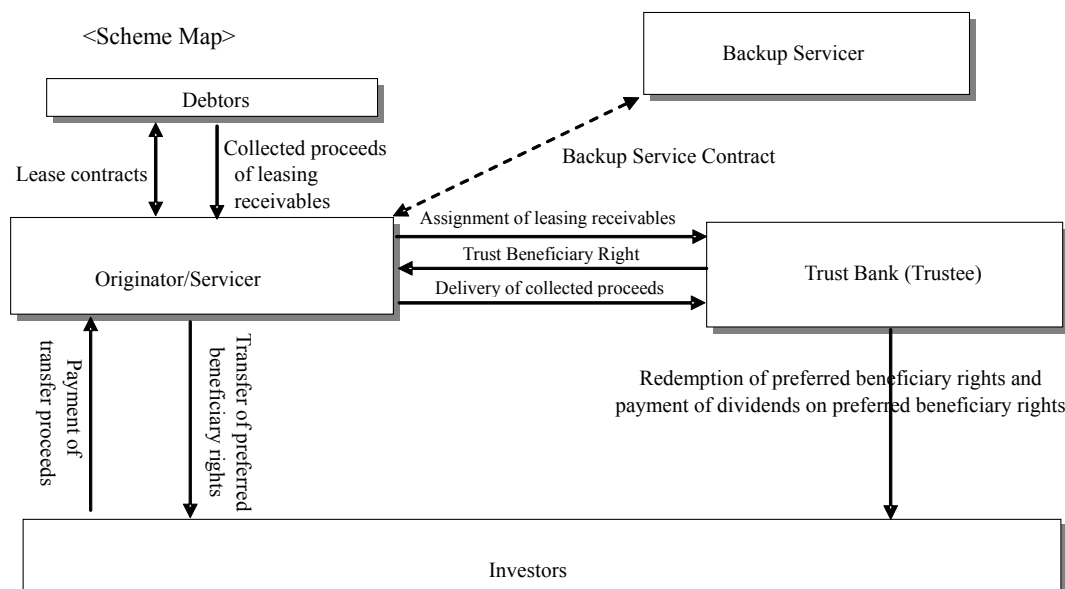


## Lease Receivables

### 1. The Outline of the General Scheme (in case of the Entrustment Method)

- (1) A lease company being the originator assigns its leasing receivables from many underlying debtors to a trust bank (trustee) to raise funds<sup>1</sup>.
- (2) The originator assigns its leasing receivables in trust to the trustee and issues preferred beneficiary rights and subordinated beneficiary rights.
- (3) The originator retains the subordinated beneficiary rights and transfers the preferred beneficiary rights to investors to raise funds.
- (4) When assigning the leasing receivables in trust, the originator fulfills the necessary conditions for opposing any third person by making the registration as stipulated in Article 4, Paragraph 1 of the special exception law on transfer of movable properties and claims. The originator's fulfillment of the necessary conditions for opposing any debtors will be reserved until any event of the servicer's default occurs.
- (5) Based on the entrustment operation commission contract, the originator first acts as the servicer for collecting leasing receivables, and delivers (pays) the collected proceeds to the trustee every month. During the collection period, the trustee redeems the principals of and pays the dividends on preferred beneficiary rights using the collected proceeds.
- (6) In case that the originator fails to pursue normal servicing operations, the backup servicer stands by from the very beginning<sup>2</sup>.



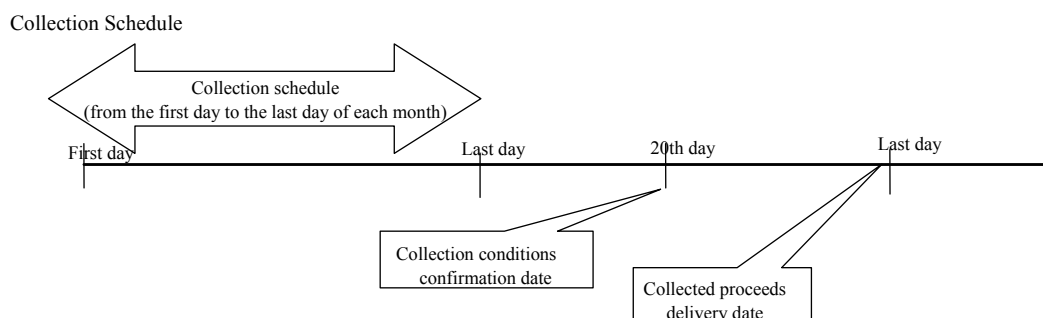
<sup>1</sup> In the case where a lease company securitizes its retaining claims for the proceeds of installment sales to corporate customers only or in the case where a lease company securitizes its retaining claims for the proceeds of installment sales to corporate collectively with leasing receivables, the same credit rating method of leasing receivables is applied to either case.

<sup>2</sup> There are some projects in which no backup servicer is arranged at the beginning.

## 2. General Waterfalls

### (1) Collection of claims from debtors

The originator credits the proceeds of the claims in trust as collected from the first day to the last day of each month at the end of the next month to the account opened in the name of the trustee for the delivery of the collected proceeds.



### (2) Normal time

The trustee pays various charges including taxes and public charges as well as trust fees from the interest equivalent amount out of the collected proceeds received from the originator. From the remaining amount, the trustee pays the dividends on preferred beneficiary rights. With the residual amount in full, the trustee pays the dividends on subordinated beneficiary rights. The trustee repays the amount scheduled for the redemption of principals of the preferred beneficiary rights from the principal equivalent amount out of the collected proceeds. With the remaining amount, the trustee redeems the principals of subordinated beneficiary rights. However, a minimum retention amount is set for the principals of subordinated beneficiary rights, so the trustee retains the principals of the subordinated beneficiary rights equal to or more than a certain amount of money. The residual amount of the collected proceeds unused for the redemption of principals of subordinated beneficiary rights is reserved and it is allowed to make the amount of money available as the resources for the redemption of the principals of subordinated beneficiary rights in the next month and thereafter.

### (3) Accelerated redemption time

The trustee pays various charges including taxes and public charges as well as trust fees from the interest equivalent amount out of the collected proceeds received from the originator. From the remaining amount, the trustee pays the dividends on preferred beneficiary rights. From the principal equivalent amount and the interest equivalent amount after having paid the dividends on preferred beneficiary rights, the trustee redeems the principals of preferred beneficiary rights. Until all preferred beneficiary rights are redeemed in full, any payment of the dividends on subordinated beneficiary rights and any redemption of the principals of subordinated beneficiary rights will be suspended.

### 3. Risk of the Securitization of Leasing Receivables and Risk Assessment

#### (1) Risk of delay in collection of the proceeds from the underlying claims

In securitized products, any redemption of principals and interest (dividends) on a due date as scheduled entirely depends on the collection conditions of proceeds from underlying debtors and so shortage of funds may possibly occurs on a temporary basis and no payment of principals and interest may be made on a due date as scheduled depending on the delinquent conditions of underlying debtors and on the conditions of pursuing collection operations by the servicer. In response to such risk, liquidity enhancement measures with cash reserves and credit enhancement measures by a preference-and-subordination structure are taken.

#### (2) Risk of debt defaults by underlying debtors

If debt defaults by underlying debtors emerge in securitized products at a rate equal to or more than a certain level, the principals of the securitized products may possibly be damaged by such defaults.

Against this risk, credit enhancement is made by a preference-and-subordination structure corresponding to individual credit ratings. (See Section 4 Calculation of an amount of money necessary for the subordination.)

#### (3) Risk involved in the originator's bankruptcy, etc.

In the originator's bankruptcy, civil rehabilitation, or corporate rehabilitation proceedings, there is a risk that the relevant court or receiver (administrator) may judge the claims transferred by securitization as the claims or the security rights belonging to the bankrupt estate, the rehabilitation debtor's property, or the rehabilitation corporate property as the claims or security rights subject to the bankruptcy, civil rehabilitation, or corporate rehabilitation proceedings. (This is the so called problem "true purchase and sale".)

Major focal points in terms of credit ratings are cited below:

- i. It has already been confirmed whether or not the originator has an intention of transferring its claims. The originator's intention of transferring its claims has already been approved according to the internal procedures.
- ii. The originator has no control rights, except that it has the rights and obligations as the subordinated beneficiary and as the servicer.
- iii. Except in the case of occurrence of certain events<sup>3</sup>, the originator has neither obligation nor claim right to repurchase the transferred claims.
- iv. With regard to the transfer of the claims in trust from the originator to the trustee, the necessary conditions for opposing any third person have been fulfilled. In case of occurrence of any cause for replacing the servicer including the originator's deteriorated creditworthiness, the necessary

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<sup>3</sup> Cleanup calls, violation of representations and warranties, violation of the conditions for qualification, other contractual violations, etc.

conditions for opposing any debtors have been fulfilled.

- v. The originator assumes no liability for security of monetary resources for repayments by debtors.
- vi. The selling/buying price of the claims to be transacted between the originator and the trustee has been determined based on the standard of rational and fair prices.

(4) Risk involved in bankruptcy, etc. of the originator doubling as the servicer

When its claims are securitized, the originator often concludes an operation commission contract with the trustee to whom the claims have been assigned, on the basis of which it pursues collection operations by continuing the collection method as has been practiced by it. In this case, however, if any bankruptcy, civil rehabilitation, corporate rehabilitation, or any other insolvency proceedings have been commenced by or against the originator, the collection operations may possibly be confused and suspended on a temporary basis.

In response to this risk, liquidity enhancement measures are implemented and a scheme is established to ensure that the collection operation commission contract with the originator can be cancelled and the backup servicer can take over the collection operations with the approval of the trustee, etc.

(5) Risk involved in the case where the necessary conditions for opposing any debtors are not fulfilled

In many cases of securitizing leasing receivables, the originator fulfills the necessary conditions for opposing any third person by making the registration as stipulated in the special exception law on transfer of claims, while the necessary conditions for opposing any debtors are reserved at the beginning. If the originator falls into bankruptcy by any chance, collected proceeds to be received by the trustee, etc. from the debtors may possibly decrease because the originator does not have the necessary conditions for opposing any debtors.

In response to this risk, the provisions are set forth to ensure that the originator will promptly have the necessary conditions for opposing any debtors using the method as stipulated in the special exception law on transfer of claims or in the civil code in case of occurrence of any cause for replacing the servicer including the originator's deteriorated creditworthiness.

#### **4. Calculation of an Amount of Money Necessary for the Subordination**

(1) Risk of deteriorated creditworthiness of underlying debtors

In pursuit of securitizing leasing receivables, claims inappropriate for the securitization are excluded from all the leasing receivables retained by the originator to make the pool of parent claims, from which the pool of claims (transferred claims) subject to the securitization is extracted. The pool of transferred claims generally consists of no less than 300 underlying corporate debtors with a maximum concentration ratio of one debtor group limited to about one percent. In the case of the pool of well-dispersed claims, the amount of losses expected to arise from defaults of the underlying claims are

calculated by the approach of many small lots using the law of great numbers.

The securitization obtains a base case to be applied when confirming and analyzing the development of credit loss percentages and that of delinquency percentages using the historical data of parent claims. Based on the average value of historical data and with overall considerations on trends and irregular values from the past, confirmed items at a due diligence meeting, macro data on lease markets, and other factors, each parameter is adjusted to such a level as nearer to the performance of the pool of claims subject to the securitization, whenever appropriate<sup>4</sup>. After the replacement of the servicer, if collected proceeds due to cancellations before the maturity of the lease contracts are expected to fall below the remaining lease fees, the securitization sets a base case of losses arising from the cancellations before the maturity based on the historical data of parent claims and confirmed items at the due diligence meeting.

Then through a stress test, the securitization gives rise to credit losses, delinquencies, and cancellations before maturity by putting a certain stress on expected cash flows during period. Thereafter the securitization obtains the amount of the subordination necessary to get the targeted credit rating. The following stress magnifications are basically applied according to the attributions and targeted credit ratings of underlying debtors. However, as a result of confirmation of attribution data and historical data beginning with a comparison of composition ratios of the attributions (including capitals, regions, business categories, classifications of lease properties, etc. of underlying debtors) between the parent claims and the transferred claims, if it is determined that the transferred claims are inferior to the parent claims in creditworthiness, the securitization sometimes adds additional stress.

|     |             |
|-----|-------------|
| AAA | Fivefold ~  |
| AA  | Fourfold ~  |
| A   | Threefold ~ |

The stress test usually verifies the possibility of repayments based on the assumption of the worst case in which a credit event occurs on the part of the originator doubling as the servicer at any point in time after the commencement of securitization and accelerated redemption begins.

The following is often used as part of the efforts for the securitization scheme: A minimum retention amount of the principals of subordinated beneficiary rights is set during a period for fear that excessive withdrawals of subordinated beneficiary rights by the collected proceeds due to cancellations

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<sup>4</sup> When extracting transferred claims, they are filtered by the conditions for qualification and so the claims extracted for their securitization become superior to parent claims. The credit loss ratio of the securitization pool (pool of transferred claims subject to securitization) is expected to become lower than the historical data of parent claims. On the other hand, the number of debtors in the pool of transferred claims is smaller than that of the pool of parent claims (in other words, the degree of dispersion of the former is lower than that of the latter.) The concentration ratio of the amount of money for one debtor of the former becomes higher than that of the latter and the impact of credit losses from one debtor of the former becomes heavier than that of the latter.

before maturity take place with the cancellations before maturity continuing at a high level.

In the case of leasing receivables, a maximum ratio of the amount of money for one debtor is set to disperse them into many small lots when extracting transferred claims. However, as underlying claims are redeemed, the number of debtors decreases. As a result, the impact of creditworthiness of the debtors that tops the list of remaining debtors sometimes increases. It is required to verify such dispersion degrees and changes of the attributions.

## (2) Commingling risk

When the originator becomes bankrupt at any point in time after the commencement of securitization, a maximum amount of money expected to be uncollectible is determined to be the amount of money necessary for the subordination in response to the commingling risk as a general rule. The period during which the collected proceeds are commingled with others is determined to be two months in many cases, but it is calculated according to the remittance schedule of collected proceeds of securitization products subject to the credit rating.

## (3) Cash reserves (liquidity enhancement)

When the originator doubling as the servicer falls into difficult situations that disable implementation of normal collection operations due to bankruptcy and any other reasons, cash reserves make up the major funds as required during the period until the originator hands over the collection operations to the backup servicer and collected proceeds are credited again to the trust bank (trustee) and to the SPC. A necessary amount of money is estimated as follows.

- (a) An amount of money necessary for liquidity enhancement (the securitization of leasing receivables sets aside an amount of money equivalent to the lease fees for more than three months.)
  - Interest and dividends on securitization products
  - Trust fees or maintenance fees of the SPC, as well as taxes and public charges
  - Backup service fees (level of fees after the change of the redemption method)
- (b) An amount of money as required when the servicer is replaced (payment in a lump sum)
  - Fees for preparing and sending notices of the replacement of the servicer
  - Fees for obtaining and sending the certificate of registered items in the commercial registration
  - Fees for taking responses to the system and for establishing a call center when the servicer is replaced, and so on
- (c) An amount of money required for others
  - Automobile tax, automobile weight tax, automobile liability insurance premiums, and voluntary insurance premiums (in the case of car leasing/installments)
  - Commitment fees required when the backup servicer is arranged (when taking responses using cash reserves) in the case of no arrangement of the backup servicer at the beginning

## 5. Other Contentions

- (1) Initial reserve of the subordination for responses to the commingling risk (see the reference report under the title of “Reconsideration of Commingling Risk”.)

When the originator meets the requirements as described below in Item (a), it is allowed to set forth the provisions under which the subordination required at the beginning for responses to the commingling risk can be reserved by setting the trigger for responses to the commingling risk as described below in Item (b) until the time of conflict of the trigger standard.

- (a) Relevant originators:

As a general rule, the relevant originators are limited to the non-banks that have been receiving from JCR, a credit rating of Range “A” or higher for their long-term preferred debts at the stage of organizing or structuring securitization products. The initial standard in the foregoing do not exclude any possibility of taking into consideration the same qualitative factors as those of the trigger standard as described in Item □, below.

- (b) Trigger in response to the commingling risk

If the credit rating of long-term preferred debts of an originator is basically “BBB” and it shows a downward (negative) tendency (including when it falls below “BBB”), the originator will contribute an additional amount of money in response to commingling losses within thirty (30) days as provided for in the original contract, or the originator will make an advance payment at a level as admitted by JCR according to the receiving schedule of collected proceeds. The trigger standard is basically “BBB” or higher. Concerning the notch (credit rating), however, the possibility is not foreclosed that a different notch is set for the trigger standard with a comprehensive judgment made on the individual factors as described below.

- Dependence on securitization in terms of fundraising by an originator
- If an originator’s fundraising depends on securitization to a high degree, a higher-level trigger may be applied to the originator in view of its ability to procure funds at the time of conflict of the trigger standard.
- Other factors: qualitative evaluation of the factors including an originator’s business bases and shareholders as well as supports from its group companies.

- (2) No arrangement of the backup servicer at the beginning (see the reference report under the title of “Backup Servicer in Securitization”.)

It is the basic handling for the securitization to arrange the backup servicer from the very beginning. However, when the credit rating of an originator doubling as the servicer is equal to or higher than “A-”, it is exceptionally allowed to make no selection of the backup servicer at the beginning, provided that

the trustee has an ability to select a new backup servicer and actually selects a new backup servicer at the stage where the originator's credit rating falls into Range "BBB".

In any securitization project that arranges no backup servicer, it is necessary to increase cash reserves (for liquidity enhancement) by the amount of commitment fees necessary for the arrangement of the backup servicer, or to take other responses including an additional obligation of cash in trust for the equivalent amount, an increase in the reserved amount of the subordination, and so on.