

## USER'S GUIDE TO THE 2005 ISDA COMMODITY DEFINITIONS

### **A. THE 2005 ISDA COMMODITY DEFINITIONS PROJECT**

The 2005 ISDA Commodity Definitions project (the "Project") was active throughout 2004 and the first half of 2005. The Project followed a rather unique period in the development of the privately negotiated commodity transactions markets. On the one hand, improvements in the legal environment (the passage of the Commodity Futures Modernization Act, for instance, in the U.S. and numerous directives of the European Parliament and Council dealing with individual commodities and market regulation) generally stimulated market growth. On the other hand, the collapse of Enron and related events caused a renewed focus on institutional risk management, including documentation risk management, while at the same time precipitating the entry of new institutional competitors into the energy markets. Many of these new competitors were already familiar with the ISDA documentation architecture and process. The resultant period of market change contributed to the need to update and strengthen the relevant ISDA definitions, both to accommodate present needs and to create a structure that will readily accommodate future needs.

The Project began with a survey of ISDA members to determine appropriate issues to resolve. The completed Project represents the result of an 18-month process of responding to those issues and other issues raised as the Project matured.

### **B. INTRODUCTION TO THE 2005 ISDA COMMODITY DEFINITIONS**

The 2005 ISDA Commodity Definitions (the "Commodity Definitions"), which include the Exhibits to the 2005 ISDA Commodity Definitions (the "Exhibits") and the Annex thereto (the "Annex"), are intended for use with the 2002 ISDA Master Agreement or the ISDA Master Agreement (the "1992 ISDA Master Agreement") (each an "ISDA Master Agreement") published by the International Swaps and Derivatives Association, Inc. ("ISDA") in 2003 and 1992, respectively, or other agreements, and designed to be incorporated into Confirmations of individual transactions governed by those agreements. Copies of the ISDA Master Agreements are available from the executive offices of ISDA and also from the ISDA web-site ([www.isda.org](http://www.isda.org)). A sample form of letter agreement constituting a Confirmation for privately negotiated commodity transactions is included in the Exhibits to the Commodity Definitions. Sample forms of specific provisions for inclusion in Confirmations to document certain types of commodity transactions are also included in the Exhibits to the Commodity Definitions. Additional Confirmation materials related to still other types of transactions may be found in the Annex.

The 1993 ISDA Commodity Derivatives Definitions (the "1993 Definitions"), as supplemented by the 2000 Supplement to the 1993 Definitions (the "2000 Supplement"), served as the basis for many of the definitions and provisions contained in the Commodity Definitions. In fulfillment of the intent of the 2000 Supplement, much of Article 7 of the 2000 Supplement has been merged into the Annex. All material from the 1993 Definitions and the 2000 Supplement has been reviewed and updated in light of the continuing evolution of ISDA terminology, including as seen in the 2000 ISDA Definitions (which include the Annex thereto), as amended and/or supplemented from time to time (the "2000 ISDA Definitions") and the 2002 ISDA Master Agreement. This review process, as well as the development of additional definitions and provisions, was carried out by working groups sponsored by ISDA. These working groups acted on the basis of market practice and studied consideration of the relevant issues. These working groups included representatives from ISDA member institutions as well as representatives from institutions that are not ISDA members, but that specialize in certain types of commodity

transactions. The material in each of the Sub-Annexes was developed by a dedicated working group prior to or contemporaneously with the preparation of the Commodity Definitions. Each of the Sub-Annexes form has been integrated into the Annex to the Commodity Definitions with a view to preserving the unique mechanisms that each contains. In particular, the 1997 ISDA Bullion Definitions have been consolidated into the Commodity Definitions through use of generic material (for example, the fundamental fixed rate and floating rate calculational provisions) and particularized definitions in Sub-Annex A and, in bulk, Sub-Annex B.

The purpose of the Commodity Definitions is to provide commodity market participants with one basic framework for the documentation of cash-settled commodity swaps, basis swaps, options, caps, collars, floors, swaptions and commodity index transactions or such other cash-settled commodity transactions as the parties desire, as well as certain physically-settled commodity transactions. The Annex contains an expanded and revised body of Commodity Reference Prices as well as additional definitions, versions of optional parts to the schedule to an ISDA Master Agreement (a "Schedule") and relevant forms of Confirmation applicable specifically to Bullion Transactions, Weather Index Derivative Transactions, Gas Transactions, Power Transactions, Freight Transactions and EU Emissions Allowance Transactions. These supplemental definitions and provisions are organized by product category within Sub-Annexes (each a "Sub-Annex" and collectively, the "Sub-Annexes") to the Annex that forms a part of and supplements the Commodity Definitions.

It is important to note that, unless otherwise agreed, parties adopting the Commodity Definitions will be deemed to have incorporated Sub-Annex A (Commodity Reference Prices for agricultural products, energy, freight, metals, paper and composite commodity indices together with the Commodity Reference Price Framework) and Sub-Annex B (Bullion provisions) to the Annex as amended and supplemented through the date on which the parties enter into the relevant transaction. Parties should consider this feature with care as they develop their documentation. As for the remaining Sub-Annexes, they may each be incorporated by express agreement of the parties in any agreement, in the Schedule of an ISDA Master Agreement, in a Confirmation or otherwise.

Other than within certain Sub-Annexes, the Commodity Definitions do not contain generic settlement or other provisions designed to permit the documentation of transactions that settle by physical delivery of the underlying commodity. Accordingly, parties should carefully consider any necessary modifications and consult with their legal advisors before using the Commodity Definitions when documenting such a transaction.

Inevitably, in certain areas market practice has not been uniform or has otherwise not provided definitive guidance. Each working group member has, where appropriate, sought the views of his or her own trading, operational, legal, compliance and other relevant personnel. None of this research, however, obviates the need for each user of the Commodity Definitions to review the provisions of the Commodity Definitions carefully and to form its own independent judgment on whether the Commodity Definitions are appropriate for documenting any particular transaction.

The separation of the Commodity Definitions into a principal section, the Exhibits and the Annex composed of separable Sub-Annexes is intended to facilitate publication of additional and revised material. The Commodity Definitions may be updated periodically to include additional definitions and provisions, such as new or revised Commodity Reference Prices or new commodity transactions. While the definitions and provisions contained in the Commodity Definitions may be modified in any update, it