
User's Guide to the 2004 ISDA[®] Novation Definitions

ISDA[®]

INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC.

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INTRODUCTION

This User's Guide is intended to highlight a number of points relating to the provisions of the 2004 ISDA Novation Definitions (the "Definitions"), published by the International Swaps and Derivatives Association, Inc. ("ISDA") on April 12, 2004. In particular, the User's Guide is meant to focus attention upon the choices and variations which parties entering into a Novation Agreement may wish to consider.

Capitalised terms used in this User's Guide and not defined herein are intended to have the meanings given such terms in the Definitions or in the 2002 ISDA Master Agreement, as the context may require.

THIS USER'S GUIDE DOES NOT PURPORT TO BE, AND SHOULD NOT BE CONSIDERED TO BE, A GUIDE TO OR EXPLANATION OF ALL ISSUES AND OTHER CONSIDERATIONS RELEVANT TO DECIDING WHETHER TO ENTER INTO A NOVATION AGREEMENT, INCLUDING RELEVANT ENFORCEABILITY, REGULATORY, TAX, ACCOUNTING AND OTHER CONSIDERATIONS. EACH PARTY SHOULD CONSULT WITH ITS LEGAL AND TAX ADVISERS AND ANY OTHER ADVISER IT DEEMS APPROPRIATE PRIOR TO USING ANY STANDARD ISDA DOCUMENTATION. ISDA ASSUMES NO RESPONSIBILITY FOR ANY USE TO WHICH ANY OF ITS DOCUMENTATION OR ANY DEFINITION OR PROVISION CONTAINED THEREIN MAY BE PUT.

USER'S GUIDE TO THE 2004 ISDA NOVATION DEFINITIONS

1. What is Novation?

In a novation, with the consent of all parties, one contract is entered into in substitution for and supersession of another contract. This concept is valid under both English and New York law (as confirmed by the recent legal opinions obtained by ISDA, which are available on ISDA's website at www.isda.org). Consent of all parties is a key ingredient for novation, and accordingly under Section 7 of the ISDA Master Agreement, neither an ISDA Master Agreement nor any interest or obligation in or under that agreement (for example, a Transaction) may be transferred by either party without the prior written consent of the other party, subject to certain limited exceptions. The ISDA Board of Directors published a statement on the importance of obtaining consent for transfer of Transactions under an ISDA Master Agreement in April 2003 (attached as Exhibit V hereto).

2. Documenting the Transfer of OTC Derivatives: Novation or Assignment?

The transfer of rights and obligations between legal entities in relation to privately negotiated, or over-the-counter, derivative transactions is generally referred to as "novation" (under English law) and "assignment" (under New York law).

Historically the transfer of OTC derivatives in the U.S. market has been achieved by way of an "assignment" agreement governed by New York law. In U.S. usage, the term "assignment" is typically used by way of abbreviation to refer both to an assignment of rights and a delegation and assumption of obligations.

There is no exact equivalent of an assignment and assumption agreement under English law. Under English law, rights but not obligations under a contract may be assigned without the consent of the other contracting party.

ISDA undertook an analysis of the kinds of agreements being used in the market to transfer OTC derivatives and concluded that assignment and assumption was broadly equivalent to novation (if not in the strictest legal sense identical). Since novation is valid under both New York and English law, consensus among market participants was to encourage standardisation by streamlining ISDA standard documentation and to use a novation-only approach.

3. Using the Definitions.

The Definitions allow a greater degree of flexibility in documenting the transfer of OTC derivative transactions by way of novation. The Definitions are intended for use in documenting the novation of any Transaction governed by the terms of an ISDA Master Agreement. Whilst the Definitions contain certain product-specific requirements (for example, for Credit Derivative Transactions), parties are reminded that the precise documentation of each Transaction remains the responsibility of the parties concerned. Parties should satisfy themselves that the provisions of the Definitions are appropriate for documenting the novation of any specific Transaction(s) and reflect the commercial terms the parties intended.

The Definitions include a template for a short-form Novation Confirmation which incorporates by reference the terms of a standard Novation Agreement and underlying terms defined in the Definitions themselves. This simplifies the documentation for novating a Transaction. The standard legal terms and conditions (for example transfer, release and discharge of

obligations and representations and warranties) typically found in a long-form novation agreement are covered by the Definitions; therefore the Novation Confirmation needs only to identify the principal economic terms of the Novation Transaction itself.

The Novation Definitions allow for updates and additions to be made from time to time through supplements published on ISDA's website at www.isda.org. Any supplements published will be incorporated into the Definitions with effect from and including the date of the supplement. A Novation Transaction will be deemed to include the provisions of any supplements dated prior to the Novation Trade Date, unless parties specify otherwise in a Novation Confirmation. The terms of any supplement dated after a Novation Trade Date will not apply to that Novation Transaction.

The Definitions may be used to document the transfer of single or multiple Transactions between the same parties, and can accommodate partial novations where less than the full principal amount of a Transaction is to be novated. Where a partial Novation of an Old Transaction has taken place, the Definitions provide in Section 1.18, for the Old Confirmation to be reduced by the Novated Amount. It is therefore not necessary for parties to send an amended Confirmation for the Old Transaction.

The Definitions provide parties with several options to identify the novated Transaction in a Novation Confirmation:

- A. *Identifying the Old Transaction.*** In Section 3 of the Novation Confirmation, parties may elect to (a) attach the Old Confirmation or (b) include summary terms of the Old Transaction; and
- B. *Identifying the New Transaction.*** In Section 4 of the Novation Confirmation, parties may elect to (a) detail summary terms of the New Transaction; (b) identify specific sections of the Old Confirmation which are to apply to the New Transaction; or (c) attach a New Confirmation to the Novation Confirmation.

The ISDA Operations Process Working Group has endeavoured to define consensus in the market regarding the process of novating Transactions. The results have been published as a Best Practice Statement with guidance on operational practice, which is attached as Exhibit IV to this User's Guide. The Best Practice Statement recommends identification of the Old Transaction by way of summary terms and evidencing the New Transaction by attaching a New Confirmation to the Novation Transaction. The benefits of this approach are to allow parties, where systems permit, to straight-through process (STP) the novation of Transactions and to assist the growing market in trade affirmation/auto-matching services to handle novations. A commentary on attaching the Old or New Confirmation follows later in this User's Guide.

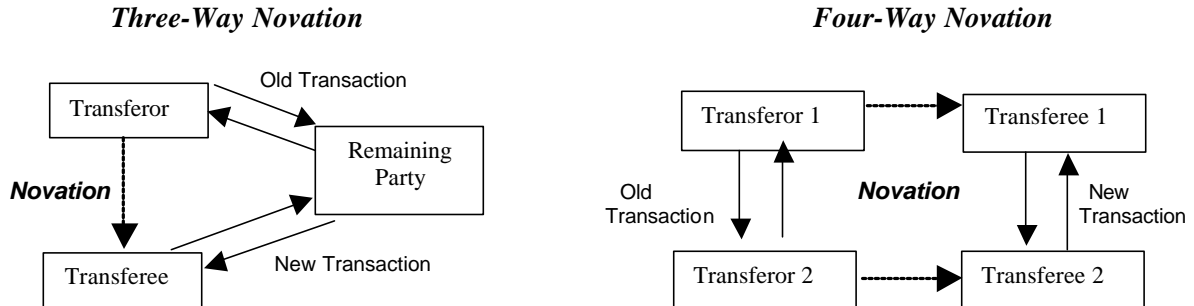
Parties may find it useful to refer to the process flow diagram in Exhibit I of this User's Guide. This sets out the main elements involved in novating a Transaction and the order in which they should be accomplished.

4. *The Novation Agreement.*

Two forms of Novation Agreement are included as Exhibits A and B to the Definitions. The form in Exhibit A may be elected for typical three-way novations of single or multiple deals, where either the whole or part of each deal is to be transferred. The form of Exhibit B is specifically for four-way novations where one or more deals are transferred from two Transferors to two Transferees and there is no Remaining Party to the Transaction. The terms of each

Novation Agreement are consistent with one another, except for specific requirements to accommodate the particular structure of the novation being documented.

Figure 1



In this User’s Guide, references to the Transferor, Transferee and Remaining Party as parties to a three-way Novation also include, where applicable, references to Transferors 1 and 2 and Transferees 1 and 2 under a four-Way Novation.

The Novation Agreement accommodates the legal requirements for effecting the novation itself: the transfer, release, discharge of obligations and undertakings of the parties in relation to the novated Transaction. Representations and warranties of the parties are incorporated from Article II of the Definitions and from Section 3 of the ISDA Master Agreement.

In Section 2(c), the Novation Agreement refers to the Old Confirmation as being deemed to be modified to reflect the terms of the New Transaction between the Remaining Party and the Transferee. A Confirmation, or the Master Agreement of which it is a part, may contain credit or other terms that are relevant to the Old Transaction, but that the parties do not intend to see replicated in the New Transaction. As it has not been possible to characterise the range of terms that may be subject to this intention, it is important to note that:

- A. It is the usual expectation of parties that a novated Transaction will become subject to the credit and other terms in the New Agreement, if any, between the Remaining Party and the Transferee; and
- B. Industry participants are advised to exercise care in attaching the Old Confirmation as the agreed record of the terms of the New Transaction, where the Confirmation may include terms beyond those usually considered necessary to the particular type of Transaction being novated.

The parties may disapply particular terms of an Old Transaction in a number of different ways, including through specific provision in the Novation Confirmation or by attaching the terms of a New Transaction as a New Confirmation. Section 8 – Amendments to Old Transaction – gives guidance on amending an Old Confirmation to reflect the terms of the New Transaction.

5. The Novation Confirmation.

The short-form Novation Confirmation template is set out in Exhibit C to the Definitions. This may be used in conjunction with an Old or a New Confirmation at the discretion of the parties.

By way of guidance:

A. *Attaching the Old Confirmation.*

- (i) For structured Transactions, market participants may prefer to attach the Old Confirmation since this may better evidence any complex terms of the Old Transaction as they relate to the New Transaction.
- (ii) When attaching the Old Confirmation, any terms to be amended in the New Transaction should be identified in the Novation Confirmation. Economic amendments to the New Transaction would normally be agreed separately between the Remaining Party and the Transferee and therefore be the subject of an amended Confirmation outside the scope of the Novation Confirmation. The Best Practice Statement in Appendix IV provides guidance on this point.

B. *Attaching the New Confirmation.*

- (i) Attaching a New Confirmation enables a simpler process for documenting the novation. This method is particularly suited to novating Transactions which are standard OTC derivative products (generally referred to as “vanilla” Transactions).
- (ii) Where the Old Confirmation evidences a Transaction with standard terms, a preferred approach by participants is to attach a New Confirmation to evidence the New Transaction. This facilitates automated processing of these transfers.
- (iii) This method dispenses with using an Old Confirmation. The requirement to reflect changes to the Old Transaction in the Novation Confirmation falls away since the particular terms of the New Transaction are incorporated directly into the New Confirmation.

It should be stressed that attaching either an Old Confirmation or a New Confirmation is effective for the purposes of novating a Transaction and parties should agree amongst themselves which method is most appropriate for their requirements.

The Novation Confirmation incorporates the Definitions and the Novation Agreement by reference. The ISDA definitional booklet(s) which governs the Novation Transaction should be incorporated into the Novation Confirmation to give meaning to any product-specific terms used.

In preparing and reviewing Novation Confirmations, parties will need to make certain elections. A commentary on these elections, and an explanation where applicable, follows in Section 8 below. An example of how to complete a Novation Confirmation when attaching (i) a New Confirmation is set out in Exhibit II for an interest rate swap and (ii) an Old Confirmation is set out Exhibit III for a credit default swap where particular terms apply in relation to the provision of Credit Event, Physical Settlement and Publicly Available Information notices.

The Novation Confirmation may be signed in counterparts. Generally speaking, market practice is not to match Novation Confirmations but parties are free to agree bilateral arrangements which best suit their own circumstances. By execution of the Novation Confirmation, the Transferee agrees to the terms of the New Transaction and the Transferor is released from its obligations and duties.

6. ***The ISDA 2002 Novation Agreement.***

It may be helpful to draw participants' attention to the ISDA standard long-form Novation Agreement which may be used under English law or New York law to document the novation of bespoke structured Transactions, or multiple Transactions of any type between the same three parties. Although the Definitions are drafted in such a way as to allow for the transfer of multiple trades, it is not expected that participants will use a Novation Confirmation to document the transfer of, for example, a portfolio of OTC derivative transactions. Identifying multiple Transactions is, as a practical matter, more effectively accomplished using a schedule rather than listing Transactions individually. The 2002 Novation Agreement published by ISDA on its website at www.isda.org includes a template Schedule as part of the User's Guide which can be used when novating a series of Transactions between the same three parties.

7. ***Explanation of Key Definitions.***

- A. ***Novation Confirmation.*** The Novation Confirmation is the written (or electronic) agreement evidencing the novation of a Transaction between the relevant parties. The Novation Confirmation is normally signed by all parties to the novation and may be signed in counterparts if preferred.
- B. ***Novation Transaction.*** The Novation Transaction is the Transaction confirmed under the terms of an ISDA Master Agreement which is being transferred from a Transferor to a Transferee.
- C. ***Transferor.*** The Transferor is the outgoing party to the Novation Transaction. The Transferor is required to agree the novation with the Transferee and the Remaining Party before the transfer takes place and, absent such agreement, a Novation Date cannot be established.
- D. ***Transferee.*** The Transferee is the incoming party to the Novation Transaction and assumes the position taken by the Transferor under the Old Transaction.
- E. ***Remaining Party.*** The Remaining Party is the constant party in what is the most frequent type of novation, the three-way novation. The Remaining Party's consent is required for any novation to occur. Since the Remaining Party's rights with and obligations to the Transferor under the Old Transaction are extinguished and replaced with identical rights with and obligations to the Transferee, the Remaining Party will rebook the Old Transaction as the New Transaction.
- F. ***Old Transaction.*** The Old Transaction is the original Transaction traded between the Remaining Party and the Transferor which was entered into under the terms of an ISDA Master Agreement.
- G. ***New Transaction.*** Under a novation, upon the extinguishment of the Old Transaction, the New Transaction is simultaneously created and has identical terms to the Old Transaction (except where agreed between the parties and evidenced by the Novation Confirmation).
- H. ***Old Agreement.*** The Old Agreement is the ISDA Master Agreement between the Transferor and the Remaining Party. In cases where the Transaction that is being novated is subject to a guarantee, the parties should consult with a legal advisor to determine if the guarantor's consent is required.

- I. ***New Agreement.*** The New Agreement is the ISDA Master Agreement between the Transferee and the Remaining Party. The Novation Confirmation constitutes a “Confirmation” for purposes of the New Agreement.

Where a New Agreement has not been executed, Article 1.11 of the Definitions incorporates the terms of the standard ISDA Master Agreement without a Schedule. The election of Governing Law, pursuant to Article 3.4 of the Definitions, may be either English law or the laws of the State of New York, and should be elected in the Novation Confirmation. Where English law is selected, the Termination Currency is deemed to be the Euro, and where the laws of the State of New York is selected, the Termination Currency is deemed to be the US Dollar.

If either of the parties is located in a jurisdiction where the application of Automatic Early Termination is recommended, the parties may wish to add a sentence in the Novation Confirmation under Section 2 designating that Automatic Early Termination is to apply with respect to the New Agreement.

Where the New Agreement is governed by the laws of the State of New York, Article 3.5 of the Definitions incorporates a provision for waiver of jury trial. This applies unless the parties have already included an alternative provision in the New Agreement in which case the New Agreement will override Article 3.5.

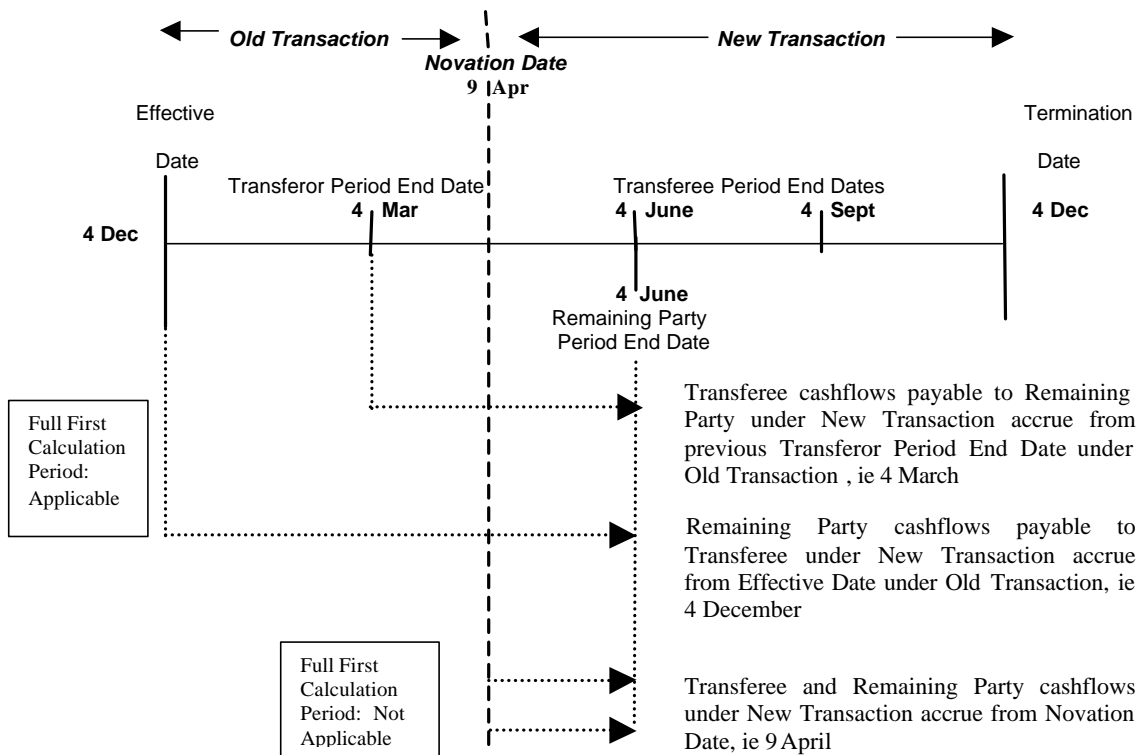
- J. ***Old Confirmation.*** The Old Confirmation is the written (or electronic) agreement evidencing the terms of the Old Transaction that was executed, or exchanged, between the Transferor and the Remaining Party. Where a partial novation of the Old Transaction has taken place, the Old Confirmation is deemed reduced by the Novated Amount.
- K. ***New Confirmation.*** The New Confirmation is the written (or electronic) agreement evidencing the terms of the New Transaction which is attached as Exhibit A to the Novation Confirmation, or (by agreement between the parties) may be otherwise exchanged or executed between the Remaining Party and the Transferee.
- L. ***Novation Trade Date.*** Novation Trade Date is the date all parties agree to enter into the Novation Agreement. This is usually the Novation Date but in certain markets or to suit individual requirements, Novation Trade Date may fall a number of Business Days prior to the Novation Date. In the Credit Derivatives market, for example, Novation Trade Date is typically one Business Day prior to the Novation Date. The Definitions provide a fallback that the Novation Trade Date will be deemed to be the Novation Date unless otherwise specified in the Novation Confirmation.
- M. ***Novation Date.*** The Novation Date is the date that the rights, liabilities and obligations set forth in Section 2 of the Novation Agreement become effective. On the Novation Date, the Transferor is released from its obligations under the Old Transaction and its rights and obligations are reinstated in the New Transaction between the Remaining Party and the Transferee. The Novation Date is agreed by front office personnel and is the date on which the deal will be re-booked in all the parties’ records.

- N. **Novated Amount.** The Novated Amount is the principal amount (Currency Amount, Notional Amount, Notional Quantity, Number of Options, etc.) of the Old Transaction which is being novated. The Novated Amount is expressed in absolute terms rather than as a percentage. The Novated Amount may be less than the full principal amount of the Old Transaction.
- O. **Novation Agreement.** The Novation Agreement governs the Novation Transaction and contains the legal requirements to effect the novation. The Novation Agreement is incorporated by reference into the Novation Confirmation, and provides the formal transfer of rights, assumption and release of obligations, and representations and warranties, otherwise contained within the ISDA 2002 long-form Novation Agreement.
- P. **Full First Calculation Period.** Full First Calculation Period relates to initial cashflow accruals for payment by each party on the first Payment Date following a novation.

When a novation takes place mid-Calculation Period, the normal method is for cashflows of the Remaining Party and the Transferee under the New Transaction to accrue from and including the last Period End Date to occur for each relevant party under the Old Transaction. If the novation occurs before a party's first Period End Date under the Old Transaction, the cashflow accrue for that party accrues from and including the Effective Date. This method may be elected by specifying "Full First Calculation Period: Applicable".

An alternative method is to accrue initial cashflows for each party under the New Transaction from the Novation Date. This method may be elected by specifying "Full First Calculation Period: Not Applicable".

Figure 2 : Example of a novation effected mid-Calculation Period with non-synchronised Period End Dates



Where the New Transaction is evidenced by a New Confirmation, the last Period End Dates to occur under the Old Transaction for the Remaining Party and the Transferor should be detailed in the Novation Confirmation. There is no requirement to specify this information where the New Transaction is evidenced by the Old Confirmation.

8. *Completing the Novation Confirmation.*

Examples for completing a Novation Confirmation are shown in Exhibits II and III of this User's Guide. The narrative which follows will assist users to select the appropriate options. It is, however, not intended to be exhaustive and participants should ensure for their own purposes that the Old Transaction and those terms which apply to the New Transaction are adequately identified in the Novation Confirmation. This particularly relates to Section 5 which deals with amended terms in the New Transaction when an Old Confirmation is to be attached as Exhibit A.

A. *Section 1 - incorporating governing legal provisions and definitions.*

The relevant ISDA definitional booklet(s) which apply to the Old and New Transactions should be inserted to give effect to the product-specific terms used in the Novation Confirmation. This section incorporates the Definitions and the Novation Agreement which govern the Novation Confirmation.

B. *Section 2 – identifying parties to, and principal terms of, the Novation Transaction.*

Section 2 identifies the parties to the Transaction(s) being novated. Identifying the parties (either as "Transferor", "Transferee" and "Remaining Party", or as "Transferor 1", "Transferor 2", "Transferee 1" and "Transferee 2") in a Novation Confirmation will automatically incorporate the relevant form of Novation Agreement into the Novation Confirmation.

The term Novation Trade Date may be omitted where this is the same as the Novation Date.

The Novated Amount is expressed as a figure and not a percentage. Where the Old Transaction has two notional amounts, for example a foreign exchange transaction (Call Currency, Put Currency), show the Novated Amount applicable to each party as a "Transferee Novated Amount" and a "Remaining Party Novated Amount"

Where the Novated Amount is less than the full amount of the Old Transaction, i.e. a partial novation of the Old Transaction is taking place, enter the amount to be novated into the Novation Confirmation. The notional amount for the Old Transaction is deemed to be reduced by the Novated Amount pursuant to Article 1.18 of the Definitions, and the Old Confirmation is thereby amended. There is no requirement for parties to send an amended Confirmation for the Old Transaction.

The date of the ISDA Master Agreement between the Remaining Party and the Transferee, i.e. the New Agreement, should be inserted if applicable.

In cases where the New Agreement is executed, parties should consider whether the Office through which the Remaining Party or the Transferee is acting for purposes of the Novation Transaction needs to be added under the Multibranch provisions of Section 10(c). If amendment is required, an example of language which could be used in the Novation Confirmation follows:

“For purposes of the New Transaction, both parties agree that [.....] branch shall be deemed to be an Office with respect to [Remaining Party][Transferee] for purposes of Section 10(c) of the New Agreement [and the parties agree to execute a multibranch amendment agreement thereto providing for the addition of [Remaining Party][Transferee]’s [.....] branch.]”

Where no New Agreement exists, Article 1.11 of the Definitions incorporates the standard terms of the ISDA Master Agreement. In this case, parties can replace the wording “ISDA Master Agreement dated as of -----” to read “ISDA Master Agreement as per Section 1.11” and elect whether English or New York law will govern the New Agreement. If parties require Automatic Early Termination to apply to the New Agreement, an election may be made at this point in the Novation Confirmation.

For Credit Derivative Transactions, confirmation of delivery status for certain notices is required pursuant to Article 2.1(a)(iii)(D) of the Definitions. Details for notices of Credit Events, Publicly Available Information and Physical Settlement are not required unless the Old Transaction is a Credit Derivative Transaction.

C. Section 3 – identifying the Old Transaction.

To identify the Old Transaction(s), Section 3 should be completed in all cases. Two options are available: identifying the principal terms of the Old Transaction, or, attaching the Old Confirmation as Exhibit A. These may be selected as follows:

- (i) if the Old Confirmation will be used to evidence the New Transaction, select the option to attach the Old Confirmation as Exhibit A. No further details are required.
- (ii) if a New Confirmation (or some other method agreed between the parties) will be used to evidence the New Transaction in Exhibit A, complete the following details to identify the Old Transaction:

Trade Date
Effective Date
[Scheduled] Termination/Expiration Date
For Credit Derivative Transactions include the Reference Entity

D. Section 4 – identifying the New Transaction.

Section 4 identifies the New Transaction(s) and should be completed in all cases, selecting from one of the options:

- (i) if the New Confirmation is to appear at Exhibit A, or if another method has been agreed between the parties, to evidence the New Transaction (for example by agreeing that the New Transaction shall be subject to an existing Master Confirmation previously agreed between the Transferee and the Remaining Party and then specifying the economic terms of the New Transaction), complete the following details:

Full First Calculation Period: Applicable or Not Applicable
(add dates from which cashflows are to accrue, if
'Applicable' is selected)

- (ii) if the Old Confirmation is to appear at Exhibit A, list those sections from the Old Confirmation which will apply to the New Transaction and select whether Full First Calculation Period will be Applicable or Not Applicable. It is not necessary to add the dates applicable from which cashflows accrue as these will be evidenced in the Old Confirmation.

Note: it customary that terms relating to the parties' trading relationship, for example break-clauses and collateral, will not be transferred to apply to the New Transaction. Bilateral terms are normally restated in the New Transaction in line with the existing relationship between the Transferee and Remaining Party.

E. Section 5 – other provisions.

- (i) **Amendments to Old Transaction.** Where the Old Confirmation is being used to evidence the New Transaction, any new terms which are to apply to the New Transaction should be detailed under Additional Provisions in Section 5. These terms may include:

Optional Termination provisions (break-clauses)
Bilaterally negotiated language (for example, Calculation Agent)

Amendments to the economic terms of an Old Transaction are usually dealt with between the Remaining Party and the Transferee separately through the normal amended Confirmation process. However, if preferred, such amendments or additional provisions can be detailed in Section 5.

Note: Where a New Confirmation is to be attached as Exhibit A, any amendments to the Old Transaction will be evidenced in the New Confirmation. There is therefore no requirement to include these amendments within Additional Provisions in Section 5 of the Novation Confirmation.

- (ii) **Collateral or other credit terms.** When attaching an Old Confirmation, any collateral or credit terms which are to apply bi-laterally between the Remaining Party and Transferee should be detailed in the Novation Confirmation.

F. Section 6 – Miscellaneous: Non-Reliance.

For all novations, whether an Old or New Confirmation is to be attached as Exhibit A or whether some other method is chosen by the parties, participants should elect whether the Non-Reliance Representation in Section 2(c) of the Definitions is to apply. This provision will not override any alternative language which parties may have bilaterally negotiated in the relevant Old Agreement or New Agreement. The Non-Reliance clause addresses the position of older ISDA Master Agreements where this provision may not have been included. The Best Practice Statement attached as Exhibit IV offers guidance on this point.

G. Section 7 – Notice Details.

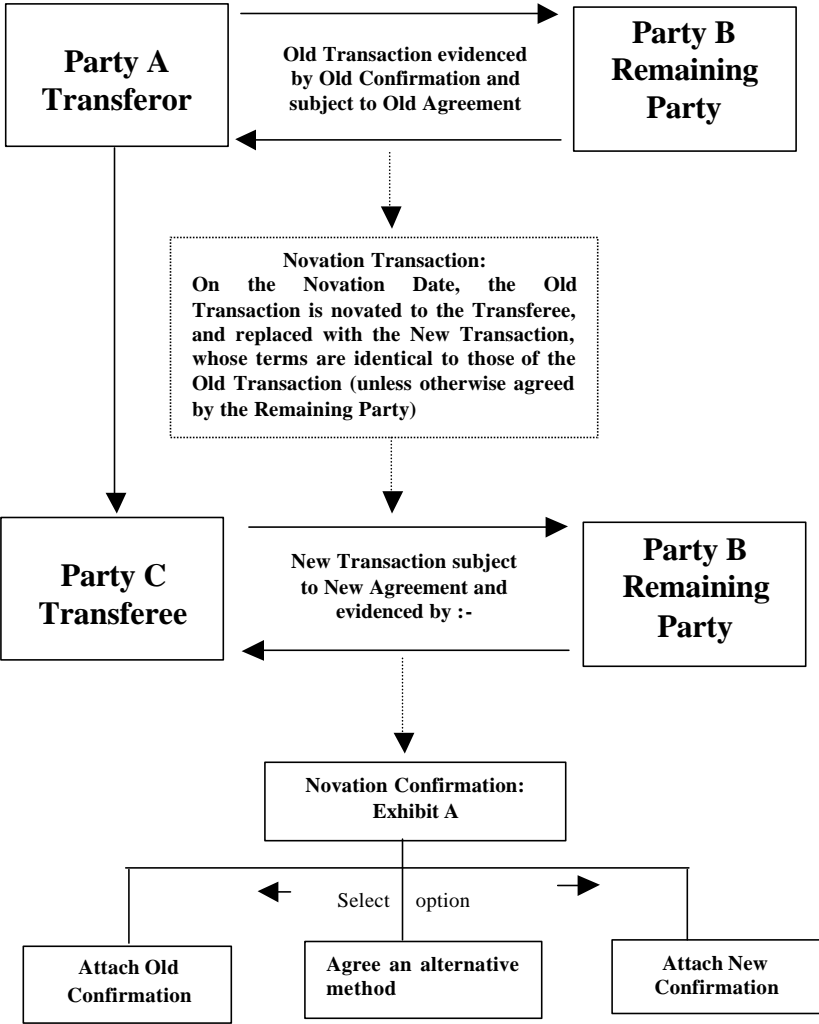
Details for notices are only required in the Novation Confirmation when the New Transaction is being evidenced by the Old Confirmation. Special attention should be given to ensure that full notice details are provided where exercise of an option may be required under the New Transaction. Account details and Offices of the parties to the New Transaction may be added to Section 7 if required. There is general support within the

market to exclude Account Details from Confirmations where these have otherwise been exchanged between the parties based on payments to be made according to that party's Standard Settlement Instructions. Any requirement to include Office details will be limited to the New Agreement having been executed on a multibranch basis between the Transferee and the Remaining Party.

Where parties are attaching a New Confirmation to the Novation Confirmation, notice details, payment and Office details relating to the New Transaction will appear in the New Confirmation.

Process Flow Diagram for Novating a Transaction

- Party A agrees novation with Party C and seeks consent from Party B
- All parties agree the Novation Date



- Remaining Party will typically assume responsibility for documenting the Novation and dispatch the Novation Confirmation to Transferor and Transferee
- All parties sign the Novation Confirmation, in counterparts if required, to complete the novation

Example of a Novation Confirmation attaching a New Confirmation

ABC Bank

Date: 9 March 2004

To: DEF Bank
Address
Fax:

To: XYZ Bank
Address
Fax:

From: ABC Bank
Address
Fax:

Re: Novation Transaction

Dear _____,

The purpose of this facsimile is to confirm the terms and conditions of the Novation Transaction entered into between the parties on the Novation Date specified below.

1. The definitions and provisions contained in the 2004 ISDA Novation Definitions (the "Definitions") and the terms and provisions of the 2000 ISDA Definitions, as published by the International Swaps and Derivatives Association, Inc. and amended from time to time, are incorporated in this Novation Confirmation. In the event of any inconsistency between the Definitions and this Novation Confirmation, this Novation Confirmation will govern. In the event of any inconsistency between the Definitions and the 2000 ISDA Definitions, this Novation confirmation will govern. In the event of any inconsistency between the Novation Agreement and this Novation Confirmation, the provisions set forth in this Novation Confirmation will govern.

2. The terms of the Novation Transaction to which this Novation Confirmation relates are as follows:

| | |
|---------------------------------------------------------|-------------------------------------------------------------------------------------|
| Novation Date: | 9 April 2004 |
| Novated Amount: | USD 5,000,000.00 |
| Transferor: | DEF Bank |
| Transferee: | XYZ Bank |
| Remaining Party: | ABC Bank |
| New Agreement (between Transferee and Remaining Party): | ISDA Master Agreement as per Section 1.11 of the Definitions subject to English law |

3. The terms of the Old Transaction to which this Novation Confirmation relates, for identification purposes, are as follows:

| | |
|-------------------------------------|-----------------|
| Trade Date of Old Transaction: | 2 December 2003 |
| Effective Date of Old Transaction: | 4 December 2003 |
| Termination Date of Old Transaction | 4 December 2004 |

4. The terms of the New Transaction to which this Novation Confirmation relates shall be as specified in the New Confirmation attached hereto as Exhibit A.

| | |
|--------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Full First Calculation Period: | Applicable, commencing on 4 March 2004 with respect to any amounts to be paid by the Transferee and 4 December 2003 with respect to any amounts to be paid by the Remaining Party |
|--------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

5. Other Provisions relating to the New Transaction:

| | |
|---------------------------|------|
| Additional Provisions: | None |
| Credit Support Documents: | None |

6. Miscellaneous

| | |
|---------------|------------|
| Non-Reliance: | Applicable |
|---------------|------------|

The parties confirm their acceptance to be bound by this Novation Confirmation as of the Novation Date by executing a copy of this Novation Confirmation and returning it to us. The Transferor, by its execution of a copy of this Novation Confirmation, agrees to the terms of the Novation Confirmation as it relates to the Old Transaction. The Transferee, by its execution of a copy of this Novation Confirmation, agrees to the terms of the Novation Confirmation as it relates to the New Transaction..

.....
ABC Bank

By:
Name:
Title:
Date:

.....
DEF Bank.

By:
Name:
Title:
Date:

.....
XYZ Bank

By:
Name:
Title:
Date:

Exhibit A

The terms of the particular Transaction to which this Confirmation relates are as follows:

| | |
|------------------|----------------------------------------------------------------------------------------------------------|
| Notional Amount | USD 5,000,000.00 |
| Termination Date | 4 December 2004, subject to adjustment in accordance with the Modified Following Business Day Convention |

Fixed Amounts

| | |
|--------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Fixed Rate Payer | ABC Bank. |
| Fixed Rate Payer Payment Dates | The 4th of each June and December, commencing on 4 June 2004 to and including the Termination Date subject to adjustment in accordance with the Modified Following Business Day Convention. |
| Fixed Rate | 2.50000% |
| Fixed Rate Day Count Fraction | 30/360 |

Floating Amounts

| | |
|----------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Floating Rate Payer | XYZ Bank |
| Floating Rate Payer Payment Dates | The 4th of each March, June, September and December, commencing on 4 June 2004 to and including the Termination Date subject to adjustment in accordance with the Modified Following Business Day Convention. |
| Floating Rate for initial Calculation Period | 1.12000% (exclusive of Spread where applicable) |
| Floating Rate Option | USD-LIBOR-BBA |
| Designated Maturity | 3 month(s) |
| Spread | None |
| Floating Rate Day Count Fraction | Actual/360 |
| Reset Dates | The first day of each Calculation Period |
| Business Days | London, New York |
| Calculation Agent | ABC Bank or, if different, as stated in the New Agreement |

Notice Details:

Telephone and/or Facsimile Numbers for Notices:

| | |
|-----------|--------------|
| ABC Bank: | xxx-xxx-xxxx |
| XYZ Bank: | xxx-xxx-xxxx |

Account Details:

Payments to ABC Bank:

[.....][As per our Standard Settlement
Insuctions advised separately in writing]

Payments to XYZ Bank

[.....][As per your Standard Settlement
Instructions advised separately in writing][Please
provide your settlement instructions]

Offices:

The Office of ABC Bank for the Transaction is:

New York

The Office of XYZ Bank for the Transaction is:

London

Example of a Novation Confirmation attaching an Old Confirmation

ABC Bank

Date: 9 March 2004

To: DEF Bank
Address
Fax:

To: XYZ Bank
Address
Fax:

From: ABC Bank
Address
Fax:

Re: Novation Transaction

Dear _____:

The purpose of this facsimile is to confirm the terms and conditions of the Novation Transaction entered into between the parties on the Novation Date specified below.

1. The definitions and provisions contained in the 2004 ISDA Novation Definitions (the "Definitions") and the terms of the 2003 ISDA Credit Derivatives Definitions as supplemented by the May Supplement, each as published by the International Swaps and Derivatives Association, Inc. and amended from time to time, are incorporated in this Novation Confirmation. In the event of any inconsistency between the Definitions and this Novation Confirmation, this Novation Confirmation will govern. In the event of any inconsistency between the Definitions and the 2003 ISDA Credit Derivatives Definitions, the Definitions will govern. In the event of any inconsistency between the Novation Agreement and this Novation Confirmation, the provisions set forth in this Novation Confirmation will govern.

2. The terms of the Novation Transaction to which this Novation Confirmation relates are as follows:

| | |
|---------------------------------------------------------|------------------------------------------------|
| Novation Trade Date: | 8 April 2004 |
| Novation Date: | 9 April 2004 |
| Novated Amount: | US\$ 5,000,000.00 |
| Transferor: | DEF Bank |
| Transferee: | XYZ Bank |
| Remaining Party: | ABC Bank |
| Reference Entity: | EMA, Inc (ISIN: 000000000000) |
| New Agreement (between Transferee and Remaining Party): | ISDA Master Agreement dated as of 30 June 1999 |

Credit Event Notice Delivered Under Old Transaction and Deemed Delivered Under New Transaction: None

Notice of Publicly Available Information Delivered Under Old Transaction and Deemed Delivered Under New Transaction: None

Notice of Physical Settlement Delivered Under Old Transaction, a copy of which is attached: None

3. The terms of the Old Transaction to which this Novation Confirmation relates are attached hereto as Exhibit A.

4. The terms of the New Transaction to which this Novation Confirmation relates shall be as specified in Sections 2, 3 and 4 of the copy of the Old Confirmation attached hereto as Exhibit A.

Full First Calculation Period: Applicable

5. Other Provisions relating to the New Transaction:

Additional Provisions: None

Credit Support Documents: None

6. Miscellaneous

Non-Reliance: Applicable

7. Notice Details:

Telephone and/or Facsimile Numbers for Notices:

Transferee: xxx-xxx-xxxx

Remaining Party: xxx-xxx-xxxx

Account Details:

Payments to ABC Bank: [.....][As per our Standard Settlement Instructions advised separately in writing]

Payments to XYZ Bank [.....][As per your Standard Settlement Instructions advised separately in writing][Please provide your settlement instructions]

Offices:

The Office of ABC Bank for the Transaction is: New York

The Office of XYZ Bank for the Transaction is: London

The parties confirm their acceptance to be bound by this Novation Confirmation as of the Novation Date by executing a copy of this Novation Confirmation and returning it to us. The Transferor, by its execution of a copy of this Novation Confirmation, agrees to the terms of the Novation Confirmation as it relates to the Old Transaction. The Transferee, by its execution of a copy of this Novation Confirmation, agrees to the terms of the Novation Confirmation as it relates to the New Transaction..

.....
ABC Bank

By:
Name:
Title:
Date:

.....
DEF Bank

By:
Name:
Title:
Date:

.....
XYZ Bank

By:
Name:
Title:
Date:

(Attach Old Confirmation as Exhibit A)

ISDA Operations Committee

Process Working Group

- Drive Process Efficiency
- Standardise Operational Practice
- Evolve 'Best Practice' Standards
- Influence Market Development / Technological Change

Best Practice Statement: Processing Novations

Purpose

The purpose of this Best Practice Statement is to outline guidelines for processing the transfer of privately negotiated or over-the-counter (“OTC”) derivative transactions confirmed under the terms of an ISDA Master Agreement.

ISDA publishes the following documents for use in effecting novations:

- long-form standard Novation Agreement, published in 2002; and
- 2004 ISDA Novation Definitions containing definitions, standard Novation Agreements and a short-form Novation Confirmation.

This Best Practice Statement addresses processing novations under the 2004 ISDA Novation Definitions and, in more general respects, applies to processing the novation of any Transaction documented under an ISDA Master Agreement.

Current State

- Differing standards and expectations exist across the market to process novations. This proliferation of practices causes uncertainty and consequent delays, increasing risks to the counterparties involved and creating operational inefficiency and backlogs in processing documentation.
- The ISDA Operations Process working group has consulted widely with ISDA members to identify the operational issues which cause problems in processing novations and has sought to address these directly in market discussions. The resulting consensus on a consistent approach going forward is set out in the Commentary which follows.
- Although parties are not obliged to adopt these guidelines, ISDA encourages participants to follow this Best Practice Statement in order to support a standardisation of the novations process.

Commentary

- **Notifications**

| | |
|--------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Transferor seeking approval | <ul style="list-style-type: none"> • The Transferor (outgoing party) should notify the Transferee (incoming party) and the Remaining Party of a novation on or before the Novation Date • The Novation Date needs to be agreed by all parties in advance of the transfer taking place so that the trade may be rebooked and reported accurately |
| Remaining Party communications | <ul style="list-style-type: none"> • All communications should be at Front Office level and relevant approvals obtained • Front Office personnel should ensure that any deals booked as cancellations or new trades which form part of novations are clearly identified as such to Operations support staff |

- **Effectiveness of Transfer**

| | |
|---------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Novation Date and Rebooking of trades | <ul style="list-style-type: none"> • The Novation Date is the date that the deal transfers, ie the rights and obligations of the Transferor are novated to the Transferee • The Transferor, Transferee and Remaining Party should rebook a novated trade to take effect from and including the Novation Date |
| Novation Trade Date | <ul style="list-style-type: none"> • Parties may, as part of the consent process on the Novation Trade Date, agree that the transfer will be effective from a forward starting Novation Date. This can occur for portfolio transfers where a longer lead-in period is required. A one Business Day delay in a Novation becoming effective is common practice for Credit Default Swaps |
| Due Date of Fees | <ul style="list-style-type: none"> • Payment of fees for the novation is a separate arrangement between the Transferor and the Transferee. Any 'effective date' agreed for calculation and settlement of fees is quite separate from the operation of Novation Date in relation to the Novation Transaction |

| | |
|---------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Treatment of Cash Flow accruals | <ul style="list-style-type: none"> • When a novation occurs part way through a Calculation Period, accepted market practice under the New Transaction is for cash flows to accrue: <ul style="list-style-type: none"> ▪ from the last applicable Period End Date (usually same as Payment Date) for each party under the Old Transaction; or ▪ if the first Period End Date has not yet occurred for a party, from the Effective Date of the Old Transaction • These cash flows are settled in full by the Transferee and the Remaining Party on the first Payment Date to occur under the New Transaction • The 2004 ISDA Novation Definitions use the full accrual method for both parties as a standard election and the definition for Full First Calculation Period applies as default • Parties may elect alternative arrangements. They may accrue their initial payment obligations under the New Transaction from a different date, eg the Novation Date. However, this requires agreement by the Remaining Party |
|---------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

- **Timelines of Process**

| | |
|-------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Guidelines on turnaround times (Business Days unless otherwise stated) | <p>T(-x) Transferor contacts Remaining Party for consent to novate</p> <p>T Transferor confirms date of transfer (Novation Date) to Transferee and Remaining Party (« T »)</p> <p>T Remaining Party rebooks the trade with Transferee</p> <p>T+1 If applicable, Remaining Party recalculates exposure, initiating collateral process per terms of bilateral CSA or other collateral agreement</p> <p>T+5 Novation Confirmation (Novation Agreement) dispatched by T+5 business days latest</p> <p>T+30 All documentation fully executed by Transferor, Transferee and Remaining Party by T+30 calendar days</p> <p>These guidelines follow market established practice for confirming transactions set out in Sound Practices and Escalation Procedures published on ISDA's website at www.isda.org. The published guidelines for Telephone Confirming Trades may also be relevant where parties wish to adopt this additional procedure</p> |
|-------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

- **Transferring the Trade**

| | |
|--------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Provision of 'original' confirmation | <ul style="list-style-type: none"> • A Transferor should, if available and if so requested, supply an original trade Confirmation to a Transferee prior to a novation taking place • A review of the original Old Confirmation should be undertaken by the Transferee for structured trades • If no Old Confirmation is available, a detailed statement of principal terms is acceptable, eg Term Sheet |
|--------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

| | |
|-------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Netting of trade positions | <ul style="list-style-type: none"> • Aggregation of trades with identical trade terms being novated from the same Transferor to the same Transferee should be at the discretion of the Remaining Party |
|-------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

- **Renegotiation of Terms**

| | |
|------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Mutual break-clauses | <ul style="list-style-type: none"> • Renegotiation of mutual break-clauses should be at the Remaining Party's discretion • In general market participants will consider renegotiating break-clause tenors to match their existing trading relationship with the incoming Transferee counterparty • Where a new break clause is added to a New Transaction, it is usual to run the first break date from: <ul style="list-style-type: none"> • the last common Payment Date to occur under the Old Transaction or, • if no Payment Date has occurred, from the Effective Date of the Old Transaction or, • if no Effective Date under the Old Transaction has occurred, from the Novation Date |
| Bilateral counterparty language | <ul style="list-style-type: none"> • Renegotiation of bilateral counterparty-specific language should be at the Remaining Party's discretion • A majority of participants are willing to consider amending vanilla deals (ie, without special terms) to include existing bilaterally agreed language with the incoming party. Examples are: <ul style="list-style-type: none"> Calculation Agent Collateral terms Calculation Agent City <p>Bilateral language in equity and commodity derivatives trades is typically agreed on a case-by-case basis</p> |

| | |
|------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Changes to other terms | <ul style="list-style-type: none"> • Any economic terms or special provisions should not be renegotiated. This includes conforming ‘original’ terms to market standards, eg, Business Days which may impact the risk and hedging of the trade for the Remaining Party • Any changes agreed to economic or, for example, fallback provisions which may have an economic impact should be specifically and separately agreed between the Transferee and the Remaining Party. • It is recommended that amendments to the terms of a New Transaction should fall outside the scope of the Novation process discussed here, and that these should be handled subsequently through each party’s usual amended confirmation procedures |
|------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

- **Documenting the Transfer**

| | |
|-----------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Who prepares the documentation | <ul style="list-style-type: none"> • The Remaining Party should document the Novation, unless otherwise agreed between the parties • The Remaining Party is a party to the original Confirmation and knows the terms of the original trade • Where the Remaining Party dispatches novation documentation within T+5 business days in ISDA standard format, best practice is to sign the Remaining Party’s agreement • If the Remaining Party fails to send ISDA standard documentation after T+5 business days, either the Transferor or Transferee can dispatch the required documentation for the novation and assume responsibility for the execution process • It is recommended that a party assuming responsibility for documenting a novation after T+5 should notify the Remaining Party that it intends to do so |
| Use of ISDA templates | <ul style="list-style-type: none"> • As far as possible, the standard template in the 2004 ISDA Novation Definitions should be used for the novation of vanilla OTC derivative transactions • More structured deals or portfolio transfers may require the long-form ISDA Novation Agreement published in April 2002. This is available from ISDA’s website at www.isda.org • In certain cases, bespoke amendments to ISDA standard documents may be required. These should be the exception rather than the rule |
| Counterparty regulatory language requirements | <ul style="list-style-type: none"> • Language covering counterparty regulatory requirements is recognised (eg, where one party acts through an agent, instructions are inserted to clarify requirements that all payments or deliveries go through that party’s agent and not directly between Party A and Party B) |

| | |
|--------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Non-Reliance | <ul style="list-style-type: none"> Older agreements may not include this language. The consensus agreed is to elect for Non-Reliance to apply since this will not override bi-laterally agreed language agreed by parties in governing ISDA Master Agreements |
|--------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

| | |
|---------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Attach Old Confirmation or New Confirmation | <ul style="list-style-type: none"> The 2004 ISDA Novation Definitions offer an opportunity to attach the New Confirmation (ie, for the trade between the Remaining Party and the Transferee) to the Novation Confirmation To document the novation of vanilla OTC derivative transactions, attaching the New Confirmation is considered best practice. This facilitates STP and the re-documentation of any Transferee bilateral terms Sufficient details of the original trade should be included on the Novation Confirmation or other Novation Agreement to identify the Old Transaction accurately Historically, participants have attached the original, or Old Confirmation, or a schedule to the standard ISDA long-form Novation Agreement. This alternative may still be appropriate for complex trades and bulk transfers |
|---------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

• **Legally Executing the Transfer**

| | |
|-----------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Match documentation or execute | <ul style="list-style-type: none"> It is recommended that a Novation Confirmation (or Novation Agreement) should be executed by all three parties Matching of Novation Confirmations (or Novation Agreements) is not considered accepted market practice |
| Signing in counterparts | <ul style="list-style-type: none"> There is industry agreement that signing in counterparts is acceptable and preferable wherever possible |
| Order for all three parties to sign | <ul style="list-style-type: none"> Parties are encouraged to sign the relevant Novation documents as soon as possible in order to complete the documentation process by T+30 calendar days at the latest The party assuming responsibility for documenting the novation has responsibility for distributing fully executed copies to other parties. (Normally the Remaining Party will initiate the novation documentation and facilitate all signatures) |
| Issuing separate Confirmations for New Transactions | <ul style="list-style-type: none"> Some market participants automatically generate and issue an independent Confirmation outside the documentation required for novation of the New Transaction. This practice should be discouraged |

- **Fees and Bilateral Arrangements**

| | |
|------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Fees | <ul style="list-style-type: none">• The outgoing Transferor and the incoming Transferee will typically agree a fee between them for the transfer of the trade• Calculations regarding this fee and its value date are outside the scope of this guidance statement• Fees and their settlement terms do not form part of the formal Novation Confirmation or Novation Agreement since these arrangements do not include the Remaining Party• A sample fee letter is attached as Appendix 1 which, subject to individual requirements, may be used between the Transferor and Transferee if required to document these separate arrangements |
|------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

Appendix A

Example Fee Letter

To: [Date]
Attn:
Tel:
Fax:

From:
Attn:
Tel:
Fax:

Dear Sir/Madam

Novation of OTC derivative Transaction

We refer to the Old Transaction identified below. We confirm our agreement that with effect from and including the Novation Date set out in the New Transaction below, you have novated the Old Transaction to us on the following terms and conditions:-

Old Transaction

Your Counterparty
Notional Amount
Effective Date
[Scheduled] Termination Date
Type of Transaction

New Transaction

Remaining Party
Novated Amount
Novation Date
Full First Calculation Period: Applicable/Inapplicable

Fees

Fee payable
Payable by
Payable to
Due date

In consideration for novating the Old Transaction, a Fee as identified above will be payable on or before the due date specified above in freely transferrable funds and in the manner customary for payments in the required currency.

This letter agreement may be executed in counterparts. Capitalised terms not otherwise defined in this letter agreement shall have the meaning given to them in the ISDA 2004 Novation Definitions. This letter agreement shall be governed by and construed in accordance with the laws of England.

Yours faithfully,

[Authorised

Signatory]

ISDA Statement on Consent Requirement for Transfer of Transactions

The ISDA Trading Practice Committee wishes to remind market participants that, under the ISDA Master Agreement¹, a party to a transaction must obtain the written consent of the other party to the transaction prior to transferring its rights and obligations under that transaction to a third party.

The decision as to whether or not to agree to a transfer is within the discretion of the party whose consent is required. Relevant factors in deciding whether to consent to a transfer include credit, collateral, netting, tax, operational, accounting, relationship and other considerations. Furthermore, these considerations may relate to either the transferor or the transferee. Examples of these considerations include:

- (1) The transfer of a single transaction or set of transactions can impact the credit exposure of the remaining party to the transferor by reason of the trades remaining in the portfolio or under other arrangements between the two parties that could be subject to a right of set-off.
- (2) The remaining party may attribute a value to its mark-to-market exposure to the transferor that is different than the value that it determines when that exposure is to a different party. Also, the remaining party may have entered into other transactions with the transferor in reliance on the value or credit exposure attributable to transactions between the parties. Termination of those other transactions may create an expense for the remaining party.
- (3) The cost to the remaining party to be in a contractual relationship with the transferee rather than the transferor may be materially different (for example, due to a requirement to post collateral to the transferee). The remaining party may wish to take this into account in evaluating its willingness to consent to the transfer of a transaction to that transferee.

¹ Section 7 of the 1992 ISDA Master Agreement provides:

Subject to Section 6(b) (ii), neither this Agreement nor any interest or obligation in or under this Agreement may be transferred (whether by way of security or otherwise) by either party without the prior written consent of the other party, except that: -

- (a) a party may make such a transfer of this Agreement pursuant to a consolidation or amalgamation with, or merger with or into, or transfer of all or substantially all its assets to, another entity (but without prejudice to any other right or remedy under this Agreement); and
- (b) a party may make such a transfer of all or any part of its interest in any amount payable to it from a Defaulting Party under Section 6(e).

Any purported transfer that is not in compliance with this Section will be void.

The 2002 ISDA Master Agreement is, in substance, the same with two modifications: (i) the phrase “and to the extent permitted by applicable law” is added in the first line after the reference to Section 6(b)(ii) and (ii) the phrase “, together with any amounts payable on or with respect to that interest and any other rights associated with that interest pursuant to Section 8, 9(h) and 11.”

These considerations are provided by way of example. They are not intended to be an exclusive list of the considerations that may be taken into account by a party in deciding whether or not to agree to a transfer. Whether or not a party agrees to a transfer will be dependent on the facts and circumstances involved in any specific transfer request. In particular, because of the economic considerations involved for all three

parties (transferor, transferee and remaining party), compensation may be an appropriate matter for discussion in connection with a transfer.

A novation working group, consisting of ISDA members active in the operations and documentation areas, was formed earlier this year and will look at various operational and legal issues surrounding the novation agreement published in May 2002 by ISDA and the novation provisions in the 2003 Credit Derivatives Definitions. Based on input from working group members, and expected input from a questionnaire that has been distributed to the wider Operations Committee, the working group will produce a flow-chart to describe the novation process. The working group will also start working on a novations definitions booklet with templates that cover different types of transfers and product categories.

If you would like to receive information regarding the consideration of these issues by the novation working group, please contact Kimberly Summe (ksumme@isda.org) or Karel Engelen (kengelen@isda.org).