International Swaps and Derivatives Association, Inc.
One Bishops Square
London E1 6AD
United Kingdom
Telephone: 44 (20) 3088 3550
Facsimile: 44 (20) 3088 3555
email: isdaeurope@isda.org
website: www.isda.org

Per E-mail

Department of Finance

Government Buildings

Upper Merrion Street

Dublin 2

Attn. Ann Nolan (ann.nolan@finance.gov.ie) and Aidan Carrigan (aidan.carrigan@finance.gov.ie)

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Dear Sirs

National Asset Management Agency Bill 2009 (the "NAMA Bill") – concerns regarding the implications for legal certainty

1. Background

The International Swaps and Derivatives Association, Inc. ("ISDA")[1] has been following closely the progress of the NAMA Bill and wishes to bring to your attention certain concerns that it has identified regarding the implications of the NAMA Bill for legal certainty.

ISDA defers, of course, to national experts in Ireland on the appropriateness, generally, of the provisions of the NAMA Bill to address the threats to the Irish economy and the systemic stability of credit institutions in Ireland, and the need for the maintenance and stabilisation of the financial system in Ireland, noted in section 2 of the NAMA Bill. However, ISDA would like to bring to your attention, from an international perspective, a particular aspect of the NAMA Bill that has the potential to have a significant adverse effect on the transaction by participating institutions (within the meaning of the NAMA Bill) of domestic and

[1] ISDA is the global trade association representing leading participants in the privately negotiated derivatives industry, a business that includes interest rate, currency, commodity, credit and equity swaps, options and forwards, as well as related products such as caps, collars, floors and swaptions. ISDA currently has more than 830 member institutions from 58 countries on six continents, including dealers, service providers or end users of derivatives. ISDA member institutions encompass potential participating institutions, within the meaning of the NAMA Bill and potential derivatives counterparties of such potential participating institutions. A core part of ISDA's mission is to strengthen the legal infrastructure of the financial markets. ISDA seeks to do this in several ways, including strengthening legal certainty by promoting appropriate law reform.

cross-border financial transactions, including privately negotiated or "over-the-counter" (OTC) derivative transactions ("Relevant Transactions").

2. Concern – partial property transfers

We note that the provisions of Section 213 of the NAMA Bill seek to protect certain early termination, close-out netting, set-off and financial collateral arrangements the subject of existing legislative protections (each a "Protected Arrangement") and ISDA welcomes the inclusion of such protections. However, the fact that the NAMA Bill envisages that partial property transfers - potentially of some, but not all, of a participating institution's rights and obligations arising under a Protected Arrangement - may be effected raises a significant risk of legal uncertainty for Protected Arrangements. If some, but not all, of such rights and obligations were "cherry-picked" for transfer pursuant to the NAMA Bill, the net position of that participating institution's counterparty (and, indeed, of that participating institution) would be disrupted notwithstanding the provisions of Section 213.

Our concerns in relation to this issue are heightened by:

(a) our experience from similar legislative efforts that have been concluded recently or are currently under way in several European jurisdictions. In particular, the Banking Act 2009 in the United Kingdom comes to mind. During the UK consultations industry put particular emphasis on the possibility that the stabilisation measures provided for in the UK Banking Act 2009, which included a partial property transfer power (the power to effect a transfer of some but not all of the property, rights and liabilities of an affected UK institution), could be used to "cherry-pick" transactions, or even parts of transactions, under a netting arrangement, or otherwise disrupt the mutuality of obligations under a netting or set-off agreement; and

(b) comparisons drawn by ISDA members, in the context of partial property transfers, between the NAMA Bill and the situation that was anticipated to pertain in the UK, had the relevant UK protections not been introduced.

ISDA was closely involved in the consultation process undertaken in the UK in relation to these measures, with a view to ensuring that concerns regarding the implications of partial property transfers for netting/collateral arrangements was adequately addressed. It is notable that, in the UK context, the validity of the industry concern in this regard was always acknowledged by the relevant authorities (HM Treasury, the Bank of England and the Financial Services Authority)[2], so that the consultation process, in this regard, focused on how best to structure the relevant protections. As you are probably aware, the relevant protections were set out in Article 3(1) of The Banking Act 2009 (Restriction of Partial Property Transfers) Order 2009, as amended by The Banking Act 2009 (Restriction of Partial Property Transfers) (Amendment) Order 2009. Article 3(1) provides that a partial property transfer, within the meaning of the

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[2] See, for example, paragraphs 2.16 and 2.17 of the consultation document "Special regime: safeguards for partial property transfers" (Cm 7497) issued by HM Treasury in November 2008: "2.16 The Government's clear intention is to protect contracts relevant for regulatory capital purposes from the threat of disruption under a partial transfer. Therefore this consideration will outweigh any of the carve-outs listed above. 2.17 Overall, this option is framed in order to offer the market certainty on set-off and netting. Except for the contracts excepted under the carve-outs, counterparties would have certainty that their relationship with the failed bank would be transferred whole, or not at all, and that their set-off and netting calculations would not be disrupted.

legislation, may not provide for the transfer of some, but not all, of the "protected rights and liabilities" between the affected UK institution and a third party under a "netting agreement"."

3. Potential impact on participating institutions and their counterparties

Risk management policies of parties to Relevant Transactions tend to require such parties to monitor credit exposure to counterparties under Relevant Transactions and, where relevant, put in place appropriate risk-reducing close-out netting and collateral arrangements. In the case of a party that is subject to prudential supervision (such as an Irish or foreign bank), whether it can treat its exposure to a Relevant Transactions counterparty as net, and take related collateral arrangements into account for risk-reducing purposes, will also be key to the level of capital that the party is required to allocate to Relevant Transactions with that counterparty.

A supervised institution will not be able to recognise close-out netting or a related collateral arrangement unless it can satisfy its supervisor that the close-out netting or collateral arrangement is enforceable with a high degree of legal certainty and with no unduly restrictive assumptions or material qualifications. Currently such opinions can be obtained in respect of potential participating institutions (within the meaning of NAMA) in respect of many industry close-out netting and collateral agreements (including those the subject of ISDA publications).

If the position in this regard were to change, the commercial and financial implications for potential participating institutions and their counterparties to Relevant Transactions would be severe in that:

(a) supervised institutions would be constrained in their ability to extend credit, or otherwise incur exposures, to participating institutions;

(b) supervised[3] participating institutions themselves would find their own ability to conduct business constrained by much heavier capital requirements and their access generally to liquidity would be impaired.

Whereas the “super-priority” afforded by Section 213 of the NAMA Bill for Protected Arrangements assists in avoiding the negative implications of a change of law outlined at paragraphs (a) and (b) above, a concern remains that a participating institution’s counterparty’s net exposure could be disrupted by a partial property transfer of the type outlined at paragraph 2. If such a partial transfer of a bank asset by a participating institution to NAMA or a NAMA group entity occurred (or by NAMA or a NAMA group entity to a third party) occurs, the fact that the participating institution’s counterparty may terminate the agreement with the participating institution and enforce the close-out netting and collateral provisions will not provide comfort if, as a result of the transfer, the transactions the subject of the netting/collateral arrangement have changed so that its net exposure differs from that which would have pertained but for the partial transfer.

4. Recommendation

ISDA therefore strongly recommends that safeguards be introduced to the NAMA Bill to ensure that a Protected Arrangement may only be transferred as a whole under the NAMA Bill, or not at all, and that

[3] We note that the concept of a “participating institution” includes a credit institution designated by the Minister under section 65 of the Bill *including any of its subsidiaries that is not excluded under that section*, and so can include non-supervised entities.

individual rights and obligations under the Protected Arrangement should not be vulnerable to cherry-picking. We would be happy to input on the drafting of those safeguards, if that would be helpful. We would, however, like to emphasise the importance of such safeguards providing the level of legal certainty necessary to permit outside counsel to opine on these issues with sufficient robustness that will enable supervised institutions to calculate, for regulatory capital purposes, their exposures on a net basis and rely on those calculations from a risk management perspective.

5. Amendments to provisions of Protected Arrangements

An additional issue of concern to us is the proposal that, after acquisition of a bank asset (which can encompass a Relevant Transaction) by NAMA or a NAMA group entity, NAMA may change a term or condition of that bank asset where it is of the view that it is no longer reasonably practicable to operate that term or condition4. Whereas it is clear that, given the terms of Section 213, changes could not be introduced pursuant to Section 99(3) that would prevent the operation of the legislation referred to in Section 213, the absence of legal certainty that would arise from this unilateral right to amend other contractual terms of Relevant Transactions – particularly when taken together with the provisions of Section 107 of the NAMA Bill – seems likely to have a negative impact on the ability of participating institutions to transact Relevant Transactions.

We would strongly recommend that no greater modification to, or invalidation of, Relevant Transactions of participating institutions occurs than is strictly necessary in the context of circumstances that the NAMA Bill is designed to address, as outlined in section 2. If it is considered strictly necessary to extend the ambit of Sections 99(3) and 107 to Relevant Transactions, it would be important at least to include some parameters on the nature of changes that could be made pursuant to Section 99(3), so as to limit legal uncertainty and the consequential negative implications for participating institutions' ability to continue to transact Relevant Transactions.

We would be happy to discuss this issue with you if that would be helpful. Please contact the undersigned (ISDA European Office, One Bishops Square, London E1 6AD, U.K., pwerner@isda.org) if we can be of any assistance.

Yours faithfully,

Dr Peter M Werner
Director of Policy
pwerner@isda.org

[4] Section 99(3) of the NAMA Bill.