

**Commentary on the
Form of Amendment to ISDA Master Agreements**

THE AMENDMENTS DISCUSSED IN THIS COMMENTARY ARE FOR USE BY PARTIES TO ISDA MASTER AGREEMENTS AS THEY DEEM APPROPRIATE BASED ON THEIR OWN CIRCUMSTANCES. THIS COMMENTARY DOES NOT PURPORT, AND SHOULD NOT BE CONSIDERED, TO BE A GUIDE TO OR EXPLANATION OF ALL ISSUES AND CONSIDERATIONS THAT MAY BE RELEVANT TO A PARTICULAR CONTRACTUAL RELATIONSHIP. EACH PARTY SHOULD THEREFORE CONSULT WITH ITS LEGAL ADVISERS AND ANY OTHER ADVISERS IT DEEMS APPROPRIATE PRIOR TO USING THE AMENDMENT OR ANY OTHER ISDA STANDARD DOCUMENTATION. ISDA ASSUMES NO RESPONSIBILITY FOR ANY USE TO WHICH ANY OF ITS DOCUMENTATION OR ANY DEFINITION OR PROVISION CONTAINED IN ITS DOCUMENTATION MAY BE PUT.

I. FORM OF AMENDMENT TO ISDA MASTER AGREEMENTS

Beginning in late 1999, ISDA conducted a review and analysis of certain provisions of the ISDA Master Agreements.¹ This process took into account the recommendations on documentation contained in the June 1999 report of the Counterparty Risk Management Policy Group entitled “Improving Counterparty Risk Management Practices” (the “CRMPG Report”) and the experiences of ISDA’s members (both dealers and end-users) since publication of the ISDA Master Agreements in 1992.

Several working groups were formed in late 1999 to prepare amendments to various Sections of the ISDA Master Agreements. Initially, it was proposed that such amendments to ISDA Master Agreements be accomplished through the use of a Protocol, but the working groups concluded that such a Protocol was too complicated from an operational and logistical perspective, given the number and nature of the proposed amendments. Thus, it was decided that ISDA should publish a form of Amendment to the ISDA Master Agreements (the “Amendment”), whereby parties could incorporate these amendments into their ISDA Master Agreements on a bilateral basis (each amendment is presented as an “Attachment”). At the same time that the Amendment was published, ISDA decided to proceed with the preparation of a new ISDA master agreement. The Attachments to the Amendment are expected to form the basis for an initial draft of the new master agreement.

The amendments to the ISDA Master Agreements have been organized into Attachments for purposes of ready adoption by parties. In the Amendment, parties should incorporate only those Attachments they select to amend their ISDA Master Agreements and delete any references to Attachments they do not select.

¹ As used in this Commentary, unless otherwise indicated, the term “ISDA Master Agreements” is intended to refer to the ISDA Master Agreement (Multicurrency – Cross Border) and the ISDA Master Agreement (Local Currency – Single Jurisdiction), each as published by ISDA in 1992.

All section references in this Commentary are to the more widely used Multicurrency-Cross Border version of the ISDA Master Agreement (the “Master Agreement”), unless specifically indicated otherwise. Users of the Amendment should note that the forms of Attachments have been prepared on the assumption that the agreement to be amended is in the form of the relevant Master Agreement, as published by ISDA. The Attachments do not anticipate any amendments that the parties to an agreement might have made to this form. Parties should therefore be aware that, to the extent the Attachments refer to provisions of the Master Agreement that have been amended or to issues that are addressed elsewhere in the parties’ agreement, adjustments to the terms of the Attachments may be required.

Attachments 1 to 8 have been designed to be used with either form of the ISDA Master Agreements, but certain section references will need to be altered if the agreement to be amended is in the Local Currency – Single Jurisdiction form. These alterations are noted in the Attachments themselves by way of footnotes. Attachment 9 was drafted with the intention that it would be used only in connection with the Multicurrency – Cross-Border form. If parties wish to use this Attachment in connection with the Local Currency – Single Jurisdiction form, appropriate changes would need to be made. Parties to any other form of ISDA standard form agreement, including the ISDA Interest Rate and Currency Exchange Agreement and the ISDA Interest Rate Swap Agreement, should consult with their legal advisers or any other advisers they deem appropriate prior to entering into the Amendment.

II. ATTACHMENT 1 – CONDITION PRECEDENT

This amendment adds a new subclause (iv) to Section 2(a) of the Master Agreement. This clause specifies that the Section 2(a)(i) obligations of one party are conditional when an Additional Termination Event which affects all then outstanding Transactions has occurred and is continuing with respect to which the second party is an Affected Party. This permits the first party to withhold payments after the occurrence of one of these events with respect to the second party without being required to designate an Early Termination Date for the Affected Transactions. The intent is to provide more flexibility for the first party in dealing with the consequences of Additional Termination Events. A number of members are of the view that, because most Additional Termination Events are credit-related, the occurrence of an Additional Termination Event should be treated in a manner similar to an Event of Default. Parties should consider whether non-credit related events which may nonetheless have been specified by them to be Additional Termination Events should continue to be treated as Additional Termination Events in light of this amendment or whether the applicability of this provision should be limited to Additional Termination Events that are credit-related. It should be noted that if the parties incorporate Attachment 9, a new condition precedent set forth in Section 2(a)(v) would be added.

III. ATTACHMENT 2 – FAILURE TO PAY OR DELIVER

This amendment adds a new clause (2) to Section 5(a)(i) (Failure to Pay or Deliver) of the Master Agreement. This amendment also adds to what becomes clause (1) of Section 5(a)(i), the introductory phrase “in the case of any such payment” and changes “third Local Business Day” to “first Local Business Day”.

The addition of a new clause (2) and a new introductory phrase to clause (1) has the effect of distinguishing between failures to pay and failures to deliver. A failure to pay now becomes an Event of Default one Local Business Day after notice of such failure is given to the relevant party. Many market participants found three Local Business Days after notice to be too long a period during times of market stress in 1998.

At the same time, failures to deliver items such as securities or commodities were found to require more flexibility. For example, problems in a local settlement system can cause a failure to deliver without fault on the part of the party required to make a delivery under a Master Agreement. Consequently, a new term, “Local Delivery Day”, has been added and a failure to deliver becomes an Event of Default on the first Local Delivery Day after notice of failure to deliver is given, which may or may not be the first Local Business Day. A Local Delivery Day is a day on which settlement systems are generally open for business such that delivery of the items is capable of being accomplished in accordance with customary market practice. “Customary market practice” is intended to refer to generally recognized practice in regard to the delivery of securities or other relevant items in a particular jurisdiction. Problems in a local settlement system on a given day could, depending upon the specific circumstances, result in that day not being a Local Delivery Day as either the settlement system would not be open or delivery could not be accomplished due to those problems.

IV. ATTACHMENT 3 – DEFAULT UNDER SPECIFIED TRANSACTION AND ATTACHMENT 7 – SPECIFIED TRANSACTION

Attachment 3 and Attachment 7 are connected in that Attachment 7 contains the definition of “Specified Transaction” and Attachment 3 contains the description of the related Event of Default. While parties to a Master Agreement may agree to one or both of these amendments as they deem appropriate, they are considered together in this Commentary because certain changes in Attachment 7 led to a change in Attachment 3.

Attachment 7 divides clause (a) in the definition of “Specified Transaction” in the Master Agreement into parts (i) and (ii). Clause (a)(i) is expanded from clause (a) in the Master Agreement to include various credit derivatives as well as repurchase transactions, reverse repurchase transactions, buy/sell back transactions, securities lending transactions and forward purchases or sales of a security. Clause (a)(i) is also changed from the printed form of Master Agreement to delete the phrase “or any other similar transaction”, which is treated more comprehensively in the new clause (a)(ii).

Clause (a)(ii) in Attachment 7 is intended to clarify the types of new transactions that will become “Specified Transactions” as markets evolve over time. It also reflects the expanded scope of the definition of “swap agreement” currently under consideration by the U.S. Congress in the financial contract provisions of the proposed U.S. Bankruptcy Reform Act of 2001.

The expansion of the definition of “Specified Transaction” by Attachment 7 has been considered by counsel in all jurisdictions where ISDA has obtained netting opinions to date, and the guidance obtained from such counsel is available to all ISDA members upon request. Parties are encouraged to review this guidance to ensure that they are comfortable with this expansion in regard to the relevant jurisdictions.

Parties that have amended a Master Agreement to provide that all “Specified Transactions” will be “Transactions” for the purposes of that Master Agreement should consider the impact of this change to the definition of Specified Transaction on that Master Agreement. The combined effect of the prior amendment and Attachment 7 may cause certain transactions to be deemed to be documented under the Master Agreement, even though those transactions are subject to the terms of another industry master agreement.

Attachment 3 amends clause (2) of Section 5(a)(v) (Default under Specified Transaction) of the Master Agreement in two respects. First, the deemed grace period in the parenthetical in clause (2) is shortened to one Local Business Day from three Local Business Days. This is consistent with the similar

change made by Attachment 2 to Section 5(a)(i) and explained above under that heading. This deemed grace period is only relevant if the underlying obligation has no applicable notice requirement or grace period.

Second, a phrase is added at the end of Section 5(a)(v)(2) to require, in the case of a failure to deliver, that “such failure constitutes an event of default with respect to all transactions included under the documentation applicable to such Specified Transaction”. This change is responsive to comments made on drafts of Attachment 3 and Attachment 7. Several market participants observed that the addition of transactions such as repurchase agreements and securities lending transactions to the definition of “Specified Transaction” could have the effect of making failures to deliver securities that are not events of default under the relevant repurchase or securities lending agreements into Events of Default under a Master Agreement. It was also noted that failures to deliver occur with some frequency in connection with repurchase and securities lending transactions due to administrative or settlement system problems. The phrase included at the end of Section 5(a)(v)(2) in Attachment 3 is intended to make clear that a failure to deliver at maturity under a transaction such as a repurchase or securities lending transaction becomes an Event of Default under a Master Agreement if an event of default has been triggered under the documentation relating to the repurchase or securities lending transaction (i.e., the parties to that transaction have agreed in the relevant documentation that a failure to deliver is or can become an event of default and any notice has been given that is required to make it an event of default for all transactions included under the relevant documentation that includes the Specified Transaction). The “mini close-out” mechanics, which are applicable to a single transaction, found in certain repurchase and securities lending master agreements will not form the basis for a Default under Specified Transaction under the Master Agreement unless and until they cause an event of default in respect of all transactions under such agreement.

Parties should also consider the addition of the new term, “Local Delivery Day”, as discussed in Section III of the Commentary above.

V. ATTACHMENT 4 - BANKRUPTCY

Attachment 4 modifies clause (4) of Section 5(a)(vii) (Bankruptcy) of the Master Agreement in order to distinguish between proceedings started by a party or its principal regulator, on the one hand, and by other third parties, on the other hand. Section 5(a)(vii) of the Master Agreement treats all proceedings started by third parties in the same way. Unless a judgment of insolvency or bankruptcy occurs earlier, the party subject to the petition is given 30 days to try to have the petition discharged or stayed. After market events in 1998, many market participants thought that a 30-day Waiting Period is too long. Through discussion a consensus emerged to treat differently proceedings started by officials with primary insolvency or rehabilitative jurisdiction and proceedings started by other third parties. The former are now treated the same as proceedings started by a party itself; they are Events of Default immediately. Proceedings started by other third parties are now subject to a five Local Business Day Waiting Period unless a judgment of insolvency or bankruptcy or other Event of Default occurs earlier.

In recognition of the shorter grace period for proceedings brought by third parties described in Section 5(a)(vii)(4)(B), Section 6(a) of the Master Agreement is also amended so that Automatic Early Termination, if elected by the parties, no longer applies to proceedings described in Section 5(a)(vii)(4)(B). This change has been reviewed by ISDA’s netting counsel in three jurisdictions (Germany, Japan and Switzerland) where Automatic Early Termination is recommended. Counsel in all three jurisdictions have verbally confirmed to ISDA that this change would not affect their netting

opinion, and this view will be officially confirmed in the netting opinion update process currently underway.

VI. ATTACHMENT 5 – CREDIT EVENT UPON MERGER

Section 5(b)(iv) (Credit Event Upon Merger) of the Master Agreement covers only certain events that result in a party having materially weaker credit. The events covered include mergers and the transfer of all or substantially all the assets of a party. Attachment 5 expands Section 5(b)(iv) to cover other change of control transactions and capital restructurings that result in the creditworthiness of a party being materially weaker than it was immediately prior to the transaction in question.

VII. ATTACHMENT 6 - NOTICES

Attachment 6 amends Section 12(a) (Notices-Effectiveness) of the Master Agreement in two main respects. First, the parenthetical in the second and third lines of Section 12(a) is deleted in Attachment 6 so that notices under Section 5 or 6 of the Master Agreement may be given by any of the specified methods. The inability to give notices under Sections 5 or 6 via facsimile or electronic messaging systems proved to be unduly restrictive during the market turbulence experienced in 1998. Second, Attachment 6 adds a new clause (a)(vi) to permit giving notice via e-mail, the effectiveness of which is upon delivery of the email.

VIII. ATTACHMENT 8 – SECTION 6 AND RELATED AMENDMENTS

1. Introduction. The CRMPG Report considered the Market Quotation method of valuing transactions after early termination of a Master Agreement in light of market disruptions in 1998. Some ISDA members reported uncertainty and delays in determining when to fall back to the Loss method in the Master Agreement, as contemplated in the definition of Settlement Amount. The CRMPG Report recommended the use of the Loss method due to its greater flexibility.

Other ISDA members commented that Market Quotation frequently has worked well, and they thought it should be preserved as a valid and enforceable valuation method. After long discussions it was decided that Market Quotation and Loss in reality reflect the existence of a continuum of methods for valuing terminated transactions. In stable markets, price quotations are readily available, particularly, for relatively simple transactions. In turbulent markets, price quotations may not be available, but other market data is available to provide a basis for commercially reasonable valuations. ISDA members also wished to take account of the need to value complex transactions as well as the development of more sophisticated internal valuation systems. A consensus developed that ISDA should combine elements of both Market Quotation and Loss into one valuation provision, which is called “Replacement Value”. As Replacement Value contains elements of both Market Quotation and Loss, it is important to note that those two methods remain valid valuation techniques. In all events it is important that the Non-defaulting Party use commercially reasonable procedures in order to avoid successful challenges to its determinations.

2. Section 6 Changes. Attachment 8 makes changes to Section 6 that reflect the elimination of “Market Quotation” and “Loss” and the addition of “Replacement Value”.

Attachment 8 changes the parenthetical in Section 6(d)(i)(1) to refer to “all relevant market information” rather than “all relevant quotations”. This reflects the greater flexibility in Replacement Value with respect to the sources of information to be used for valuations.

Attachment 8 simplifies Section 6(e) based upon the use of only one valuation method rather than the two found in the Master Agreement.

The definition of “Settlement Amount” in Attachment 8 has been simplified for the same reason.

3. *Replacement Value.* The first section of the definition of “Replacement Value” establishes the basic principle that should guide the use of the various types of flexibility contemplated in the remainder of the definition. The Determining Party or its agent is to value transactions “in good faith using commercially reasonable procedures”.

The first three paragraphs of the definition of “Replacement Value” then establish parameters for the procedures to be followed.

A. Grouping. Determinations may be made for all Terminated Transactions, any group of Terminated Transactions or individual Terminated Transactions. Valuations must be made, however, for all Terminated Transactions.

B. Methods. A Determining Party may apply different valuation methods to different transactions or group of transactions. This permits, for example, a Determining Party to distinguish between simple and complex transactions and between transactions where the underlying markets are liquid or illiquid.

C. Timing. Each Replacement Value is to be determined as of the relevant Early Termination Date, or if that would not be commercially reasonable, as of the latest dates before or the earliest dates after that would be commercially reasonable. This flexibility is important, for example, in valuing large portfolios or in illiquid markets. Price quotations will remain an important source for determining values, and dealers provide quotations on a real time rather than an “as of” basis. Establishing Replacement Values on a date before the Early Termination Date will occur in unusual circumstances. An example was the need to use the most recent available information for the Kuwaiti Dinar after the virtual disappearance of the currency after the invasion of Kuwait in 1990.

D. Sources of Information. While price quotations will remain an important source of information for establishing Replacement Values, other sources of market data may also be used as appropriate in the circumstances.

E. Credit. The Determining Party may take into account its creditworthiness and its credit and documentation policies. The Determining Party’s instructions to third parties should clearly state whether or not these factors are to be taken into account by the third party. Any differences in applying these factors to different transactions should have a commercially reasonable basis.

The fourth paragraph of the definition of “Replacement Value” lists certain costs or gains that may be taken into account. The listed items are derived from either “Market Quotation” or “Loss”. The listed items must be taken into account “without duplication”.

4. *Housekeeping Matters.* Part IV of Attachment 8 deletes the definitions of “Loss”, “Market Quotation” and “Reference Market-makers” from a Master Agreement, but it preserves those terms to the extent they are used outside Sections 5 and 6 of the Master Agreement for purposes of an Annex, a Schedule or a Confirmation.

IX. ATTACHMENT 9 – ILLEGALITY AND FORCE MAJEURE

1. **Amendment.** Although the printed form of the Master Agreement contains an Illegality Termination Event, a form of “Impossibility” or “Force Majeure” provision is not included. The User’s Guide to the ISDA Master Agreements published in 1993 explains the background to the decision not to include such a provision and contains a form of suggested wording for an “Impossibility” provision. In addition, various ISDA definitions booklets (in particular, the 1998 FX and Currency Option Definitions published by ISDA, the Emerging Markets Traders Association (“EMTA”) and The Foreign Exchange Committee) contain provisions that are intended to allow parties to address force majeure and impossibility in the context of specific transactions.

In response to concerns voiced by its members, ISDA established a Force Majeure and Impossibility Working Group (the “Force Majeure Working Group”) to consider whether it was appropriate to establish a standard set of provisions that could be used to address force majeure and impossibility issues at a master agreement level and to amend the existing illegality provisions. The Force Majeure Working Group decided that it was appropriate to do so and prepared the force majeure provisions (the “Force Majeure Provisions”) reflected in Attachment 9.

The Force Majeure Provisions are intended to be incorporated into Master Agreements as a whole. If parties wish to apply the Force Majeure Provisions selectively to their Master Agreement, they should consult with their legal advisers or any other advisers they deem appropriate and should ensure that care is taken in transcribing the relevant provisions.

The Force Majeure Provisions assume that the Master Agreement between the parties has not been amended in any material way, and in particular has not been amended to: (i) alter the governing law of the Master Agreement to that of a jurisdiction other than England or the State of New York; or (ii) alter the Events of Default or Termination Events so as to include a force majeure, impossibility or similar provision. To the extent that parties have amended their Master Agreement in any material way and, in particular, to alter the governing law or to add a force majeure, impossibility or similar provision, they should consult with their legal advisers or any other advisers they deem appropriate prior to entering into the Amendment.

2. **Background.**

The Force Majeure Provisions are intended to allow parties to a Master Agreement to address within their Master Agreement certain events that could affect their ability to perform obligations under the Master Agreement. The types of events that the Force Majeure Provisions are intended to address are those that make it unlawful, impossible or impracticable for a party (or its Credit Support Provider) to perform, or that otherwise prevent the party (or its Credit Support Provider) from performing, its obligations under the Master Agreement or Credit Support Document. These events could be caused by a change in law or by a natural or man-made disaster, armed conflict, act of terrorism, riot, labor disruption, or any other circumstance beyond a party’s control.

A schematic diagram reflecting the way in which the Force Majeure Provisions are intended to work is attached as Exhibit I.

3. *Section-by-Section Analysis.*

A. General Comments. The types of events covered by the Force Majeure Provisions fall into two categories:

(a) *Illegality.* Illegality is defined to include events or circumstances that make it unlawful for a party to make or receive a payment or a delivery under the Master Agreement (including a termination payment due under Section 6(e) of the Master Agreement) or for a party's Credit Support Provider to perform its obligations under a Credit Support Document. These are events that would fall within the Illegality Termination Event contained in Section 5(b)(i) of the Master Agreement. However, a new Section 5(b)(i), that effectively replaces the existing clause, is set out in Paragraph (c) of the Force Majeure Provisions.

(b) *Force Majeure Event.* Force Majeure Event is defined to include events that are categorized as force majeure or acts of state and that would either prevent a party from making or receiving a payment or delivery under the Agreement (including a termination payment due under Section 6(e) of the Master Agreement) or make it impossible or impracticable for the party to make or receive such payments or deliveries. As with Illegality, events affecting a Credit Support Provider's ability to perform under any Credit Support Document are also included. This second category of events is included in a new Termination Event (Section 5(b)(vi) (for the Multicurrency - Cross Border Master Agreement) or Section 5(b)(iv) (for the Local Currency - Single Jurisdiction Master Agreement)) that is set out in paragraph (e) of the Force Majeure Provisions.

As set out in the Force Majeure Provisions, both Illegality and Force Majeure Event are subject to a Waiting Period. An event that would otherwise constitute an Illegality or a Force Majeure Event, as the case may be, will only become a Termination Event if the relevant Waiting Period has expired. The Waiting Period creates a "wait and see" period during which neither party would be entitled to terminate Transactions. During this period, all payment and delivery obligations under Transactions affected by the Illegality or Force Majeure Event are suspended (see Paragraph J below). The Waiting Period for Illegality is three Local Business Days following the occurrence of the relevant event, and the corresponding period for Force Majeure Events is eight Local Business Days.

The Force Majeure Working Group generally agreed that the scope and extent of events falling within the definition of Illegality would be ascertained in a relatively short period of time. The effect of these events is also typically more long-lasting than other force majeure events. Consequently, a short Waiting Period of three days was thought to be appropriate for these events: at the end of three days, if the event still exists, the parties will be entitled to terminate.

Conversely, a wide range of events could be encompassed by the definition of Force Majeure Event. The impact of certain events, for instance, natural disasters, may not be clear within several days after the event. Furthermore, events of this type may be short-lived and a right of termination may be inappropriate. A longer Waiting Period of eight days has therefore been introduced for Force Majeure Events.

The concept of Waiting Periods has been introduced to compensate, in part, for the disapplication of Section 6(b)(ii) of the Master Agreement (Transfer to Avoid Termination Event) in relation to Illegality and the fact that Section 6(b)(ii) of the Master Agreement has not been made applicable to Force Majeure Events (see Paragraph H below).

There is express recognition in the Force Majeure Provisions that the parties may have agreed elsewhere in their contract (often in a Confirmation and on the terms of standard provisions included in sets of ISDA definitions) for specific fallbacks or remedies for one or more of the events that would otherwise constitute an Illegality or a Force Majeure Event. For example, as noted above, the parties using the 1998 FX and Currency Option Definitions may agree upon one of the approaches to a change in law provided for in those Definitions. The new Illegality and Force Majeure Event provisions defer to these other contractual remedies, so that the new provisions will only apply if the illegality, impossibility or impracticability exists “after giving effect to any applicable provision, disruption fallback or remedy specified in, or pursuant to, the relevant Confirmation or elsewhere in [their Master Agreement or any definitional booklets applicable to the Transaction]”.

B. Condition Precedent. The provision discussed here is contained in Paragraph (a) of the Force Majeure Provisions.

Section 2(a)(iii) contains conditions precedent which allow a non-Affected or Non-defaulting Party to defer making payments in regard to Affected Transactions to the Affected or Defaulting Party in certain situations. These conditions precedent are set forth in a new subsection which applies specifically to situations where an Illegality or Force Majeure Event has occurred so that the non-Affected Party in these cases is able to defer making payments in regard to Affected Transactions to the Affected Party for so long as the Illegality or Force Majeure Event is continuing. This provision will become a new Section 2(a)(iv).

C. Illegality. The provisions discussed here are contained in Paragraph (c) of the Force Majeure Provisions.

As noted above, Illegality can be broadly described as covering events or circumstances that make it unlawful for a party to make or receive a payment or a delivery under the Master Agreement (including a termination payment due under Section 6(e) of the Master Agreement) or for a party’s Credit Support Provider to perform its obligations under a Credit Support Document.

The relevant event will constitute an Illegality if the performance of a payment or delivery obligation under the Master Agreement is unlawful under any applicable law; in other words, an event could give rise to an Illegality even if it were not an illegality under the governing law of the contract, be it English law or New York law. This approach is intended to give express recognition to the fact that other laws may impact upon the parties’ contractual obligations.

D. Force Majeure Event. The provisions discussed here are contained in Paragraph (e) of the Force Majeure Provisions.

Force Majeure Event is included in the Master Agreement as a Termination Event under Section 5(b) of the Master Agreement. In brief, a Force Majeure Event is triggered if a party is prevented from making or receiving payment or delivery under a Transaction (including a termination payment due under Section 6(e) of the Master Agreement) or for a party’s Credit Support Provider, by virtue of a force majeure or an act of state in respect of an Early Termination Date. A Force Majeure Event is also triggered if the relevant event has made it impossible or impracticable for a party to perform.

Whether or not an event constitutes a force majeure is a matter of judicial interpretation. Consequently, the Force Majeure Working Group decided that it would be unhelpful to specify the types of events that would fall within the definition of force majeure and that it would be preferable to rely

instead on the interpretation of this term under established principles of English law and New York law as appropriate. The inclusion of acts of state in Section 5(b)(vi) is intended to address actions by sovereign states, such as a foreign invasion, that may not fall within the scope of Illegality.

The wording also provides that the impracticability of performance would be sufficient to constitute a Force Majeure Event. It is contemplated that certain events that would affect a party's ability to perform, such as the effect on a party's payment obligation of a disruption to the local settlement system resulting from a natural disaster, could be capable of being overcome (for example by physically delivering cash), although performance in such circumstances would be unreasonably onerous. It was therefore agreed that if performance of the relevant obligation would be impracticable, this would constitute a Force Majeure Event. A Force Majeure Event is only considered to occur if a party has used all reasonable efforts during the Waiting Period to overcome the event or circumstance.

E. Timing of Determination. The provisions discussed here are contained in Paragraphs (c) and (e) of the Force Majeure Provisions.

In the case of both Illegality and Force Majeure Event, the determination of whether or not it would be unlawful, impossible or impracticable for a party or Credit Support Provider to perform on a given day is made on the premise that performance of the relevant obligation is required on that day. In other words, the Illegality or Force Majeure Event occurs (subject to the Waiting Period) upon the occurrence of the relevant event, irrespective of whether payment or performance is actually due on that day.

The timing of this determination, whereby payment or performance is presumed to be due on the given day for the purposes of determining whether or not Illegality or Force Majeure Event has occurred, does not apply, however, in the case of a party's obligation to make a termination payment under Section 6(e) of the Master Agreement or a Credit Support Provider's obligation to make a payment in respect of a termination payment. There was some discussion of the implications of this approach for credit support arrangements where the Credit Support Provider's obligation was limited to making payments in respect of Section 6(e) termination payments. The concern here was that an Illegality or Force Majeure Event affecting only the Credit Support Provider's contingent payment obligation should not entitle the parties to terminate Transactions where Transactions have not otherwise been accelerated even though there was doubt over whether the Credit Support Provider would be able to perform.

F. Hierarchy of Events. The provisions discussed here are contained in Paragraph (f) of the Force Majeure Provisions.

If an event giving rise to an Illegality or a Force Majeure Event would also constitute an Event of Default by virtue of a failure to pay or deliver under Section 5(a)(i) (or to the extent that a failure to pay or deliver by a Credit Support Provider would give rise to an Event of Default under Section 5(a)(iii)), it will not constitute an Event of Default. The occurrence of an Illegality or Force Majeure Event would not, however, prejudice the parties' rights in relation to other Events of Default, such as the insolvency of the other party.

If the relevant event could give rise to both an Illegality and a Force Majeure Event, then it will constitute an Illegality and not a Force Majeure Event, thus enabling the parties to terminate Affected Transactions after expiration of the shorter Waiting Period applicable to Illegality.

G. Obligation to Give Notice. The provisions discussed here are contained in Paragraph (g) of the Force Majeure Provisions.

The present arrangement regarding the obligation of a party to provide notice upon the occurrence of a Termination Event under Section 6(b)(i) of the Master Agreement has been modified in relation to a Force Majeure Event. In respect of such an event, each party is under an obligation to use all reasonable efforts to notify the other party of the relevant event.

It is envisaged that following the occurrence of a Force Majeure Event such as a natural disaster, it may not be possible for the party affected by the relevant event to give notice to the other party setting out the details of the event. There was a concern in the Force Majeure Working Group that this may prejudice the other party's rights. It was agreed that this problem could be addressed by allowing both parties to give notice in respect of the relevant event. Please note, however, that the Waiting Period begins upon the occurrence of the Force Majeure Event, not upon the provision of notice.

H. Transfer to Avoid Termination Event. The provisions discussed here are contained in Paragraph (h) of the Force Majeure Provisions.

The obligation of an Affected Party in respect of a Termination Event to use all reasonable efforts to transfer its rights and obligations under Section 6(b)(ii) of the Master Agreement to another Office or Affiliate, as a condition to its right to designate an Early Termination Date, is amended so that it does not apply to Illegality. The Force Majeure Working Group was of the view that such a transfer is generally difficult to implement in practice. Being able to terminate Affected Transactions at an earlier point in time was generally agreed to be a better approach. For the same reasons, the transfer provisions of Section 6(b)(ii) of the Master Agreement have not been made applicable to Force Majeure Events.

I. Right of Termination following Illegality and Force Majeure Event. The provisions discussed here are contained in Paragraph (j) of the Force Majeure Provisions.

Following the occurrence of an Illegality or a Force Majeure Event, either party to the Master Agreement will have the right to terminate the Affected Transactions. The existing position under Section 6(b)(iv) of the Master Agreement is varied so that parties are not obligated to terminate all Affected Transactions in respect of the Illegality or Force Majeure Event, but will instead have the discretion to select the Affected Transactions to be terminated.

The principal rationale of this arrangement is that the Force Majeure Working Group envisaged that there would be situations where an indiscriminate termination of all Affected Transactions would be undesirable for both parties. The impact of an event on the economics of a Transaction may be different in every case, and would depend primarily on the term, pricing and underlying entity or asset of the particular transaction. For example, Transactions forming part of a structured scheme, such as swap transactions comprised in securitisation or repackaging structures may not be capable of being replaced at a commercially reasonable price and the economic burden of terminating such Transactions may outweigh the potential benefits of termination.

Under the Force Majeure Provisions, a party seeking to terminate Affected Transactions will be able to designate a day not earlier than two Local Business Days following the day on which such notice becomes effective as an Early Termination Date. In this situation, the other party would in any case have the right to terminate any or all other Affected Transactions on the same Early Termination Date if prior

notice is given. The Force Majeure Working Group agreed that this approach would be more appropriate and would discourage a party from electing to terminate only those Transactions that are in its favor since the other party could terminate the remaining Transactions.

An important exception to the general right of termination by the parties in respect of an Illegality or a Force Majeure Event is that an Affected Party would not have the initial right of termination in a situation where only its Credit Support Provider is affected by the relevant event. In this situation, the Affected Party would only be able to terminate any or all other Affected Transactions if the other party has initiated the process by electing to terminate some, but not all, of the Affected Transactions. The Force Majeure Working Group felt that it is only necessary for the non-Affected Party to determine the impact upon the credit support provided to it. However, to again discourage that party from electing to terminate only those Transactions that are in its favor, the Affected Party has been given the ability to terminate any or all other Affected Transactions where the non-Affected Party has chosen to terminate less than all the Transactions as a result of the Illegality or Force Majeure Event.

J. Deferral of Obligations. The provisions discussed here are contained in Paragraph (k) of the Force Majeure Provisions.

The Force Majeure Provisions provide, in a new Section 6(b)(v)(1), that any payment or delivery that would otherwise be required under an Affected Transaction during the Waiting Period will not be due until the first Local Business Day after the Waiting Period (at which point a right of termination would accrue) or the date on which the relevant event ceases to exist, if this occurs before the end of the Waiting Period.

Similarly, the Force Majeure Provisions provide, in a new Section 6(b)(v)(2), that the failure of a party to make a payment or delivery in respect of an Affected Transaction after the occurrence of an Illegality or a Force Majeure Event will not constitute an Event of Default under Section 5(a)(i) of the Master Agreement for so long as the event in question continues.

The new Section 6(b)(v)(3) is intended to cover not only Events of Default, but also Credit Event Upon Merger and Additional Termination Events where all Transactions are Terminated Transactions, as defined in the Master Agreement. The situation where all Transactions can be terminated are typically credit-related events, such that the designation of an Early Termination Date is likely to be the termination of the relationship between the parties. In this case, it was considered that a final accounting should occur to include the Section 6(e) amount owing as a result of an Illegality or a Force Majeure Event. This result is accomplished by treating such Section 6(e) amount as an Unpaid Amount.

The types of events referred to in the new Section 6(b)(v)(3) should be contrasted with events such as Tax Event or Tax Event Upon Merger where only the Affected Transactions can be terminated. For those types of events, the Section 6(e) amount owing as a result of an Illegality or a Force Majeure Event would not be treated as an Unpaid Amount even if all Transactions then outstanding are Affected Transactions.

K. Compensation for Deferral Payments and Deliveries. The provisions discussed here are contained in Paragraph (l) of the Force Majeure Provisions.

In respect of payments that would have been due under a Transaction during the Waiting Period for an Illegality or a Force Majeure Event, compensation will be at such current market rate for the applicable currency determined in good faith by the non-Affected Party, or, if there are two Affected

Parties, the average of the rates determined by each party in good faith. If one of the parties fails to determine a rate within two Local Business Days, the rate determined by the other party will prevail.

If a payment obligation, either under an Affected Transaction or in respect of a Section 6(e) payment, is not met following the end of the Waiting Period, the party that would otherwise be required to make such payment will compensate the other party at the Non-default Rate.

In respect of delivery obligations required to be performed during or subsequent to the relevant Waiting Period, compensation will be determined on the basis of any costs, losses or expenses resulting from the deferral or failure to deliver. An indemnity for loss may be a more appropriate basis of compensation for a failure to deliver than an interest payment.

L. Valuation of Terminated Transactions. The provisions discussed here are set out in Paragraph (m) of the Force Majeure Provisions.

For purposes of calculating the amount payable following termination of Affected Transactions as a result of an Illegality or a Force Majeure Event, the valuation mechanics are different from the standard approach used in respect of other Termination Events.

The parties may elect to include Alternative A or Alternative B in Paragraph (m) of the Force Majeure Provisions. If Attachment 8 (Section 6 and Related Amendments) has been selected by the parties in order to amend their Master Agreement, then Alternative A should be chosen. If Attachment 8 has not been selected by the parties, then Alternative B should be chosen.

Alternative A provides that in the event of an Early Termination Date resulting from a Termination Event where Market Quotation applies, in calculating the amount payable following termination of a Transaction due to an Illegality or Force Majeure Event, for the purpose of obtaining quotations for replacement transactions, Reference Market-makers will be asked to assume that the party requesting the quotations is a dealer of the highest credit standing in the relevant market, and no account will be taken of any existing Credit Support Document. The standard applied for this purpose is identical to the standard applied for the determination of a Reference Market-maker in the Master Agreement. Quotations will be obtained from dealers on a mid-market basis. The effect of this provision is that quotations obtained will reflect the economic characteristics of the particular Transaction and not the credit quality of the parties in question. Because valuation is at mid-market, any bid-offer spread will also be disregarded for the purpose of valuation.

Alternative B, which applies where the parties have opted to include the new concept of Replacement Value by selecting Attachment 8, provides for the same methodology, except that Reference Market-makers are not utilized, but rather the Determining Party uses mid-market values to determine the amount.

Under Alternative A, where Loss is the applicable payment measure, the same approach is reflected: any rates, prices or other quotations taken into the calculation of Loss should disregard the credit quality of the parties and valuation should be at mid-market. Loss is not considered under Alternative B since there is no need to fall back to Loss, unlike for Market Quotation.

4. *Set-Off.*

This provision discussed here is not contained in the Force Majeure Provisions.

Members of the Force Majeure Working Group considered whether to include in the Force Majeure Provisions a provision that would add a new Sub-paragraph to Section 6(d)(ii) of the Master Agreement as follows:

“Any amount payable by an Affected Party in respect of an Illegality or a Force Majeure Event which would otherwise be required to be made pursuant to Section 6(e) will, at the election of the other party, be set off, to the extent permitted by law, against any amount payable by that other party under this Agreement.”

The effect of this provision would have been expressly to provide that any amount payable under Section 6(e) of the Master Agreement as a result of the occurrence of an Illegality or a Force Majeure Event and payable by an Affected Party would be subject to set-off, to the extent permissible by law, against any amount payable by the other party under the Master Agreement at the election of that other party. A Section 6(e) payment, which related only to one office of a party and which could not be paid as a result of the occurrence of an Illegality or Force Majeure Event, could therefore be set off against payments under Section 2(a)(i) of the Master Agreement in respect of other on going Transactions entered into by the parties. While some felt that this may be particularly useful where the Section 6(e) payment cannot be made due to the existence of an Illegality or Force Majeure Event, others were concerned that it was overreaching, particularly in situations where the parties have otherwise attempted to “ring fence” the obligations of a particular office. To facilitate broad adoption of the Force Majeure Provisions, this provision has not been included in the standard form of Attachment to the Amendment, but may be used by parties on a bilateral basis if appropriate. Parties should also consider whether in such circumstances they would have contractual set-off rights under applicable law.

While this set-off provision has not been included in the Force Majeure Provisions, parties should note that Paragraph (k) of the Force Majeure Provisions does provide, as part of new Section 6(b)(v)(3), that Section 6(e) payments that a party fails to make due to the occurrence of an Illegality or Force Majeure Event may be treated as Unpaid Amounts in a subsequent close-out calculation arising as a result of the occurrence of an Event of Default, Credit Event Upon Merger or Additional Termination Event in which all outstanding Transactions are Affected Transactions.

5. *Section 10(a) Ring-Fencing Agreements.*

In addition to force majeure and impossibility issues, the Force Majeure Working Group also considered the application of Section 10(a) of the Master Agreement and certain related issues.

Some market participants have included provisions in their documentation (“Ring-fencing Provisions”) that provide that counterparties may not seek recourse to a head office in the event that the branch with which they transacted is unable to perform due to events such as exchange controls or expropriation.

ISDA is aware that member institutions may hold different views and adopt different practices in relation to Ring-fencing Provisions. ISDA acknowledges that these issues are ultimately a question of policy for each institution and that the resolution of such issues between industry participants is a matter for bilateral negotiation between the parties. ISDA does not take a position on these issues.

If a party considers it appropriate to include Ring-fencing Provisions in its documentation, or is presented with such a provision by its counterparty, the relevant issues that the party may wish to consider

include the types of risks and the obligations being ring-fenced, the scope of the Ring-fencing Provisions and their effect in the subsequent insolvency of the party seeking to ring fence.

In view of the legal issues raised by ring-fencing, best practice suggests that if one or both of the parties to a Master Agreement choose to ring-fence, they should address this issue by including an agreed provision either in the Schedule or in an amendment to a signed Master Agreement. ISDA wishes to emphasize that this suggested approach is not intended to call into question the legal effectiveness of a Ring-fencing Provision included in a Confirmation.

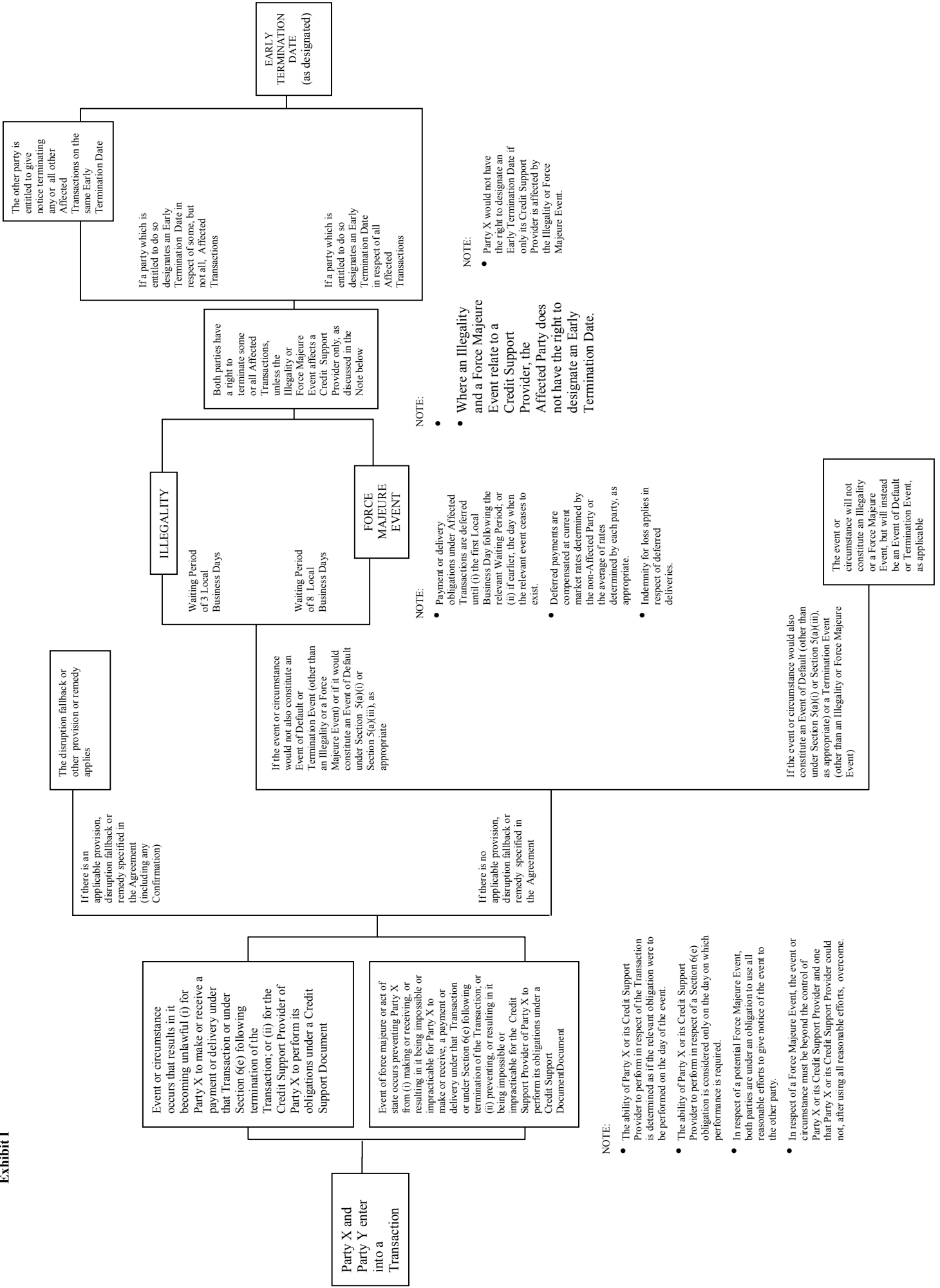
6. *Freely Transferable Funds.*

In light of the amendments to the Illegality provision, the Force Majeure Working Group also considered issues relating to exchange controls and other restrictions affecting the ability to deliver or transfer funds. In particular, there was some discussion of Section 2(a)(ii) of the Master Agreement.

Section 2(a)(ii) of the Master Agreement contains a requirement that payments under a Master Agreement should be made “in freely transferable funds”. There was some sentiment within the Force Majeure Working Group that, while this requirement was appropriate when the majority of payments under Transactions entered into under Master Agreements were in G-7 currencies, it was less obviously appropriate when Transactions were conducted in more restricted currencies. It was noted, for example, that the 1998 FX and Currency Option Definitions published by ISDA, EMTA and The Foreign Exchange Committee, addressed issues of transferability in some detail and that the 1999 Hungarian Forex Association Supplement to the ISDA Master Agreements also addressed this issue.

As part of the discussion with regard to preparing a new master agreement, consideration will be given to providing further clarification on the term “freely transferable funds”.

Exhibit I



NOTE:

- Payment or delivery obligations under Affected Transactions are deferred until (i) the first Local Business Day following the relevant Waiting Period; or (ii) if earlier, the day when the relevant event ceases to exist.
- Deferred payments are compensated at current market rates determined by the non-Affected Party or the average of rates determined by each party, as appropriate.
- Indemnity for loss applies in respect of deferred deliveries.

NOTE:

- Where an Illegality and a Force Majeure Event relate to a Credit Support Provider, the Affected Party does not have the right to designate an Early Termination Date.

NOTE:

- Party X would not have the right to designate an Early Termination Date if only its Credit Support Provider is affected by the Illegality or Force Majeure Event.

NOTE:

- The ability of Party X or its Credit Support Provider to perform in respect of the Transaction is determined as if the relevant obligation were to be performed on the day of the event.
- The ability of Party X or its Credit Support Provider to perform in respect of a Section 6(e) obligation is considered only on the day on which performance is required.
- In respect of a potential Force Majeure Event, both parties are under an obligation to use all reasonable efforts to give notice of the event to the other party.
- In respect of a Force Majeure Event, the event or circumstance must be beyond the control of Party X or its Credit Support Provider and one that Party X or its Credit Support Provider could not, after using all reasonable efforts, overcome.

The event or circumstance will not constitute an Illegality or a Force Majeure Event, but will instead be an Event of Default or Termination Event, as applicable

If the event or circumstance would also constitute an Event of Default (other than under Section 5(a)(i) or Section 5(a)(iii), as appropriate) or a Termination Event (other than an Illegality or Force Majeure Event)