



International Swaps and Derivatives Association, Inc.

ISDA has published two new documents, the “ISDA Non-ECP Guarantor Exclusionary Terms” (the “**ISDA Exclusionary Terms**”) and the “ISDA ECP Guarantor Keepwell Terms” (the “**ISDA Keepwell Terms**”) as part of the Dodd-Frank Documentation Initiative aimed at assisting the industry in implementing and complying with regulatory requirements imposed under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“**Dodd-Frank**”). ISDA is providing the Exclusionary Terms and the Keepwell Terms as tools that may easily be incorporated into transaction documentation to address issues that may arise in connection with the guaranty of swap obligations by third parties.

Background

In joint regulations issued last year by the Commodity Futures Trading Commission (“**CFTC**”) and the Securities and Exchange Commission further defining the terms “swap” and “security-based swap,”¹ the CFTC provided an interpretation to the effect that the guaranty of a swap (but not a security-based swap or a “mixed swap”) is an integral part of the guaranteed swap for purposes of the Commodity Exchange Act (“**CEA**”). Under Section 2(e) of the CEA as amended by Dodd-Frank, it is unlawful for any person other than an “eligible contract participant” (“**ECP**”) to enter into a swap unless the swap is entered into on, or subject to the rules of, a board of trade designated as a contract market under Section 5 of the CEA. In light of the CFTC’s interpretation of the term “swap,” the CFTC Office of the General Counsel (“**OGC**”) has interpreted CEA Section 2(e) as requiring that each guarantor of a swap (but not a security-based swap or a mixed swap) must be an ECP absent an exemption.²

Notwithstanding that the Products Adopting Release provided that the compliance date for the CFTC interpretation regarding the guarantees of swaps will be the effective date of rules that have yet to be proposed, OGC issued a time-limited no-action position regarding the application of CEA Sections 2(e) and 13(a) to guarantors and beneficiaries of a swap guaranty which ended on March 31.³ As a result, the guaranty of a swap by a non-ECP may raise

¹ Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement” Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 FR 48208 (Aug. 13, 2012) (“**Products Adopting Release**”).

² See, CFTC No-Action and Interpretation Letter No. 12-17 (October 12, 2012) (“**NAL 12-17**”).

³ See NAL 12-17 at p. 15.

significant issues for guarantors and swap counterparties, including whether the CFTC may take enforcement action against the parties and whether a guaranty may be found to be unenforceable. Additionally, depending on the agreements between the parties, an unlawful guaranty could trigger contractual breaches or events of default by a guaranteed party, and may have uncertain effects on collateral or other related contractual arrangements.

ISDA Exclusionary Terms and Keepwell Terms

Market participants may address these issues in a number of different ways, including conducting diligence to establish that swap guarantors are ECPs, use of ECP representations and ensuring that guarantees are drafted to exclude any guaranty of a swap obligation by a non-ECP. In addition, market participants are including “keepwells” in their guaranty arrangements pursuant to which certain transaction participants agree to provide financial support to guarantors who may not otherwise qualify as ECPs. These arrangements rely on a portion of the ECP definition provided in Section 1(a)(19)(A)(v) of the CEA, which states in relevant part that an ECP includes a corporation, partnership, proprietorship, organization, trust or other entity “the obligations of which under an agreement, contract, or transaction are guaranteed or otherwise supported by a letter of credit or keepwell, support, or other agreement” by persons that qualify as ECPs under certain other specified prongs of the ECP definition.⁴

The purpose of the ISDA Exclusionary Terms and the ISDA Keepwell Terms is to provide contractual terms that may be easily inserted into transaction documentation to address issues relating to guarantees by parties that may be non-ECPs. While ISDA does not endorse any particular method of addressing these issues, situations may arise where it is not feasible to conclusively establish the ECP status of each guarantor at all relevant times. For example, blanket guarantees provided in connection with master agreements or in connection with credit facilities that also may cover related swaps may raise practical issues in obtaining representations from all relevant guarantors at all appropriate times.⁵ Transaction facilities and master agreements that pre-date the effective date of the OGC interpretation but that provide for the execution of new guaranteed swaps at later times may also raise practical issues. For these situations, it may be useful to have pre-packaged terms that can easily be inserted into a variety of forms of documentation. The ISDA Exclusionary Terms and Keepwell Terms can be used individually or in combination for these situations.

⁴ In particular, corporate entities with total assets exceeding \$10,000,000 can confer ECP status to an eligible corporate entity under the terms of Section 1a(18)(A)(v). By a separate rulemaking, the CFTC established that a “commodity pool” is not eligible to qualify as an ECP under this section.

⁵ In this regard it is important to note that Section 2(e) of the CEA requires that a party is an ECP at the time that a swap is entered into. The time at which a guarantor is deemed to enter into a swap under the OGC’s interpretation may depend on whether the guaranty is executed before or after the swap, and blanket guarantees may require the guarantor to be an ECP at multiple times.

The ISDA Exclusionary Terms include agreements that provide that any guarantees that have been provided in connection with a transaction do not cover swap obligations to the extent that the relevant guarantor is not an ECP at the time of the execution of the guaranty or the swap (whichever is later). Because the OGC's interpretive position is explicitly limited to guarantees and excludes other credit support arrangements, the ISDA Exclusionary Terms are similarly limited to situations in which a person acts as guarantor or surety and do not include persons who provide collateral or other credit support in connection with a swap. The ISDA Exclusionary Terms are also drafted to exclude application to any guarantor that has represented in writing that it is an ECP as of the applicable date.

The ISDA Keepwell Terms provide basic keepwells that market participants may use in a variety of situations. The ISDA Keepwell Terms allow parties to specify which participants in a transaction will be the providers and recipients of keepwells, but also contain default elections for situations where such specification is not feasible or desirable. By default, each corporate entity that is a guarantor of swap obligations and has more than \$10,000,000 in total assets or that is otherwise eligible to confer ECP status provides a keepwell to each other guarantor of the same obligations that is not an ECP but is eligible under the express terms of the CEA or CFTC regulation to become an ECP through keepwell support.

The ISDA Exclusionary Terms and Keepwell Terms have been structured like ISDA product definitions and can be incorporated into documentation by reference in the same manner. As with product definitions published by ISDA, parties using the ISDA Exclusionary Terms and/or Keepwell Terms may adapt or supplement the standard provisions set out in these documents to reflect the specific terms of agreement between the parties for a particular transaction or group of transactions. *The precise documentation of each individual transaction remains the responsibility of the parties concerned, and ISDA does not assume any responsibility for any use to which the ISDA Exclusionary Terms and/or Keepwell Terms may be put, including their use in connection with any privately negotiated derivatives transaction. Each party to a transaction evidenced by documentation incorporating the ISDA Exclusionary Terms and/or ISDA Keepwell Terms must satisfy itself that they are appropriate for the transaction, have been properly used and/or adapted in that document and that the document has generally been properly drafted, in each case, to reflect the intentions of the parties.*