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M E M O R A N D U M

TO: Credit derivatives market participants

FROM: ISDA

DATE: September 23, 2008

RE: Deliverable Obligation Characteristics for North American Corporate Transaction Type

This memorandum sets out the standard Deliverable Obligation Characteristics for a credit derivative transaction that references a Reference Entity that is a North American Corporate, as documented in the ISDA Credit Derivatives Physical Settlement Matrix, the most recent version of which is dated September 22, 2008, together with the definitions of those Deliverable Obligation Characteristics taken from the 2003 ISDA Credit Derivatives Definitions as supplemented by the May 2003 Supplement to the 2003 ISDA Credit Derivatives Definitions (as so supplemented, the "**2003 Definitions**").

The purpose of this memorandum is to assist market participants that are considering which obligations may be Deliverable Obligations following the Credit Event in respect of Fannie Mae, Freddie Mac and Lehman Brothers Holdings, Inc. All provisions contained herein are copyright by International Swaps and Derivatives Association, Inc.

Deliverable Obligation Characteristics for North American Corporate Transaction Type

The following Deliverable Obligation Characteristics apply to standard Credit Derivative Transactions referencing North American Corporate entities:

- (1) Not Subordinated

LONDON

Telephone: 44 20 3088-3550
Facsimile: 44-20-3088-3555

HONG KONG

Telephone: 852-2200-5900
Facsimile: 852-2840-0105

SINGAPORE

Telephone: 65-6538-3879
Facsimile: 65-6538-6942

TOKYO

Telephone: 81-3-5733-5500
Facsimile: 81-3-5733-5501

BRUSSELS

Telephone: 32-2-401-8760
Facsimile: 32-2-401-6868

WASHINGTON

Telephone: 1-202-756-2980
Facsimile: 1-202-756-0271

- (2) Specified Currency: Standard Specified Currencies
- (3) Not Contingent
- (4) Assignable Loan^{1,2}
- (5) Consent Required Loan^{3,4}
- (6) Transferable⁵
- (7) Maximum Maturity: 30 years
- (8) Not Bearer⁶

Definitions of the above Deliverable Obligation Characteristics

The definitions of each of these Deliverable Obligation Characteristics, as published in the 2003 Definitions, are set forth below, in each case along with definitions of certain defined terms contained in each.

- (1) **"Not Subordinated"** means an obligation that is not Subordinated to (i) the most senior Reference Obligation in priority of payment or (ii) if no Reference Obligation is specified in the related Confirmation, any unsubordinated Borrowed Money obligation of the Reference Entity. For purposes of determining whether an obligation satisfies the "Not Subordinated" Obligation Characteristic or Deliverable Obligation Characteristic, the ranking in priority of payment of each Reference Obligation shall be determined as of the later of (1) the Trade Date specified in the related Confirmation and (2) the date on which such Reference Obligation was issued or incurred and shall not reflect any change to such ranking in priority of payment after such later date.
 - (a) **"Subordination"** means, with respect to an obligation (the **"Subordinated Obligation"**) and another obligation of the Reference Entity to which such obligation is being compared (the **"Senior Obligation"**), a contractual, trust or similar arrangement providing that (i) upon the liquidation, dissolution, reorganization or winding up of the Reference Entity, claims of the holders of the Senior Obligation will be satisfied prior to the claims of the holders of the Subordinated Obligation or (ii) the holders of the Subordinated Obligation will not be entitled to receive or retain payments in respect of their claims against the Reference Entity at any time that the Reference Entity is in payment arrears or is otherwise in default under the Senior Obligation. "Subordinated" will be construed accordingly. For purposes of determining whether Subordination exists or whether an obligation is Subordinated with respect to another obligation to which it is being compared, the existence of preferred creditors arising by operation of law or of collateral, credit support or other credit enhancement arrangements shall not be taken into account, except that, notwithstanding the foregoing, priorities arising by operation of law shall be taken into account where the Reference Entity is a Sovereign.
 - (b) **"Borrowed Money"** means any obligation (excluding an obligation under a revolving credit arrangement for which there are no outstanding, unpaid drawings in respect of

¹ Only applicable in respect of Loans

² If the relevant obligation satisfies Consent Required Loan, it need not satisfy Assignable Loan

³ Only applicable in respect of Loans

⁴ If the relevant obligation satisfies Assignable Loan, it need not satisfy Consent Required Loan

⁵ Only applicable in respect of obligations that are not Loans

⁶ Only applicable in respect of Bonds

principal) for the payment or repayment of borrowed money (which term shall include, without limitation, deposits and reimbursement obligations arising from drawings pursuant to letters of credit).

- (2) **"Specified Currency"** means an obligation that is payable in the currency or currencies specified as such in the related Confirmation (or, if Specified Currency is specified in a Confirmation and no currency is so specified, any of the lawful currencies of Canada, Japan, Switzerland, the United Kingdom and the United States of America and the euro and any successor currency to any of the aforementioned currencies, which currencies shall be referred to collectively in a Confirmation as the **"Standard Specified Currencies"**).

- (3) **"Not Contingent"** means any obligation having as of the Delivery Date and all times thereafter an outstanding principal balance [or, in the case of obligations that are not Borrowed Money, a Due and Payable Amount,]⁷ that pursuant to the terms of such obligation may not be reduced as a result of the occurrence or nonoccurrence of an event or circumstance (other than payment). A Convertible Obligation, an Exchangeable Obligation and an Accreting Obligation shall satisfy the Not Contingent Deliverable Obligation Characteristic if such Convertible Obligation, Exchangeable Obligation or Accreting Obligation otherwise meets the requirements of the preceding sentence so long as, in the case of a Convertible Obligation or an Exchangeable Obligation, the right (A) to convert or exchange such obligation or (B) to require the issuer to purchase or redeem such obligation (if the issuer has exercised or may exercise the right to pay the purchase or redemption price, in whole or in part, in Equity Securities) has not been exercised (or such exercise has been effectively rescinded) on or before the Delivery Date. If a Reference Obligation is a Convertible Obligation or an Exchangeable Obligation, then such Reference Obligation may be included as a Deliverable Obligation only if the rights referred to in clauses (A) and (B) of the preceding sentence have not been exercised (or such exercise has been effectively rescinded) on or before the Delivery Date.
 - (a) **"Convertible Obligation"** means any obligation that is convertible, in whole or in part, into Equity Securities solely at the option of holders of such obligation or a trustee or similar agent acting for the benefit only of holders of such obligation (or the cash equivalent thereof, whether the cash settlement option is that of the issuer or of (or for the benefit of) the holders of such obligation).

 - (b) **"Equity Securities"** means: (i) in the case of a Convertible Obligation, equity securities (including options and warrants) of the issuer of such obligation or depositary receipts representing those equity securities of the issuer of such obligation together with any other property distributed to or made available to holders of those equity securities from time to time; and (ii) in the case of an Exchangeable Obligation, equity securities (including options and warrants) of a person other than the issuer of such obligation or depositary receipts representing those equity securities of a person other than the issuer of such obligation together with any other property distributed to or made available to holders of those equity securities from time to time.

 - (c) **"Exchangeable Obligation"** means any obligation that is exchangeable, in whole or in part, for Equity Securities solely at the option of holders of such obligation or a trustee or

⁷ The reference to "Due and Payable Amount" is only relevant to obligations that are not "Borrowed Money" obligations. Standard terms for Credit Derivative Transactions referencing North American Corporate entities specify "Bond or Loan" as the Deliverable Obligation Category, therefore a Deliverable Obligations of a North American Corporate will be a "Borrowed Money" obligation.

similar agent acting for the benefit only of holders of such obligation (or the cash equivalent thereof, whether the cash settlement option is that of the issuer or of (or for the benefit of) the holders of such obligation).

- (d) **"Accreting Obligation"** means any obligation (including, without limitation, a Convertible Obligation or an Exchangeable Obligation), the terms of which expressly provide for an amount payable upon acceleration equal to the original issue price (whether or not equal to the face amount thereof) plus an additional amount or amounts (on account of original issue discount or other accruals of interest or principal not payable on a periodic basis) that will or may accrete, whether or not (A) payment of such additional amounts is subject to a contingency or determined by reference to a formula or index, or (B) periodic cash interest is also payable.
- (4) **"Assignable Loan"** means a Loan that is capable of being assigned or novated to, at a minimum, commercial banks or financial institutions (irrespective of their jurisdiction of organization) that are not then a lender or a member of the relevant lending syndicate, without the consent of the relevant Reference Entity or the guarantor, if any, of such Loan (or the consent of the applicable borrower if a Reference Entity is guaranteeing such Loan) or any agent.
 - (a) **"Loan"** means any obligation of a type included in the "Borrowed Money" Obligation Category that is documented by a term loan agreement, revolving loan agreement or other similar credit agreement and shall not include any other type of Borrowed Money.
- (5) **"Consent Required Loan"** means a Loan that is capable of being assigned or novated with the consent of the relevant Reference Entity or the guarantor, if any, of such Loan (or the consent of the relevant borrower if a Reference Entity is guaranteeing such Loan) or any agent.
- (6) **"Transferable"** means an obligation that is transferable to institutional investors without any contractual, statutory or regulatory restriction, provided that none of the following shall be considered contractual, statutory or regulatory restrictions: (i) contractual, statutory or regulatory restrictions that provide for eligibility for resale pursuant to Rule 144A or Regulation S promulgated under the United States Securities Act of 1933, as amended (and any contractual, statutory or regulatory restrictions promulgated under the laws of any jurisdiction having a similar effect in relation to the eligibility for resale of an obligation); or (ii) restrictions on permitted investments such as statutory or regulatory investment restrictions on insurance companies and pension funds.
- (7) **"Maximum Maturity"** means an obligation that has a remaining maturity from the Physical Settlement Date of not greater than the period specified in the related Confirmation.
- (8) **"Not Bearer"** means any obligation that is not a bearer instrument unless interests with respect to such bearer instrument are cleared via the Euroclear system, Clearstream International or any other internationally recognized clearing system.

The following terms are also relevant to determining whether an obligation of a North American Corporate entity may constitute a Deliverable Obligation:

- (9) **"Deliverable Obligation"** means, subject to Sections 2.32(a) and 2.33(a) [of the 2003 ISDA Credit Derivatives Definitions]: any obligation of a Reference Entity (either directly or as provider of a Qualifying Affiliate Guarantee [or, if All Guarantees is specified as applicable in the

related Confirmation, as provider of any Qualifying Guarantee]⁸) determined pursuant to the method described in Section 2.20 (but excluding any Excluded Deliverable Obligation) that (i) is payable in an amount equal to its outstanding principal balance [or Due and Payable Amount, as applicable,]⁹ (ii) is not subject to any counterclaim, defense (other than a counterclaim or defense based on the factors set forth in Section 4.1(a)-(d)) or right of set off by or of a Reference Entity or any applicable Underlying Obligor and (iii) in the case of a Qualifying Guarantee other than a Qualifying Affiliate Guarantee, is capable, at the Delivery Date, of immediate assertion or demand by or on behalf of the holder or holders against the Reference Entity for an amount at least equal to the outstanding principal balance [or Due and Payable Amount]¹⁰ being Delivered apart from the giving of any notice of nonpayment or similar procedural requirement, it being understood that acceleration of an Underlying Obligation shall not be considered a procedural requirement....

- (a) **"Qualifying Guarantee"** means an arrangement evidenced by a written instrument pursuant to which a Reference Entity irrevocably agrees (by guarantee of payment or equivalent legal arrangement) to pay all amounts due under an obligation (the **"Underlying Obligation"**) for which another party is the obligor (the **"Underlying Obligor"**). Qualifying Guarantees shall exclude any arrangement (i) structured as a surety bond, financial guarantee insurance policy, letter of credit or equivalent legal arrangement or (ii) pursuant to the terms of which the payment obligations of the Reference Entity can be discharged, reduced or otherwise altered or assigned (other than by operation of law) as a result of the occurrence or non-occurrence of an event or circumstance (other than payment). The benefit of a Qualifying Guarantee must be capable of being Delivered together with the Delivery of the Underlying Obligation.
 - (b) **"Qualifying Affiliate Guarantee"** means a Qualifying Guarantee provided by a Reference Entity in respect of an Underlying Obligation of a Downstream Affiliate of that Reference Entity.
 - (c) **"Excluded Deliverable Obligation"** means any obligation of a Reference Entity specified as such or of a type described in the related Confirmation.
 - (d) **"Downstream Affiliate"** means an entity whose outstanding Voting Shares were, at the date of issuance of the Qualifying Guarantee, more than 50% owned, directly or indirectly, by the Reference Entity.
 - (e) **"Voting Shares"** shall mean those shares or other interests that have the power to elect the board of directors or similar governing body of an entity.
- (10) In the event that Deliverable Obligation is a Qualifying Guarantee, the following will apply:
- (i) For purposes of the application of the Deliverable Obligation Category, the Qualifying Guarantee shall be deemed to satisfy the same category or categories as those that describe the Underlying Obligation.

⁸ Standard terms for Credit Derivative Transactions referencing North American Corporate entities do not specify "All Guarantees" as applicable, therefore any Deliverable Obligation that is a Qualifying Guarantee must also be a Qualifying Affiliate Guarantee.

⁹ See 7 above.

¹⁰ See 7 above.

- (ii) For purposes of the application of the Deliverable Obligation Characteristics, both the Qualifying Guarantee and the Underlying Obligation must satisfy on the relevant date each of the Deliverable Obligation Characteristics from the following list: Not Subordinated and Specified Currency.
- (iii) For purposes of the application of the Deliverable Obligation Characteristics, only the Underlying Obligation must satisfy on the relevant date each of the Deliverable Obligation Characteristics from the following list: Not Contingent, [Assignable Loan, Consent Required Loan,]¹¹ [Transferable,]¹² Maximum Maturity and [Not Bearer]¹³.
- (iv) For purposes of the application of the Deliverable Obligation Characteristics to an Underlying Obligation, references to the Reference Entity shall be deemed to refer to the Underlying Obligor.
- (v) The terms "outstanding principal balance" [and "Due and Payable Amount"]¹⁴ (as they are used in various other Sections [of the 2003 Credit Derivatives Definitions], including without limitation, Sections 9.8(a) and 9.8(g)), when used in connection with Qualifying Guarantees are to be interpreted to be the then "outstanding principal balance" [or "Due and Payable Amount", as applicable,]¹⁵ of the Underlying Obligation which is supported by a Qualifying Guarantee.

¹¹ Only applicable in respect of Loans

¹² Only applicable in respect of obligations that are not Loans.

¹³ Only applicable in respect of Bonds.

¹⁴ See 7 above.

¹⁵ See 7 above.