

ISDA®

Safe,
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Markets

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ISDA Documentation and Domestic Implementation

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Introduction to ISDA and its Documentation Architecture

Who is ISDA?

ISDA – International Swaps and Derivatives Association

Global trade association representing the leading institutions (dealers) and the leading end-users for OTC derivatives. Chartered in 1985, now 800 member institutions from 56 countries in six continents.

What are ISDA's main purposes?

- Provide a comprehensive standard documentation (New York or English law)
- Advocate and safeguard enforceability of ISDA master agreements worldwide
- Promote insolvency-proof close-out netting of transactions and collateral
- Contribute to compliance with regulatory requirements

What are ISDA's achievements?

Standard documentation

- 1992 / 2002 ISDA Master Agreement
- 2000 / 2006 ISDA Definitions
- Other Product Related Definitions:
 - 1998 FX and Currency Option Definitions
 - 2005 ISDA Commodity Definitions
 - etc.

Standard Documentation

- 1992 / 2002 ISDA Master Agreement
- Master Agreement terms Schedule (negotiation)
- Confirmation templates for every product
- Enforceability of ISDA master agreements
- Close-out netting of transactions and collateral
- Compliance with regulatory requirements

Standard collateral documentation

- 1994 ISDA Credit Support Annex (N.Y. Law), “CSA”
- 1995 ISDA Credit Support Annex (“transfer annex”, English Law), “CSA”
- 1995 ISDA Credit Support Deed (English Law)

Enforceability of ISDA master agreements and CSAs

ISDA provides for its members:

- Close-out netting legal opinions (by local lawyers) in more than 50 countries
- Collateral legal opinions (by local lawyers) in more than 40 countries
- Close-out netting of transactions and collateral
- Compliance with regulatory requirements

ISDA promotes legal certainty of close-out netting of transactions and collateral

- Cooperation with lawmakers to establish legal environment (laws, ordinances)
- ISDA Model Netting Law
- Support of UNIDROIT's initiative for harmonised substantive netting provisions

ISDA promotes legal certainty of close-out netting of transactions and collateral

- Support of UNIDROIT's "Geneva Intermediated Securities Convention" re: collateral
- Support of European Financial Markets Lawyers Group for an EU Netting Directive
- General enhancement of worldwide harmonisation of derivatives laws

ISDA enhances compliance with regulatory rules

- Promotes practices for the prudent and efficient development of OTC transactions
- Partner of national regulators (continuous exchange of views)
- Active participation in Consultation Processes

Major details of ISDA Master Agreement and Schedule

Master Agreement (“Three pillars”)

1. “Single agreement” (bundling of the OTC transactions into one legal agreement)
2. Obligations to pay or deliver conditional upon “no Event of Default , no Early Termination Date occurred”
3. Close-out netting (termination of all obligations under the master agreement and calculation of a single settlement amount by “netting”)

Major details of ISDA Master Agreement and Schedule

Schedule (negotiation between the parties)

- Elections, changes and additions of provisions which are not transaction-specific
- ISDA offers a wide range of elections, in particular the expansion of the termination provisions (additional termination event; termination events of Specified Entities relevant to the master agreement termination events etc.)

Major details of ISDA Master Agreement and Schedule

Schedule (negotiation between the parties)

Parties can agree on various other obligations in addition to the Master agreement's obligations; other documents may be required – the most important and controversial is the delivery of one or more legal opinion re: validity and enforceability of the specific master agreement signed by the parties.

Major details of ISDA Master Agreement and Schedule

Schedule (negotiation between the parties)

Legal opinion: This is not a netting or collateral opinion as provided by ISDA to its members. It usually deals with the power of a party to incur the obligations under the MA and the legality and enforceability of its terms, also in view of exchange control regulations and other public law provisions.

Major details of ISDA Master Agreement and Schedule

Schedule (negotiation between the parties)

Choice of law: English Law or Law of New York (not: domestic law)

Agent of process (domiciled either in New York or in London)

ISDA Credit Support Annex (“CSA”) English Law

Similar structure as the MA:

§§ 1-12 General provisions

Paragraph 11 Elections and Variables (negotiation) - Eligible Credit Support (“cash”, debt obligations, other i.e. Shares)

ISDA Credit Support Annex (“CSA”) English Law

Paragraph 11 Elections and Variables (negotiation)

- Independent Amount
- Threshold
- Minimum Transfer Amount
- Rounding

ISDA standardised Confirmations and Confirmation master agreements

ISDA has always advocated the use of standardised Confirmations

Templates have been added to the product specific Definitions

More recently, master confirmation agreements have been promoted to avoid a confirmation backlog which could entail serious problems (also from the supervisory/regulatory side)

Domestic Implementation of ISDA Documentation

Four possibilities:

1. Use of ISDA documentation (choice of English law) with non-binding, ISDA-sponsored translation (for ex. French, Japanese, Chinese, Greek)
 - Some sophisticated, internationally trading banks or end-users in Germany are going this way or consider it

Domestic Implementation of ISDA Documentation

2. Use of ISDA documentation (choice of English law) with non-binding, ISDA-sponsored translation (for ex. French, Japanese, Chinese) but:

simplification of Schedule – reduction of elections, changes and additions

Advantage: Negotiation process can be significantly shortened

Disadvantage: Documentation subject to foreign law

Domestic Implementation of ISDA Documentation

3. Use of ISDA documentation (choice of domestic law and language) with no significant or little changes of the wording

Examples: Poland, Russia, Greece

Advantage: ISDA's experience and the proven consistency of the wording

Disadvantage: Long text and certain clauses which are not common in the domestic legal system (i.e. representations)

Domestic Implementation of ISDA Documentation

4. Use of a domestic master agreement (subject to domestic law) strongly based on ISDA documentation in domestic language

Examples: France, Germany, Austria

Germany - [Rahmenvertrag für Finanztermingeschäfte = Master Agreement for Financial Derivatives published in 1993 as the little brother of the 1992 ISDA Master Agreement

Domestic Implementation of ISDA Documentation

Germany – **advantages** of domestic master agreement:

- acceptance by small local banks (savings banks and popular banks), use by medium sized enterprises, domestic legal departments able to understand and explain, wording in accordance with local law, no complicated private international law issues

Domestic Implementation of ISDA Documentation

Germany – **advantages** of domestic master agreement:

- no real “negotiation” of the master agreement no “overkill” (complicated provisions for rare cases)

however: solid legal basis necessary (laws, tradition of court decisions)

Domestic Implementation of ISDA Documentation

Germany – **disadvantages** of domestic master agreement:

- continuous need to adopt ISDA developments, need to adopt ISDA's product-specific definitions and their amendments, local law always behind up-to-date rules and provisions, close-out amount calculation method not detailed enough, leaving room for interpretation

Domestic Implementation of ISDA Documentation

Discussion: How to proceed in a country where many participants are not using complex financial contracts?

Twofold approach?

- ISDA MA for cross-border transactions
- simplified domestic MA based on ISDA



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For further information about the work of the ISDA Financial Law Reform Committee and the ISDA CEE/EMEA Committee, please contact Peter Werner in ISDA's EMEA Office in London.

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