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BY Email

The Hong Kong Financial Services and Treasury Bureau
Division 4, Financial Services Branch
Financial Services and the Treasury Bureau
15/F, Queensway Government Offices
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Dear Sirs,

Consultation Paper on the Review of Corporate Rescue Procedure

The International Swaps and Derivatives Association, Inc. ("ISDA") is pleased to submit this comment letter in response to the Consultation Paper on the Review of Corporate Rescue Procedure (the "Consultation Paper") published by the Financial Services and the Treasury Bureau ("FSTB") in October 2009.

ISDA is an international organisation whose membership comprises over 840 member institutions from 58 countries on six continents. These members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter ("OTC") derivatives to manage efficiently the financial market risks inherent in their core economic activities. As such, we believe that ISDA brings a unique and broad perspective, both in terms of the depth of representation across the derivatives industry and in terms of international representation and understanding of the regulatory arrangements in other jurisdictions.

1. Introduction

First and foremost, ISDA welcomes the policy objectives of the Hong Kong government in introducing a corporate rescue procedure which gives companies in financial difficulty the opportunity to try to survive as a going concern. In particular, ISDA is strongly supportive of the policy objectives of the provisions in the Companies (Corporate Rescue) Bill 2001 (the "2001 Bill") which exempt certain derivative contracts from the moratorium contained in the 2001 Bill. A party to a derivative contract in respect of whom a provisional supervisor has been appointed may well be in default under its derivative contract, either because the commencement of the

moratorium is treated as an insolvency event of default under the derivative contract or otherwise. ISDA acknowledges and agrees that the overriding policy concern supporting the different treatment of derivative contracts from other commercial transactions is the need to minimize systemic risk potentially arising from the insolvency or other default of a party to such contracts.

It is widely thought that systemic risk could be unacceptably high if market participants are unable to exercise contractual self-help remedies immediately upon the insolvency or other default of a counterparty to OTC derivative contracts. Such self-help remedies include the right to terminate, or close-out, all outstanding derivative contracts with the insolvent counterparty, net all payment obligations thereunder and foreclose on any collateral. Many OTC derivative transactions are entered into pursuant to a master agreement or other documentation, which provides for such self-help remedies. Following the termination of outstanding derivative transactions, the close-out amount, representing the lost value to one of the parties for terminating the transactions prior to their stated maturity, is calculated for each individual transaction. Such amounts are then netted against one another, so that a single net amount will be owed from one party to another. Netting arrangements, if enforceable, dramatically reduce the credit risks inherent in OTC derivative transactions, decreasing the risk that the insolvency of an institution could have systemic effects. Therefore, the importance of clarifying the enforceability of netting arrangements for OTC derivatives in the event of an insolvency cannot be overstated.

Derivatives contract values change over time and in response to changing market circumstances. Likewise, the market value of assets used as collateral are subject to volatility that may vary at different rates and in different directions from transaction values. If a solvent party cannot terminate its contract with an insolvent counterparty and simultaneously liquidate its collateral, the value of the contract and collateral may change substantially over the course of the insolvency proceeding, until the insolvent counterparty and the court decide the contract's fate. In the interim, the solvent party may replace or hedge the contract in its portfolio without knowing the economic impact of the court's decision will have on its portfolio. This is very different of course from a loan or similar debt obligation where the ultimate value at risk is known and certain, however uncertain the repayment. Without the derivatives contract exemption, this valuation and timing uncertainty would make substantial derivatives exposure untenable for a prudent party. Consistency, predictability and enhanced protection in the case of insolvency are extremely important in the derivatives market. Any uncertainty could lead institutions to withhold payments, which could also lead to reduced liquidity, impair the capital markets and lead to greater chance that a limited crisis will spread to other institutions and markets. Indeed, in the Legislative Council Brief to the 2001 Bill, it was noted that "to impose a moratorium on such contracts could involve unravelling innumerable other contracts which would cause chaos in the market concerned".

Although ISDA is pleased that the 2001 Bill makes progress towards clarifying and enhancing the validity of close-out, termination and netting provisions, ISDA is concerned that the proposals outlined in Section 11 of the 2001 Bill together with the list of contracts in Schedule 5 of the 2001 Bill may not be sufficiently comprehensive to prevent the very systemic risk which the 2001 Bill is trying to avoid. In particular, ISDA members are concerned that:

- The list of derivative contracts in Schedule 5 may not be representative of the derivative contracts which are currently available in the market and should be expanded.

- This list should be prospective and take into account future developments in the derivatives market.

- The exception which deals with set off in respect of master agreements should be further clarified.

- It is not clear whether cross-product set-off is permitted.

- Set-off should be allowed in respect of "title transfer" collateral arrangements.

- Exception to the moratorium should also be made to security and other collateral arrangements entered into in respect of derivative transactions.
- The exception to the moratorium which deals with guarantees should be clarified.

ISDA discussed the above issues in detail in a submission to the Bills Committee on the Companies (Corporate Rescue) Bill of the Legislative Council with a copy to FSTB on 6 February 2002 (the "2002 Submission"). Since the 2002 Submission, there have been some significant developments in relation to the OTC derivatives market and the ISDA documentation. Further, the list of the financial contracts exempted from the automatic stay contained in the United States Bankruptcy Code (the "US Code") [1] discussed in the 2002 Submission was expanded in 2005 and 2006 to further improve and clarify the netting process. As a result, we feel that it is necessary for us to re-examine the issues and highlight the latest developments in a new submission.

2. List of derivative transactions in Schedule 5

2.1 List of derivative contracts not representative of the market

The 2001 Bill provides that upon the appointment of the provisional supervisor, a proposed initial moratorium period of 45 days would apply that prohibits most creditors from enforcing their rights or taking actions (including any winding-up, exercise of set-off rights or enforcement of security) against the company. It is proposed that the moratorium period could be extended up to six months if approved by a meeting of creditors. Section 11(3) provides that contracts listed in Schedule 5 are, however, exempt from the application of this moratorium. Thus, the counterparty to a Schedule 5 derivative contract should be able to exercise contractual self-help including netting. ISDA supports the efforts of the draftsman of the 2001 Bill to provide, in Schedule 5, a comprehensive and flexible list of significant derivative transactions which reflects market practice. However, if this list approach is to be followed, ISDA believes that the list of derivative transactions in Schedule 5 of the Bill is not representative of all significant derivatives activities in the market. For example, this list does not include credit derivatives and bond option transactions and should include a wider range of commodity derivatives and a more comprehensive list of equity derivative transactions.

We believe that it is very important to define the scope of exempted transactions in a way that both provides the greatest amount of legal certainty as to scope but also is capable of accommodating continuing development and innovation in the financial markets. In the following sections, we will discuss how these exempted derivative transactions are defined under the ISDA Model Netting Act, the 2002 ISDA Master Agreement and the US Code. We believe that these examples can be used as a model to expand the list of derivative transactions in Schedule 5 of the 2001 Bill.

[1] 11 U.S.C. § 101 et seq. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, which was signed into law in April, 2005 (the "2005 Act"), amended the US Code and related statutes as of October 17, 2005. The Financial Netting Improvements Act of 2006, which was signed into law on December 12, 2006 (the "2006 Act"), builds on the 2005 Act to further improve and clarify the netting process for certain financial contracts through amendments to the US Code and related statutes. References in this paper to the US Code will be references to such laws as amended by the 2005 Act and/or the 2006 Act.

ISDA 2006 Model Netting Act

To date, ISDA has published three versions of Model Netting Act which is a model law intended to set out, by example, the basic principles necessary to ensure the enforceability of bilateral close-out netting as well as the enforceability of related financial collateral arrangements.[2] The ISDA Model Netting Acts have both been used successfully as models for netting legislation in a number of jurisdictions and as a guide for policy-makers and educators to the basic principles that should underlie a comprehensive statutory regime for close-out netting.

Section 1 of the 2006 MNA provides a definition of "qualified financial contract" which lists the various types of financial transaction that should ideally be covered. It also includes broad wording at the end of the definition intended to capture all types of financial transaction of a comparable nature in a way that is flexible enough to accommodate the development of new products. This avoids the need to introduce amending legislation periodically in order to keep pace with the markets, as has happened in a number of countries that introduce early netting statutes that were relatively restricted in scope.

We attach to this paper the text of the 2006 MNA and the Memorandum on the Implementation of Netting Legislation in Appendix A for your reference.

The United States Bankruptcy Code

Under the US Code, cases may be commenced either voluntarily by the debtor, or involuntarily by the debtor's creditors. As a general rule, the US Code offers two types of insolvency proceedings, one under Chapter 7 (liquidation) and one under Chapter 11 (reorganization). We understand that the corporate rescue procedure proposed under the 2001 Bill is comparable to the reorganization proceeding under Chapter 11 of the US Code, although the Hong Kong regime relies less on courts.

Section 362(a) of the US Code imposes the automatic stay at the moment a bankruptcy petition is filed. The automatic stay provides a period of time in which all judgments, collection activities, foreclosures, and repossessions of property are suspended and may not be pursued by the creditors on any debt or claim that arose before the filing of the bankruptcy petition.

Section 362(b)(17) of the US Code creates an exception to the scope of the automatic stay set forth in Section 362(a) of the US Code. This exception permits a swap participant or a financial participant to exercise any contractual rights under any security agreement or arrangement or other credit enhancement forming a part of or related to any swap agreement or exercise any contractual right to offset or net out any termination value, payment amount or other transfer obligation arising under or in connection with one or more such agreements, including any master agreement for such agreements. This permits netting of payment (or other property transfer) obligations at any time, including obligations arising after the filing of the bankruptcy petition. This provision also allows parties holding collateral or margin, or entitled to the benefits of a guarantee, to utilize such credit support, notwithstanding the bankruptcy filing.

Section 560 of the US Code preserves the contractual right of a swap participant or financial participant to liquidate, terminate or accelerate one or more "swap agreement[s]" and offset or net

[2] The three documents were published in 1996, 2002 and 2006 respectively. References in this paper to the Model Netting Act will be references to the one published in 2006 (the "2006 MNA").

out any termination or payment amounts owed under it based solely upon the insolvent party's bankruptcy filing.

Together, the protected rights under Section 362(b)(17) and Section 560 allow the solvent party to terminate the master agreement, net the value of terminated transactions, setoff mutual debts and claims, and exercise its remedies to foreclose against collateral. The solvent party's unsecured claim (after netting, set off and application of collateral) will be treated the same as other, non-swap unsecured claims and will be paid only at the same time as other, non-swap unsecured claims as determined by a bankruptcy court.

The definitions of "swap participant", "financial participant" and "swap agreement" in the US Code are set out for ease of reference in Appendix B. It is to be noted that the range of derivative contracts covered in the definition is much broader than that covered in the 2001 Bill.

Other safe-harbored transactions under the US Code include securities contracts, forward contracts, commodity contracts and repurchase agreements. The definitions of "securities contract", "forward contract", "commodity contract" and "repurchase agreement" are also set out for ease of reference in Appendix B.

The benefits provided by the swap safe harbor provisions are invaluable. The Office of the Comptroller of the Currency at the US Treasury calculates netting benefits as the percentage difference between gross positive exposures and gross negative exposures for US banks. As of September 30, 2009, US banks reported gross positive exposures of $4.7 trillion and netted exposures of $485 billion. In essence, 90% of the risk in derivative transactions has been eliminated through the benefits of netting. We estimate very roughly that US banks alone would need to raise $100 billion of new capital to support this additional exposure if netting were to be eliminated.

Definition of Specified Transaction under the 2002 ISDA Master Agreement

ISDA suggests that the definition of "Specified Transaction" used in the 2002 ISDA Master Agreement (Multicurrency-Cross Border) can also be used as a model to expand the list of derivative transactions in Schedule 5. This definition is set out for ease of reference in Appendix C and clause (i) of this definition contains a list of derivative transactions.

The definition of Specified Transaction in the 2002 ISDA Master Agreement was formulated as the result of a review and analysis of certain provisions of the 1992 ISDA Master Agreements which ISDA began undertaking in late 1999. 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.

2.2 Is the Schedule 5 list of derivative contracts sufficiently prospective and does it take into account future developments in the derivatives market?

Paragraph 10 of Schedule 5 states that set-off is permitted in respect of a "derivative, combination or option in respect of, or agreement similar to, an agreement or contract referred to in any of items 1 to 9". ISDA welcomes the policy intention of this approach, which is designed to provide flexibility so as to avoid the need to amend the definition as the nature and uses of derivatives transactions evolve.

However, ISDA believes that Paragraph 10 is not sufficiently clear-cut in its application and, for example, "or agreement similar to" may be construed more narrowly than intended. ISDA believes that the proposed definition should provide additional legal certainty by defining further this phrase, thus reducing legal risk.

In this respect, we note that section 1 of the 2006 MNA provides that “qualified financial contracts” include

“(x) any other agreement, contract or transaction similar to any agreement, contract or transaction referred to in paragraphs (a) to (w) with respect to one or more reference items or indices relating to (without limitation) interest rates, currencies, commodities, energy products, electricity, equities, weather, bonds and other debt instruments, precious metals, quantitative measures associated with an occurrence, extent of an occurrence, or contingency associated with a financial, commercial or economic consequence, or economic or financial indices or measures of economic or financial risk or value;

(y) any swap, forward, option, contract for differences or other derivative in respect of, or combination of, one or more agreements or contracts referred to in paragraphs (a) to (x).”

In addition to the use of generic language of the type reflected at the end of the definition of "qualified financial contract" in section 1 of the 2006 MNA, Part I section 2 of the 2006 MNA provides that the Central Bank of the relevant jurisdiction should be able to designate as "qualified financial contracts" any agreement or contract in addition to those already listed in the 2006 MNA. Where the Central Bank has this authority, it may use it in relation to a newly developed product, to enhance legal certainty in relation to that developing market. Such provisions would give more flexibility to the definition of the financial instrument to be covered by the netting legislation. However, local legislators should check whether this suggestion makes sense from a constitutional perspective under local law. If such an approach is not possible under the laws of Hong Kong, it is particularly important to make sure that the definition of financial instruments covers all types of instruments, currently existing or contemplated, which are supposed to be included in the netting legislation.

Again, ISDA believes the language set out in clause (ii) of the definition of Specified Transaction as set out in Appendix C can also be an appropriate model.

This refers to any transaction:

"which is a type of transaction that is similar to any transaction referred to in clause (i) that is currently, or in the future becomes, recurrently entered into in the financial markets (including terms and conditions incorporated by reference in such agreement) and which is a forward, swap, future, option or other derivative on one or more rates, currencies, commodities, equity securities or other equity instruments, debt securities or other debt instruments, or economic indices or measures of economic risk or value, or other benchmarks against which payments or deliveries are to be made (b) any combination of these transactions and……".

Thus, the list of Schedule 5 contracts firstly, will not be limited to those expressly named in Schedule 5 and, secondly, will be prospective, anticipating future developments in the derivatives market.

2.3 The exception to the moratorium which deals with set-off in respect of Master Agreements should be clarified

Paragraph 11 of Schedule 5 has the effect of allowing set-off in respect of master agreements for derivative transactions. ISDA welcomes this approach as protecting the right to net payment obligations across different categories of derivative contracts.

ISDA is of the view that it is not entirely clear whether, if parties were to use such master agreements to document non-derivative transactions, this would "taint" the right to set off in respect of derivative transactions which is preserved under the 2001 Bill. For example, assume a counterparty enters into a currency swap agreement, which is a Schedule 5 contract, and a weather derivative which is not. The ISDA Master Agreement provides that all transactions thereunder constitute "a single agreement". The question is whether this master agreement is a single protected currency swap agreement or a single potentially unprotected weather derivative agreement.

We note that section 4(i)(i) of the 2006 MNA expressly provides:

“a netting agreement shall be deemed to be a netting agreement notwithstanding the fact that such netting agreement may contain provisions relating to agreements, contracts or transactions that are not qualified financial contracts in terms of Part I section 1 of this Act, provided, however, that, for the purposes of this section, such netting agreement shall be deemed to be a netting agreement only with respect to those agreements, contracts or transactions that fall within the definition of "qualified financial contract" in Part I section 1 of this Act.”

For the sake of clarity, ISDA proposes that whether a master agreement is a Schedule 5 contract should be "without regard to whether the master agreement provides for an agreement or contract which is not an agreement or contract referred to in any of items 1 to [10]". This will make it clear that a master agreement within Schedule 5 will be treated as such even if it documents transactions that are not within Schedule 5.

2.4 Is cross-product netting permitted?

Schedule 5 lists derivative transactions in respect of which netting is permitted but is silent in respect of cross-product netting. For example, say Party A and Party B have entered into, between them, (i) a basis swap which is in-the-money to the value of $10 to Party A; and (ii) a floor transaction which is in-the-money to the value of $10 to Party B. Both transactions are terminated on the same date. The parties have not entered into a derivatives master agreement. It is unclear whether, under the 2001 Bill as currently drafted, both Party A and Party B would have to pay $10 to each other following close-out or whether the parties can set off both sums resulting in no net flow of money.

We note that section 561 of the US Code expressly provides that cross-product netting is permitted. Sub-section (a) provides:

“(a) Subject to subsection (b), the exercise of any contractual right, because of a condition of the kind specified in section 365(e)(1), to cause the termination, liquidation, or acceleration of or to offset or net termination values, payment amounts, or other transfer obligations arising under or in connection with one or more (or the termination, liquidation, or acceleration of one or more)—

(1) securities contracts, as defined in section 741(7);

(2) commodity contracts, as defined in section 761(4);

(3) forward contracts;

(4) repurchase agreements;

(5) swap agreements; or

(6) master netting agreements,

shall not be stayed, avoided, or otherwise limited by operation of any provision of this title or by any order of a court or administrative agency in any proceeding under this title."

2.5 Collateral

As previously mentioned, the parties to OTC derivative transactions often build in risk reduction techniques such as close-out and netting provisions. Collateralisation is another means of mitigating risk. There are two principal forms of collateral arrangement used in the OTC derivatives market; one based on the creation of a security interest (which will be discussed more fully below); the other based on title transfer.

Title Transfer

Under title transfer, the collateral giver transfers full title in securities and/or cash to the taker and grants the taker the right to set off on default of the collateral giver, the taker's net exposure to the collateral giver under the derivative transaction against the value of the transferred securities and/or cash. Under this approach, the collateral taker owns the collateral, without restriction, and the collateral giver, if it performs in full, is only entitled to the return of securities and/or repayment of cash in the same currency.

For example, take a derivative transaction between Party A and Party B, both of which are Hong Kong corporates. Party A gives collateral of $10 to Party B using the title transfer approach. Party A is put under a moratorium and an insolvency event of default thus occurs under the derivative transaction which allows Party B to close out the derivative transaction. If the derivative transaction is in-the-money to the value of $6 to Party A, the derivative contract will allow Party B to net this against the value of the collateral. Thus, Party B will only have an obligation to return $4 to Party A.

Credit enhancement by title transfer is an intrinsic part of the arrangements between the parties and a means of reducing credit risk. There is an argument that set-off in respect of such arrangements and derivative transactions between the parties is already permitted under the present drafting of the 2001 Bill. Paragraph 11 of Schedule 5 contemplates that set-off under master agreements between the parties is permitted. Title transfer arrangements are usually part of such a master agreement. However, as this conclusion is not beyond doubt, ISDA is of the view that set-off arising out of title transfer arrangements should be expressly permitted as part of Schedule 5.

Security interest

Derivative contracts are often collateralised to reduce exposure. Foreclosing on collateral is a self-help remedy as intrinsic to a derivative transaction as close-out and netting. The ability of a market participant to enforce a security interest to satisfy a claim against an insolvent counterparty

without delay is important not only to reduce credit risk, but also to maintain liquidity in the securities markets and prevent systemic risk. A stay against the liquidation of securities can result in uncertainty and the potential inability of a party to finance the securities it has purchased or that have been pledged to it, which could result in gridlock and a chain of insolvencies.

ISDA is of the view that the present drafting leaves room for uncertainty as to whether the protection for set-off rights in respect of Schedule 5 derivative contracts extends to the exercise of rights under related security arrangements. Indeed, during a moratorium, section 11(2)(d) of the 2001 Bill provides that no steps may be taken to enforce any security interest over the company's property. This seems to be out-of-step with the position in Canada and in the United States.

In Canada, the Bankruptcy and Insolvency Act (Canada) (which we understand, Schedule 5 is based on) allows secured creditors to enforce their security held against the debtor (which is subject to the stay) in accordance with any applicable security agreement and pursuant to relevant security legislation.

The definition of “qualified financial contract” in the 2006 MNA includes a “collateral arrangement” which is defined to mean, among others, “a pledge or any other form of security interest in collateral, whether possessory or non possessory” (see Appendix A).

The definition of “swap agreement” in the US Code also expressly includes "any security agreement or arrangement or other credit enhancement related to any agreements or transactions referred to in clause (i) through (v), including any guarantee or reimbursement obligation by or to a swap participant or financial participant in connection with any agreement or transaction referred to in any such clause…....”(see Appendix B).

To address this concern, ISDA believes that a carve-out should be made in the 2001 Bill to the prohibition of set-off during a moratorium to allow enforcement of security interests in respect of Schedule 5 derivative transactions.

Guarantees

Paragraph 12 of Schedule 5 allows set-off under guarantees for the listed derivative transactions and master agreements in respect thereof. As a guarantee, along with collateral and netting provisions, are part of the credit support structure of the parties to a derivative contract, ISDA welcomes such provisions. However, similar points can be made in respect of this Paragraph 12 of Schedule 5 as are set out in the section headed "Master Agreement" above. That is, it is unclear whether set-off in respect of a guarantee is permitted if the guarantee guarantees Schedule 5 contracts as well as non-Schedule 5 contracts.

2.6 Clarification requested

ISDA would be grateful if the FSTB would provide clarification of the following: Paragraph 9 of Schedule 5 refers to an agreement "to clear or settle securities transactions or futures contracts or to act as depository for securities". It is currently not clear what such agreements are and further clarification of the intention of this language would be welcome.

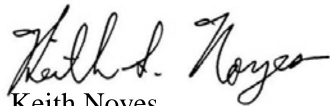
3. Conclusion

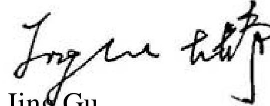
ISDA fully supports the objectives of the 2001 Bill in introducing a moratorium period in which companies in financial difficulty are given protection from creditors' actions. However, ISDA believes that it is important that any amendments to existing legislation reflect current market

practice related to the derivatives market and provide sufficient flexibility for future developments. ISDA strongly believes that the provisions in this bill represent a valuable opportunity to take tangible steps to mitigate systemic risk and improve the integrity of the financial system.

ISDA is grateful for the opportunity to comment on the Consultation Paper and would be pleased to discuss the issues addressed above in further detail or otherwise assist in any way that the FSTB deems appropriate.

Yours sincerely,





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International Swaps and Derivatives Association, Inc.

Appendix A

1. 2006 Model Netting Act

2. **2.** Memorandum on the Implementation on Netting Legislation

Appendix B

Swap Agreement

U.S.C. §101 (22A)

The term “financial participant” means

(A) an entity that, at the time it enters into a securities contract, commodity contract, swap agreement, repurchase agreement, or forward contract, or at the time of the date of the filing of the petition, has one or more agreements or transactions described in paragraph (1), (2), (3), (4), (5), or (6) of section 561 (a) with the debtor or any other entity (other than an affiliate) of a total gross dollar value of not less than $1,000,000,000 in notional or actual principal amount outstanding (aggregated across counterparties) at such time or on any day during the 15-month period preceding the date of the filing of the petition, or has gross mark-to-market positions of not less than $100,000,000 (aggregated across counterparties) in one or more such agreements or transactions with the debtor or any other entity (other than an affiliate) at such time or on any day during the 15-month period preceding the date of the filing of the petition; or

(B) a clearing organization (as defined in section 402 of the Federal Deposit Insurance Corporation Improvement Act of 1991).

(53B) The term "swap agreement"—

(A) means—

(i) any agreement, including the terms and conditions incorporated by reference in such agreement, which is—

(I) an interest rate swap, option, future, or forward agreement, including a rate floor, rate cap, rate collar, cross-currency rate swap, and basis swap;

(II) a spot, same day-tomorrow, tomorrow-next, forward, or other foreign exchange, precious metals, or other commodity agreement;

(III) a currency swap, option, future, or forward agreement;

(IV) an equity index or equity swap, option, future, or forward agreement;

(V) a debt index or debt swap, option, future, or forward agreement;

(VI) a total return, credit spread or credit swap, option, future, or forward agreement;

(VII) a commodity index or a commodity swap, option, future, or forward agreement;

(VIII) a weather swap, option, future, or forward agreement;

(IX) an emissions swap, option, future, or forward agreement; or

(X) an inflation swap, option, future, or forward agreement;

(ii) any agreement or transaction that is similar to any other agreement or transaction referred to in this paragraph and that—

(I) is of a type that has been, is presently, or in the future becomes, the subject of recurrent dealings in the swap or other derivatives markets (including terms and conditions incorporated by reference therein); and

(II) is a forward, swap, future, option, or spot transaction on one or more rates, currencies, commodities, equity securities, or other equity instruments, debt securities or other debt instruments, quantitative measures associated with an occurrence, extent of an occurrence, or contingency associated with a financial, commercial, or economic consequence, or economic or financial indices or measures of economic or financial risk or value;

(iii) any combination of agreements or transactions referred to in this subparagraph;

(iv) any option to enter into an agreement or transaction referred to in this subparagraph;

(v) a master agreement that provides for an agreement or transaction referred to in clause (i), (ii), (iii), or (iv), together with all supplements to any such master agreement, and without regard to whether the master agreement contains an agreement or transaction that is not a swap agreement under this paragraph, except that the master agreement shall be considered to be a swap agreement under this paragraph only with respect to each agreement or transaction under the master agreement that is referred to in clause (i), (ii), (iii), or (iv); or

(vi) any security agreement or arrangement or other credit enhancement related to any agreements or transactions referred to in clause (i) through (v), including any guarantee or reimbursement obligation by or to a swap participant or financial participant in connection with any agreement or transaction referred to in any such clause, but not to exceed the damages in connection with any such agreement or transaction, measured in accordance with Section 562;

(B) is applicable for purposes of this title only, and shall not be construed or applied so as to challenge or affect the characterization, definition, or treatment of any swap agreement under any other statute, regulation, or rule, including the Gramm-Leach-Bliley Act, the Legal Certainty for Bank Products Act of 2000, the securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934) and the Commodity Exchange Act.

(53C) The term "swap participant" means an entity that, at any time before the filing of the petition, has an outstanding swap agreement with the debtor.

§362 also exempts from the mandatory stay commodity contracts, forward contracts, securities contracts and repurchase contracts. For completeness, the definitions of such terms are set out below:

<u>Commodity contract</u>

U.S.C. §761(4)

"commodity contract" means—

(A) with respect to a futures commission merchant, contract for the purchase or sale of a commodity for future delivery on, or subject to the rules of, a contract market or board of trade;

(B) with respect to a foreign futures commission merchant, foreign future;

(C) with respect to a leverage transaction merchant, leverage transaction;

(D) with respect to a clearing organization, contract for the purchase or sale of a commodity for future delivery on, or subject to the rules of, a contract market or board of trade that is cleared by such clearing organization, or commodity option traded on, or subject to the rules of, a contract market or board of trade that is cleared by such clearing organization;

(E) with respect to a commodity options dealer, commodity option;

(F) any other agreement or transaction that is similar to an agreement or transaction referred to in this paragraph;

(G) any combination of the agreements or transactions referred to in this paragraph;

(H) any option to enter into an agreement or transaction referred to in this paragraph;

(I) a master agreement that provides for an agreement or transaction referred to in subparagraph (A), (B), (C), (D), (E), (F), (G), or (H), together with all supplements to such master agreement, without regard to whether the master agreement provides for an agreement or transaction that is not a commodity contract under this paragraph, except that the master agreement shall be considered to be a commodity contract under this paragraph only with respect to each agreement or transaction under the master agreement that is referred to in subparagraph (A), (B), (C), (D), (E), (F), (G), or (H); or

(J) any security agreement or arrangement or other credit enhancement related to any agreement or transaction referred to in this paragraph, including any guarantee or reimbursement obligation by or to a commodity broker or financial participant in connection with any agreement or transaction referred to in this paragraph, but not to exceed the damages in connection with any such agreement or transaction, measured in accordance with section 562;

Forward contract

U.S.C. §101(25)

"Forward contract" means

(A) a contract (other than a commodity contract, as defined in section 761) for the purchase, sale or transfer of a commodity, as defined in section 761(8) of this title, or any similar good, article, service, right or interest which is presently or in the future becomes the subject of dealing in the forward contract trade, or product or byproduct thereof, with a maturity date more than two days after the date the contract is entered into, including, but not limited to, a repurchase or reverse repurchase transaction (whether or not such repurchase or reverse repurchase transaction is a 'repurchase agreement', as defined in this section) consignment, lease, swap, hedge transaction, deposit, loan, option, allocated transaction, unallocated transaction, or any similar agreement;

(B) any combination of agreements or transactions referred to in subparagraphs (A) and (C);

(C) any option to enter into an agreement or transaction referred to in subparagraph (A) or (B);

(D)a master agreement that provides for an agreement or transaction referred to in subparagraph (A), (B) or (C), together with all supplements to any such master agreement, without regard to whether such master agreement provides for an agreement or transaction that is not a forward contract under this paragraph, except that such master agreement shall be considered to be a forward contract under this paragraph only with respect to each agreement or transaction under such master agreement that is referred to in subparagraph (A), (B) or (C); or

(E) any security agreement or arrangement, or other credit enhancement related to any agreement or transaction referred to in subparagraph (A), (B), (C) or (D), including any guarantee or reimbursement obligation by or to a forward contract merchant or financial participant in connection with any agreement or transaction referred to in any such subparagraph, but not to exceed the damages in connection with any such agreement or transaction, measured in accordance with section 562."

Securities contract

U.S.C. § 741(7)

"Securities contract"—

(A) means—:

"(i) a contract for the purchase, sale, or loan of a security [(as defined in 11 U.S.C. 101(49))], a certificate of deposit, a mortgage loan, any interest in a mortgage loan, a group or index of securities, certificates of deposit, or mortgage loans or interests therein (including an interest therein or based on the value thereof), or option on any of the foregoing, including any option to purchase or sell any such security, certificate of deposit, mortgage loan, interest, group or index, or option, and including any repurchase or reverse repurchase transaction on any such security, certificate of deposit, mortgage loan, interest, group or index, or option (whether or not such repurchase or reverse repurchase transaction is a "repurchase agreement" as defined in Section 101);

(ii) any option entered into on a national securities exchange relating to foreign currencies;

(iii) the guarantee (including by novation) by or to any securities clearing agency of a settlement of cash, securities, certificates of deposit, mortgage loans or interests therein, group or index of securities, or mortgage loans or interests therein (including any interest therein or based on the value thereof), or option on any of the foregoing, including an option to purchase or sell any such security, certificate of deposit, mortgage loan, interest, group or index, or option (whether or not such settlement is in connection with any agreement or transaction referred to in clauses (i) through (xi));

(iv) any margin loan;

(v) any extension of credit for the clearance or settlement of securities transactions;

(vi) any loan transaction coupled with a securities collar transaction, any prepaid forward securities transaction, or any total return swap transaction coupled with a securities sale transaction;

(vii) any other agreement or transaction that is similar to an agreement or transaction referred to in this subparagraph;

(viii) any combination of the agreements or transactions referred to in this subparagraph;

(ix) any option to enter into any agreement or transaction referred to in this subparagraph;

(x) a master agreement that provides for an agreement or transaction referred to in clause (i), (ii), (iii), (iv), (v), (vi), (vii), (viii), or (ix), together with all supplements to any such master agreement, without regard to whether the master agreement provides for an agreement or transaction that is not a securities contract under this subparagraph, except that such master agreement shall be considered to be a securities contract under this subparagraph only with respect to each agreement or transaction under such master agreement that is referred to in clause (i), (ii), (iii), (iv), (v), (vi), (vii), (viii), or (ix); or

(xi) any security agreement or arrangement or other credit enhancement related to any agreement or transaction referred to in this subparagraph, including any guarantee or reimbursement obligation by or to a stockbroker, securities clearing agency, financial institution, or financial participant in connection with any agreement or transaction referred to in this subparagraph, but not to exceed the damages in connection with any such agreement or transaction, measured in accordance with Section 562; and

(B) does not include any purchase, sale, or repurchase obligation under a participation in a commercial mortgage loan;

Repurchase agreement

U.S.C. §101(47)

The term "repurchase agreement" (which definition also applies to a reverse repurchase agreement)—

(A) means—

(i) an agreement, including related terms, which provides for the transfer of one or more certificates of deposit, mortgage related securities (as defined in section 3 of the Securities Exchange Act of 1934), mortgage loans, interests in mortgage related securities or mortgage loans, eligible bankers' acceptances, qualified foreign government securities (defined as a security that is a direct obligation of, or that is fully guaranteed by, the central government of a member of the Organization for Economic Cooperation and Development), or securities that are direct obligations of, or that are fully guaranteed by, the United States or any agency of the United States against the transfer of funds by the transferee of such certificates of deposit, eligible bankers' acceptances, securities, mortgage loans, or interests, with a simultaneous agreement by such transferee to transfer to the transferor thereof certificates of deposit, eligible bankers' acceptance, securities, mortgage loans, or interests of the kind described in this clause, at a date certain not later than 1 year after such transfer or on demand, against the transfer of funds;

(ii) any combination of agreements or transactions referred to in clauses (i) and (iii);

(iii) an option to enter into an agreement or transaction referred to in clause (i) or (ii);

(iv) a master agreement that provides for an agreement or transaction referred to in clause (i), (ii), or (iii), together with all supplements to any such master agreement, without regard to whether such master agreement provides for an agreement or transaction that is not a repurchase agreement under this paragraph, except that such master agreement shall be considered to be a repurchase agreement under this paragraph only with respect to each agreement or transaction under the master agreement that is referred to in clause (i), (ii), or (iii); or

(v) any security agreement or arrangement or other credit enhancement related to any agreement or transaction referred to in clause (i), (ii), (iii), or (iv), including any guarantee or reimbursement obligation by or to a repo participant or financial participant in connection with any agreement or transaction referred to in any such clause, but not to exceed the damages in connection with any such agreement or transaction, measured in accordance with section 562 of this title; and

(B) does not include a repurchase obligation under a participation in a commercial mortgage loan.

Appendix C

Definition of Specified Transaction in the 2002 ISDA Master Agreement

"Specified Transaction" means, subject to the Schedule, (a) any transaction (including an agreement with respect to any such transaction) now existing or hereafter entered into between one party to this Agreement (or any Credit Support Provider of such party or any applicable Specified Entity of such party) and the other party to this Agreement (or any Credit Support Provider of such other party or any applicable Specified Entity of such other party) which is not a Transaction under this Agreement but (i) which is a rate swap transaction, swap option, basis swap, forward rate transaction, commodity swap, commodity option, equity or equity index swap, equity or equity index option, bond option, interest rate option, foreign exchange transaction, cap transaction, floor transaction, collar transaction, currency swap transaction, cross-currency rate swap transaction, currency option, credit protection transaction, credit swap, credit default swap, credit default option, total return swap, credit spread transaction, repurchase transaction, reverse repurchase transaction, buy/sell-back transaction, securities lending transaction, weather index transaction or forward purchase or sale of a security, commodity or other financial instrument or interest (including any option with respect to any of these transactions) or (ii) which is a type of transaction that is similar to any transaction referred to in clause (i) above that is currently, or in the future becomes, recurrently entered into in the financial markets (including terms and conditions incorporated by reference in such agreement) and which is a forward, swap, future, option or other derivative on one or more rates, currencies, commodities, equity securities or other equity instruments, debt securities or other debt instruments, economic indices or measures of economic risk or value, or other benchmarks against which payments or deliveries are to be made, (b) any combination of these transactions and (c) any other transaction identified as a Specified Transaction in this Agreement or the relevant confirmation.