



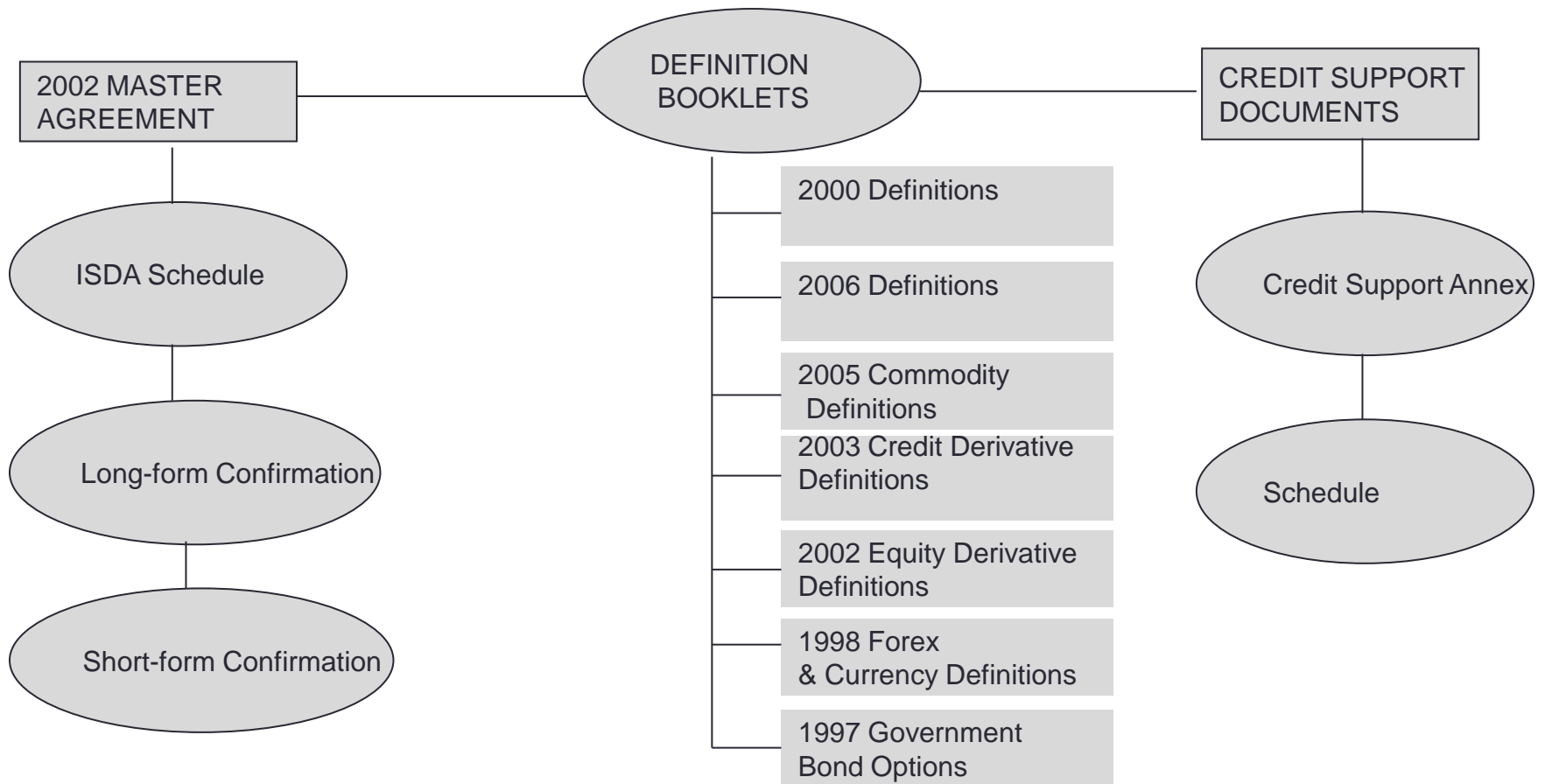
COLLATERAL MANAGEMENT LEGAL CONSIDERATIONS



COLLATERAL DOCUMENTATION ISDA AGREEMENTS

- Why ISDA Documentation
- ISDA Master vs Hedging Agreements
- ISDA Master v Long form confirmations
- Challenges with ISDA and Collateral management negotiation

ISDA AGREEMENTS STRUCTURE



REDUCING COUNTERPARTY RISK: NETTING AND SET OFF - ENFORCEABILITY

- ISDA Opinions

 - Capacity of Counterparty to enter into collateral arrangements

 - Insolvency laws and concurrent jurisdiction

 - Enforceability of foreign laws

 - Enforceability of post insolvency netting and set off

Common law- *concursum creditorum*

Section 35 A and Section 35B of the Insolvency Act

REDUCING COUNTERPARTY RISK: NETTING AND SET OFF - ENFORCEABILITY

- All unperformed obligations arising out of one or more **Master Agreements**
- Shall **upon sequestration** of the estate of a party to such Master Agreement
- **Terminate automatically** at the date of sequestration
- The values of those obligations shall be calculated at **market value** as at that date
- The values so calculated shall be **netted** and the **net amount shall be payable**

REDUCING COUNTERPARTY RISK: CLOSE OUT NETTING

- S 6(a) Where there is an event of default, the non-defaulting party has the right to designate an Early Termination Date for all outstanding transactions
 - Parties may elect in schedule whether
 - Early termination is applicable
- S 6 (b) where there is a termination event the affected party must inform other party of termination event (except Force Majeure)
- Party entitled to designate early termination differs

ISDA MASTER AGREEMENT

- Interpretation
- Section 1 (c) - single agreement
- Sections 2 (c) Netting- daylight risk, nothing to do with Close-Out Netting
 - Payments to be made net if they are in same currency with respect to the same transactions and same value date.
- Close-Out Netting

REDUCING COUNTERPARTY RISK: CLOSE OUT NETTING – EFFECT OF DESIGNATING EARLY TERMINATION

- All transaction are terminated (Except in case of Illegality, Force Majeure, Tax Event or Tax Event Upon Merger, where only affected transactions are terminated)
- Each party is no longer obliged to make payments or deliveries
- Obligation replaced by an Early Termination Amount payable.
- In 2002 Master the only payment method is now the Close-Out Amount.

REDUCING COUNTERPARTY RISK: CLOSE OUT NETTING THE CLOSE OUT AMOUNT

- Early Termination Amount = (Close Out Amount + Unpaid Amounts)
- Close Out Amount = Payment for the future value of transactions
- Unpaid Amounts = payments for obligations which became payable or deliverable prior to ETD
- Therefore
- $ETD = COM + \text{Unpaid amounts owed to Non Defaulting Party} - \text{Unpaid Amounts owed to Defaulting party}$

ISDA MASTER AGREEMENT

Events of Default



Failure to pay or deliver
Breach of agreement/repudiation
Credit Support default
Misrepresentation
Default under a Specified Transaction
Cross default
Bankruptcy
Merger without Assumption

TERMINATION EVENTS

- Illegality
- Tax Event
- Tax Event Upon Merger
- Credit Event Upon Merger
- Additional Termination Event



INTERNATIONAL DEVELOPMENTS

- The International Organisation of Securities Commissions (IOSCO)- aimed at improving standard of regulation applicable to the securities markets. Includes the 38 principles of Securities Regulation (IOSCO Principles)
- The Financial Sector Assessment Programme (FSAP), an IMF and World bank assessment of IOSCO members' compliance
- Group of 20 Recommendations

INTERNATIONAL DEVELOPMENTS

- The Rules and Recommendations of the International Institute for the Unification of Private and International Law (UNIDROIT) –aimed at improving laws around securities holding, transfer and collateralisation. South Africa made commitment to adopt UNIDROIT principles
- Foreign Account Tax Compliance Act;
- Dodd Frank Wall Street Reform Act
- Base 3 and Solvency II

NEW DEVELOPMENTS: SOUTH AFRICA

- Financial Markets Bill
- Companies Act
- Regulation 28
- Hedge Fund Regulation Proposed Framework

Collateral and the Financial Markets Bill

- Bill applies to unlisted as well as listed securities
- Inclusion of international markets players
- Extending status of self regulatory organisation to Clearing houses
- Investor protections
- Enables Central counterparty clearing
- Enables reporting to trade repository
- Primary and Secondary participants
- Segregated Depository Accounts
- Flagging of securities

Financial Markets Bill- Investor Protection

- ❑ Bill provisions on insolvency and settlement override any other law or contract excluding FICA
- ❑ The Registrar's approval must be sought before any other regulator or organ of state makes any decision that may affect the Bill or its provisions

ISDA SCHEDULE

- Specified Entities
- Specified Transaction- any agreements between the parties that fall outside the ISDA under negotiation
- Specified Indebtedness
- Cross Default – (threshold amount)
- Additional Termination Event
- Representations
- Early termination

REDUCING COUNTERPARTY RISK: CREDIT SUPPORT ANNEX -

- 1994 Credit Support Annex- New York Law
- 1995 Credit Support Deed (English Law)
 - Stand alone document; security interest
- 1995 Credit Support Annex (Eng Law) (Transfer)
- CSA- South African Version

REDUCING COUNTERPARTY RISK: GMSLA

Background and Development:

- Overseas Securities Lender's Agreement (OSLA) 1995
- Master Gilt Edged Stock Lending Agreement 1996
- Master Equity and Fixed Interest Stock Lending Agreement 1996

REDUCING COUNTERPARTY RISK AND GMSLA

The 2000 GMSLA was developed to produce one document that encompassed the above 3 documents; to internationalise the agreement;

- to take into account changes in market practices
- 2009 GMSLA developed to incorporate lessons from 2007/8 crisis
- 2010 GMSLA produced

GMSLA SOUTH AFRICAN SPECIFIC SCHEDULE ELECTIONS IN PARAGRAPH 13.

- Governing law and jurisdiction
- Insolvency issues- reference to our Companies Act 2008; Business Rescue proceedings,
- Cession *in securitatem debiti* of cash collateral shall be effected by:
 - The Borrower's deposit of cash collateral into an account opened with a bank and agreed upon by the parties

SOUTH AFRICAN SPECIFIC SCHEDULE ELECTIONS IN PARAGRAPH 13.

- A cession *in securitatem debiti* of uncertificated collateral securities to which the parties have agreed that statutory flagging does NOT apply shall be effected by transferring beneficial ownership;
- A cession *in securitatem debiti* of uncertificated collateral securities to which the parties have agreed that statutory flagging DOES apply shall be effected in accordance with section 43 of the Securities Services Act (See FMB)

MAIN CHANGES IN 2010 GMSLA

- Mini Close out
- Events of Default
- Manufactured payments
- Agency Annex

QUESTIONS AND DISCUSSION



Tel: +27 11 783 9390

Direct Tel: +27 11 057 5653

Mobile: +27 84 580 8005

Direct Fax: +27 86 692 8823

Email: michael@michaeldenenga.com

Physical Address: 87 2nd Street
Sandton, Johannesburg, 2196