COMPARISON BETWEEN EUROPEAN MASTER AGREEMENT (EMA) AND 2000 VERSION OF GLOBAL MASTER REPURCHASE AGREEMENT (GMRA)[1]

1. Comparisons between EMA and GMRA conducted by sponsors of EMA and GMRA

A Joint EBF/ISMA/TBMA Task Force on the EMA/GMRA has held a series of meetings and conference calls since January 2001 to examine the differences between the two agreements and consider whether any revisions to these agreements might be necessary in order to remove ‘basis’ risk resulting from technical differences between the two agreements. These discussions have been assisted by the efforts of three of the City of London’s leading law firms - Allen & Overy (acting for the EBF), Clifford Chance and Freshfields (acting for ISMA) - which have prepared detailed comparisons showing the differences between the terms of the EMA and the GMRA. A final statement by the Joint EBF/ISMA/TBMA Task Force on the EMA/GMRA arising out of this review process has not yet been formulated.

2. Single product vs. multi-product structures

The GMRA is a master repurchase agreement for what has traditionally been considered a single product line of financial transactions, namely repurchase and buy/sell back transactions. Cross-product netting with derivative and other financial transactions is therefore best accomplished under the GMRA through the usage of a master netting agreement, such as, for example, the February 2000 Cross-Product Master Agreement published by TBMA and a number of other market associations.

The EMA’s sponsors are in the process of developing the EMA as a multi-product agreement that would enable market participants to document under a single master agreement a variety of financial trading transactions, including derivatives. All financial transactions documented under the EMA are subject to the EMA’s General Provisions, which contain contractual provisions appropriate for all manner of financial trading transactions (e.g., repos, securities loans and derivatives), including clauses on purpose, structure and interpretation, operational details such as confirmations, payments and delivery procedures, taxes, representations, termination, close-out and calculation/payment of final settlement amounts, notices, booking

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offices, and miscellaneous matters. In addition, specific product annexes have been developed for particular financial transactions.

As presented, the EMA currently constitutes a master agreement for repurchase, buy/sell back and securities lending transactions, with repos and buy/sell backs documented under one product annex to the master agreement, securities lending transactions documented under a second product annex and margining provisions documented under a margin maintenance annex applicable to repos, buy/sell backs and securities lending.

A draft annex for derivative transactions has been under discussion for some time by the EMA drafting group. The EMA's drafters contemplate that only "plain vanilla" currency and interest rate swaps would be documented under the EMA (including the derivatives annex), whereas more complex derivative products could be documented by means of a 'bridge' construction with other market standard documentation (e.g., by incorporating the ISDA definitions into the terms of any derivative transactions documented under EMA). It is noted that the ISDA Definitions would need to be adapted in order to accommodate their usage with an underlying master agreement other than the ISDA Master Agreement (e.g., various cross-references in the ISDA Definitions would need to be changed). The EMA's sponsors have also considered an alternative approach to the documentation of derivatives under the EMA, namely a simple provision allowing the parties to incorporate the ISDA Definitions for the documentation of all derivative transactions, with the parties using the EMA as the underlying master agreement for close-out netting and other general purposes. Finally, it is noted that the EBF proposes to include within the EMA common margining provisions for the collateralisation on a net basis of all exposures arising under both repo and derivative transactions.[2]

Separate from the question of netting across different product lines documented under the EMA, the EMA also contains a set-off provision allowing the net exposure arising out of transactions documented under the EMA to be set off against transactions conducted outside the framework of the EMA. Thus, the EMA provides that the non-defaulting/terminating party may set off its obligation to pay the final amount due under the EMA following close-out against any actual or contingent claims which it has against a defaulting/ affected party on any legal grounds whatsoever (see EMA General Provisions § 7(4)). While this set-off

[2] It is noted that the practical usage of such a cross-collateralisation technique would necessitate systems changes at financial institutions.

provision is comparable to the basic set-off provision contained in the User's Guide to the 1992 ISDA Master Agreement,[3] it differs from the ISDA formula insofar as under the ISDA formala the non-defaulting/ terminating party has the option to set off an amount payable either by or to it against an amount payable either to or by it under any other agreement.

3. Single jurisdictional vs. multi-jurisdictional agreement

The GMRA is governed by English law and the parties submit to the jurisdiction of the English courts.

In order to accommodate its usage between parties located in both the same and different jurisdictions, the EMA has a strongly multi-jurisdictional character. The ISDA 1992 Master Agreement has a multi-jurisdictional character insofar as it is, based on the parties' choice, stated to be governed by either English or New York law and, depending on that choice, subject to the jurisdiction of the English courts or the non-exclusive jurisdiction of the New York state and federal (Manhattan) courts (see ISDA § 13). The EMA takes this multi-jurisdictional approach further, leaving it entirely to the parties to specify both the governing law (see EMA General Provisions § 11(1)) and the courts to whose non-exclusive jurisdiction they agree to submit (see EMA General Provisions § 11(2)). Failing any specification by the parties of the courts having jurisdiction, the parties submit to the non-exlusive jurisdiction of the courts having jurisdiction in the principal financial centre (or in the absence of a generally recognised financial centre, the capital city) of the country whose law governs the agreement (see EMA General Provisions § 11(2)).

Before using the EMA, the parties would need to consider specifying (a) the governing law to be used with counterparties in different jurisdictions and (b) the courts of the country/city whose law governs the agreement that would have exclusive or non-exclusive jurisdiction.

4. Single language vs. multi-lingual agreement

The GMRA is drawn up in the English language only. With the launch of the EMA, the sponsors of the GMRA have translated the GMRA's guidance notes into the French and German languages, but the agreement itself remains in the English language only.

[3] See User's Guide to the 1992 ISDA Master Agreements, p. 56 (1993 ed.).

A unique feature of the EMA is its multi-lingual character. While the original text of the EMA was drafted and published by its sponsors in the English language, versions in other European national languages, including French, German, Italian and Portuguese, have been agreed by the relevant national banking associations, while Greek and Spanish versions are currently under preparation.

5. Comparative review of the structures of GMRA and EMA

Consistent with its nature as a single-product agreement, the GMRA is a self-contained agreement into which the parties may incorporate supplemental terms and conditions, including standard-form Buy-Sell Back and Agency Transactions Annexes.

Consistent with its multi-product nature, the EMA contains a number of different documents that would be relevant to the conduct of repurchase transactions.

First, the EMA contains a standard-form set of ‘General Provisions’ applicable to all manner of financial trading transactions. Thus, the EMA’s General Provisions contain those provisions that are common to both master repo and master swap agreements used in cross-border financial markets (e.g., the GMRA, ISDA). These include provisions relating to such matters as confirmations, payments (including payment netting and late payments), deliveries, business day conventions/ definitions, the calculation of market values for securities, withholding and documentary taxes, standard form representations, events of default (including insolvency-related events and cross-defaults), termination due to an event of default or change of circumstances (e.g., changes in tax laws, illegality, impossibility), close-out netting/ set-off provisions and the calculation of final amounts due, notices, governing law and jurisdiction (including waiver of immunity) and miscellaneous matters (e.g., use of different booking offices, indemnification of expenses, telephone recording, termination or modification of the agreements, contractual currency, conduct of agency transactions and severability clause).

Second, the EMA contains a standard-form ‘Product Annex for Repurchase Transactions’. This product annex contains certain provisions specific to the conduct of repo and buy/sell back transactions that are typically found in a master repo agreement, including provisions relating to such matters as the basic mechanics of a repo transactions (e.g., the calculation of the repo price, the conduct of on-demand transactions, remedies for late deliveries of securities, the payment of manufactured dividends, substitution of securities, withholding taxes and tax credits, specific terms for buy/sell back transactions, repricing of transactions in lieu of margin transfers, corporate and other special events, distribution of income and subscription rights, consequential damages). The Product Annex for Repurchase Transactions also contains a suggested form of confirmation.

Third, the EMA contains a standard-form ‘Margin Maintenance Annex for Repurchase Transactions and Securities Loans’. This product annex contains streamlined provisions relating to margin maintenance for both repos and securities loans. These provisions are typically found in master repo and securities lending agreements, including provisions relating to the calculation and notification of net exposures, the transfer and return of margin, the provision of cash and securities margin and the establishment of margin thresholds.

Fourth, the EMA contains ‘Special Provisions’, which is the only contractual documentation that would need to be executed by parties conducting repo transactions under the EMA. The Special Provisions would incorporate the General Provisions, the Product Annex for Repurchase Transactions, the Margin Maintenance Annex for Repurchase Transactions and Securities Loans and other annexes which the parties agree to incorporate (e.g., an annex containing standard form provisions relating to the conduct of transactions in a particular market such as, for example, the ‘JGB’ Japanese Government bond market). The Special Provisions would also set forth the addresses for notices and other communications between the parties, the provisions relating to governing law and jurisdiction and other provisions amending or supplementing the standard-form provisions contained in the General Provisions, the Product Annex for Repurchase Transactions and the Margin Maintenance Annex for Repurchase Transactions and Securities Loans. In particular, the parties would use the Special Provisions to make any elections and amendments contemplated in particular provisions of the General Provisions and the standard form annexes, including:

- the application of payment netting,
- the interest surcharge for late payments,
- the price sources for determining the market value of securities,
- the application of certain provisions to a party’s guarantor and any guarantee provided by such guarantor,
- the application of the event of default ‘default under specified transactions’ and ‘cross-default’ to either or both parties and/or above specified default thresholds for the cross-default,

- the identification of which jurisdictions' insolvency proceedings may trigger a close-out with respect to a party,
- the applicable grace period within which the commencement of insolvency proceedings must be dismissed or stayed before a party may close out,
- the extent to which certain insolvency-related events of default trigger an automatic close-out with respect to a party,
- whether an 'impossibility' event (e.g., catastrophe, armed conflict, act of terrorism, riot or other circumstances beyond the party's reasonable control) may trigger a close-out,
- the identification of the base currency for the calculation of the net close-out amount due, the electronic messaging systems agreed by the parties for making notices to each other,
- the identification of booking offices through which transactions will be booked by the parties,
- the types of tax documents and certificates required to be provided by a party,
- a party's process agent(s) (if any),
- the identification of booking offices (e.g., all booking offices in the aggregate or particular booking offices of either or both parties) and/or transactions and groups of transactions (e.g., the aggregate or only some of all repo transactions and/or securities loans in some or all currencies) to be covered for the purposes of calculating net exposures for margin maintenance purposes,
- the identification of eligible currencies for cash margin,
- the interest payable on cash margin, party by party,
- the identification of eligible securities for securities margin, party by party,
- the valuation percentage (e.g., 102%) applicable to cash and securities margin, party by party,
- the designation of a calculation agent (if any) for margin maintenance purposes, and
- the identification of the valuation procedures applicable for margin maintenance purposes (e.g., the valuation date and time, margin triggers, margin transfer deadline).

6. Hierarchy

The EMA establishes the following hierarchy in the event of conflict between the different parts of the EMA: first, the terms of a transaction (the confirmation) prevail, in relation to that transaction only; second, the EMA Special Provisions; third, any Annexes incorporated in the EMA Special Provisions; and fourth, the EMA General Provisions (see EMA General Provisions, § 1(3)). There is no corresponding express hierarchy of interpretation in the event of inconsistency between different parts of the GMRA, although an English court would probably follow the same hierarchy expressed in the EMA.

7. ‘Single agreement’ concept

Both the EMA and the GMRA contain ‘single agreement’ clauses, confirming that the master agreement gives rise to a single contractual relationship and that each transaction is entered into in consideration of all other transactions under the agreement (see EMA § 1(4), GMRA § 13). The purpose of these clauses is to strengthen close-out netting under the master agreements and to prevent ‘cherry-picking’ by an insolvency official since netting statutes in many jurisdictions require the use of a master netting agreement based on the single agreement concept.

8. Transactions in different currencies

The GMRA is envisaged as a master agreement for the conduct of repo transactions denominated in any currency (see GMRA, §§ 2(e)(iv), 6(a), 7, 10(c)(2)), including U.S. Treasury instruments (without significant amendment to the GMRA)[4] and JPY-denominated instruments with respects to which the GMRA’s sponsors are in the process of preparing a special annex. The EMA is similarly conceived as a master agreement covering financial transactions in different currencies (see EMA General Provisions, §§ 3(1), 3(7), 7(1)(b), 7(4), 10(8)).

The development of an integrated euro-denominated repo market in the euro zone provided the main catalyst for the development of the EMA, and it may therefore be expected that the EMA will be primarily used by euro zone counterparties participating in the euro-denominated repo markets.

9. Term and on-demand transactions

The GMRA permits both term and on-demand transactions, and in the case of on-demand transactions, the demand for termination must be made by telephone or otherwise and termination must occur after not less than the minimum period customarily required for the settlement/delivery of the money/securities in question (see GMRA § 3(d), (e)).

[4] Letter of August 7, 1997 from Thomas B. Hunziker, General Counsel, International Securities Market Association, to the members of the Association re ‘Promotion of the PSA/ISMA Global Master Repurchase Agreement (GMRA) in various jurisdictions and markets’, 5.

While the EMA also permits transactions terminable on demand, (1) the demand for termination is to be made in a demand notice sent by either party to the other, implying that the demand for termination is to be made in writing, and the notice shall only take effect after not less than the minimum period customarily required for the settlement or delivery of the money/securities in question, and (2) in the absence of a demand notice the transaction will automatically terminate 364 days after the purchase date (see EMA Product Annex for Repos, § 2(4)).

It is understood that the 364-day cut-off period has been included because under German and French law there may be a degree of uncertainty as to whether insolvency netting can be applied to undated transactions. Concern has been expressed market participants in the Joint EBF/ISMA/TBMA Task Force that parties who include the 364-day cut-off period would need an operational mechanism to identify any trades in danger of termination. It has been proposed to the EBF that the 364-day period (which was chosen arbitrarily on the basis that it was sufficiently long as to render it unlikely that the termination clause would ever be triggered) be extended to two years, and consideration has also been given to whether (a) similar standard language should be drafted for inclusion in the GMRA for counterparties who feel such a provision is necessary and (b) the EMA could/should be modified to render this clause optional and/or to agree that the transaction be automatically terminated and re-opened for those counterparties who want to avoid being left with an unexpected position on automatic termination.

10. Margin calls

Each of the GMRA and the EMA contain provisions facilitating margin calls in the event a net exposure arises during the life of a repo transaction (see GMRA § 4; EMA Margin Maintenance Annex). The following represents a summary of the main points of contrast between the GMRA and the EMA in this respect.

- Under the GMRA initial margins and transaction exposures for the calculation of margin calls throughout the life of a transaction are defined by reference to (a) the repo price multiplied by a ‘margin ratio’ (i.e., the market value of the securities at the time the transaction was entered into divided by the purchase price), or such other proportion as the parties may agree, and (b) the market value of any securities and margin securities, together with cash margin, including accrued interest thereon (see GMRA §§ 2(z), (ee), (ww), 4(a), (c)). Under the EMA initial margins and net exposures in repo transactions are calculated by reference to the aggregate of (a) the repo price multiplied by a ‘margin ratio’ (defined in a similar manner as above) and (b) the market value of any securities and margin securities, together with the nominal amount of any cash margin, in each case multiplied by any applicable valuation percentage agreed by the parties (see EMA Margin Maintenance Annex §§ 1(1), 1(3)).

- Under the GMRA, unless the parties specify otherwise, net exposures triggering margin calls are calculated by reference to all the parties' transaction exposures plus amounts payable to each other (see GMRA § 4(c)). The EMA determines net exposures by reference to (a) all repo and securities lending transactions, (b) specified groups of transactions or (c) each individual transaction, as agreed by the parties, and failing such agreement by reference to all repos and all securities loans, each forming a separate group of transactions (see EMA Margin Maintenance Annex § 1(1)).

- While the GMRA contains no provisions regarding margin triggers, necessitating the specification of such triggers by the parties in the annex to the GMRA, the EMA contains provisions referring to margin triggers, providing that margin transfers would only take place (a) to the extent that the net exposure exceeds the exposure threshold agreed by the parties or (b) if the market value of the margin to be transferred exceeds the minimum transfer amount agreed by the parties, failing which agreement the exposure threshold and/or minimum transfer amount is zero (see EMA Margin Maintenance Annex § 2(6)).

- While the GMRA does not specify who should make the calculation of net transaction exposures triggering margin calls (thereby leaving it to each party to make its own calculations), the EMA provides for the designation of a third party calculation agent, failing which each party makes the necessary calculations for itself and if the two parties' calculations of net transaction exposures differ, the net exposure "shall be one-half of the difference of the amounts so calculated by both parties" (see EMA Margin Maintenance Annex § 1(2), (3)). Two drafting points are noted. First, in order to avoid the consequences of a literal interpretation of this clause which might result in a lower net exposure than was intended by the EMA's drafters, it is suggested to amend this clause in the EMA Special Provisions so as to provide that if the parties' calculations of net exposure differ from each other, the net exposure "shall be the average of the amounts so calculated by both parties". Second, all calculations for margin calls are required to be made in the base currency, and amounts not denominated in the base currency are required to be converted into the base currency at the applicable exchange rate.

- Under both the GMRA and the EMA, notice of margin calls may be given orally or in writing (see GMRA §4(b); EMA Margin Maintenance Annex §1(1)).

- Under both the GMRA and the EMA the composition of the margin to be transferred (e.g., cash and/or securities) is, in general, at the option of the party making the margin transfer, with the parties free to set out categories of eligible cash and securities typically accepted as margin by the parties (see GMRA § 4(d), (e), EMA Margin Maintenance Annex § 2(3), (4), (5)). Under the EMA, margin securities are also deemed acceptable where the securities have an original maturity of not more than 5 years and are issued by the central government of the country in which the margin recipient has its principal office or in which it is organised, incorporated or resident (see EMA Margin Maintenance Annex § 2(5)).

- While the GMRA allows either party to make a margin call "at any time", thereby covering the possibility of intra-day margin calls (see GMRA § 4(a)), the EMA provides for the calculation of net exposures on each "date" agreed by the parties or failing such agreement on "each business day" by "11 a.m., Brussels time", apparently excluding the possibility of intra-day calls (see EMA Margin Maintenance Annex § 1(2), (3)).

- Under the GMRA cash and securities margin is required to be paid or delivered within the minimum period specified by the parties or, failing such specification, the minimum period customarily required for the settlement or delivery of the relevant kind of money/ securities (see GMRA § 4(g)), with the result that in the case of securities where same-day delivery is possible the delivery would have been on a same-day basis unless otherwise agreed. Under the EMA margin is required to be transferred no later than the date agreed, and failing such agreement cash margin is required to be transferred "promptly" and securities margin to be transferred on the next business day "if practicable" (see EMA Margin Maintenance Annex § 2(2)), with the result that securities margin would not be required to be delivered on a same-day basis unless the parties agreed otherwise.

- Both the GMRA and the EMA provide that the payment of cash margin gives rise to an interest-bearing debt owing from the party receiving the cash margin to the party making the cash payment (see GMRA § 4(f); EMA Margin Maintenance Annex § 2(4)). While the GMRA requires the parties to specify the interest rate applicable to cash margin in each currency (see GMRA Annex 1 §1(i)), the EMA provides for a fall-back rate in the absence of any agreement by the parties, with cash margin bearing interest at the inter-bank offered interest rate charged by prime banks to each other for overnight deposits at the relevant place/in the relevant currency less 0.10% per annum (see EMA Margin Maintenance Annex § 2(4)).

11. Securities/margin substitutions

Substitutions under both the GMRA and the EMA may only be accomplished by one party with the consent of the other party, except that in the case of margin securities under the EMA the consent of a margin recipient is not required for a substitution by a margin provider of new eligible margin securities (see GMRA § 8; EMA Product Annex for Repos § 3, EMA Margin Maintenance Annex § 3).

Additional provisions requiring substitutions for accounting reasons (for instance, to keep assets off-balance sheet under, e.g., FASB 125 [which provision no longer appears relevant to market participants]) would necessitate additional wording under both agreements.

12. Price sources for securities

Under the EMA and the GMRA the market value of securities is similarly defined insofar as both the EMA and the GMRA refer to the generally recognised price sources agreed to by the parties (see GMRA § 2(y); EMA General Provisions § 3(8)). However, the EMA is more expansive in that it contains a fall-back formula for the valuation of securities in the unlikely events that the parties either fail to agree on price sources or that price sources fail to quote prices, in which case the market value of the securities would be (i) the last quoted price in the case of securities listed on a stock exchange; (ii) in the case of unlisted securities, the last price published by a central bank or other entity of undisputed authority on the main market on which the securities are traded; and (iii) in any other case, the average of the bid and offer prices for the securities established by two leading market participants other than the parties (see EMA General Provisions § 3(8)).

13. Payment and delivery netting

The GMRA provides for automatic payment netting with respect to all amounts payable in the same currency with respect to repo transactions outstanding between the parties (see GMRA § 6(h)) and for delivery netting, requiring a single calculation of a net quantity of securities transferable by one party to the other (see GMRA § 6(i)).

The EMA only provides for automatic payment netting with respect to payments in the same currency and in respect of the same transaction, and provides for optional additional payment netting where the parties so agree in respect of two or more transactions, or in respect of one type of transaction (e.g., repos), or in respect of more than one type of transaction (e.g., repos and, when a product annex is available, swaps) or in respect of mutual obligations to deliver assets which are fungible with each other. The EMA also facilitates delivery netting, providing that the parties may agree that the principle of payment netting shall also apply in respect of mutual obligations to deliver assets which are fungible with each other (see EMA General Provisions (§ 3(4)).

14. Tax gross-ups; tax forms

Under the GMRA, in the event that a withholding or deduction of taxes is required by law, the paying party is required to pay such additional amounts as will result in the net amounts received by the other party being equal to such amounts as would have been received by it had no such taxes been withheld or deducted (see GMRA § 6(b)), with the result that the payment is subject to a ‘gross-up’.

By contrast, under the EMA if a party is obliged to deduct or withhold taxes from a payment, it is not required to pay the other party the additional amounts necessary to ensure that the other party receives the full amount which it would have been entitled where (a) the tax is imposed by the jurisdiction in which the payee is located (or pursuant to a treaty to which such jurisdiction is party) or (b) because the payee has failed to provide any tax certificate or document requested of it (see EMA General Provisions § 4(1)). Thus, under the EMA, consistent with the ISDA Master Agreement, there is no obligation to gross up where taxes are imposed by the payee’s jurisdiction, thereby avoiding, in the repo context, that parties become involved (possibly inadvertently) in coupon-washing. Also, under the EMA, each party is liable for the payment of any stamp, documentary or similar taxes imposed by the jurisdiction in which it is located (see EMA General Provisions § 4(2)). Market participants are examining this issue closely, particularly having regard to the implications of this distinction for equity repo markets.

Similar to the ISDA Master Agreement (see ISDA § 4(a)), the EMA contains a provision - for which there is no corresponding provision in the GMRA - requiring a party to make available to the other party or to any appropriate government or taxing authority any form, certificate or document specified in the agreement or reasonably requested in order to allow the other party to make a payment without any deduction or withholding on account of any tax or other duty, provided it is reasonably able and legally in a position to do so and would not thereby materially prejudice its legal or commercial position (see EMA General Provisions § 10(4)).

15. Manufactured dividends

Both the GMRA and the EMA provide in substantively similar terms that if during the term of a transaction any distributions are made in respect of securities subject to that transaction, the buyer/margin receiver will pay a 'manufactured dividend' equal to the amount of the distribution (see GMRA § 5; EMA Product Annex for Repurchase Transactions § 4(1)).

Under the GMRA the amount paid is the gross amount, without any tax withholding or deduction even where a distribution is subject to such a withholding or deduction (see GMRA § 5), with the risk of tax withholding/deduction falling entirely on the party obliged to make the manufactured dividend.

Under the EMA if a distribution is subject to withholding tax and/or gives rise to a tax credit the amount paid is also the gross amount, described as "the full amount to which the [seller/ margin provider] would be entitled, as previously notified by it, in respect of such distribution if it were the owner of the [securities]" (see EMA Product Annex for Repurchase Transactions § 4(2)). The EMA formula would thus appear to require prior notification of the gross amount payable by the seller/ margin provider before the seller/margin provider would be entitled to be grossed up. Also, as noted above, the EMA would not require any gross-up where a tax is imposed by reason of a connection between the withholding jurisdiction and the jurisdiction of the payee.

16. Events of default

<u>Payment fails</u>. Under the GMRA any failure to pay the purchase price, repurchase price or manufactured dividends constitutes an event of default, triggering a right to serve a default notice on the defaulting party leading to close out (see GMRA § 10(a)(i), (v)).

Under the EMA any failure to make a payment that continues for three business days after notice of failure constitutes an event of default, triggering a right to serve a default notice on the defaulting party leading to close out (see EMA General Provisions § 6(1)(a)(i)).

The EMA differs from the GMRA in this respect insofar as a three business day grace period is available. The drafters of the EMA took this approach on the basis that a payment failure occurs easily due to an operational error, and that this should not, without even a warning notice, be a reason for the draconian measure of close-out. In this regard, the drafters note that the ISDA Master Agreement, as well as the standard French, German and most other master agreements, provide for such a grace period after notice of the failure. However, some market participants argue that the absence of a grace period better protects a non-defaulting party, and consideration may be given to reducing the grace period to 1 day, with an option for no grace period at all.

Another distinction between the EMA and the GMRA is that under the EMA any failure to pay (including a failure to pay damages or a cash settlement amount upon non-delivery) can trigger an event of default, whereas under the GMRA only a failure to pay the purchase/ repurchase price can trigger an event of default.

Settlement failures. Under the GMRA a failure to deliver securities constitutes an optional event of default, triggering a right to serve a default notice on the defaulting party leading to close out where the parties so specify (see GMRA § 10(a)(ii)). Unlike the GMRA, the EMA does not specify that a failure to deliver can constitute, per se, an event of default, except in the case of a failure to provide margin or collateral that becomes due (see EMA General Provisions § 6(1)(a)(ii)).

It is noted that, as compared to the 1995 version of the GMRA, the 2000 GMRA introduced a new optional event of default which enables a party to serve a default notice closing out transactions upon the occurrence of a 'settlement fail' (i.e., a failure by a party to deliver securities on either the purchase or repurchase leg of a repo transaction) (see 2000 GMRA § 10(a)(ii)). This close-out event of default is optional, and only applies if the parties expressly so provide in the annex to the master agreement. There were divergent views amongst market participants as to the desirability of including such an event of default, and this was the main reason why the event is optional. Some market participants were reluctant to include this new event of default on the ground that settlement fails frequently occur in the market and that their occurrence is not generally an indicator of credit deterioration or impending insolvency of the non delivering party. As against that, however, market participants favouring the inclusion of this event of default believed strongly that there could be circumstances in which a failure to deliver is in fact a first indicator of credit deterioration or impending insolvency (although they recognised that this would not generally be the context in which a failure to deliver occurred), and they wished to be able to act upon the occurrence of a failure to deliver where they saw it occurring in a credit deterioration or impending insolvency context.[5]

[5] TBMA/ISMA Global Master Repurchase Agreement (2000 Version), Note of principal changes from November 1995 version (taken from TBMA website).

It is noted that settlement failures constitute an event of default under the New York law Master Repurchase Agreement widely used in the U.S. repo markets, and participants in the U.S. repo markets have in practice applied this provision in a reasonable manner, not using the draconian sanction of a close out following mere operational failures, which would of course be contrary to market practices and expectations.

<u>Margin/collateral delivery fails</u>. Under the GMRA the failure to comply with the margin maintenance provisions (see GMRA § 10(a)(iv)), and under the EMA a failure to provide or return margin or collateral when due (see EMA General Provisions § 6(1)(a)(ii)) constitutes an event of default, triggering a right to serve a default notice on the defaulting party leading to close out.

<u>Other breach of agreement</u>. The GMRA and the EMA provide in similar terms that the failure to perform any other obligation under each agreement which is not remedied within 30 days after notice is given constitutes an event of default, triggering a right to serve a default notice on the defaulting party leading to close out (see GMRA § 10(a)(x); EMA General Provisions § 6(1)(a)(iii)).

<u>Misrepresentation</u>. Under the GMRA the fact that a representation proves to be incorrect or untrue in any material respect is sufficient to trigger an event of default (see GMRA § 10(a)(vii)), while under the EMA the representation must not only prove to be incorrect, but the injured party must also make a good faith determination that the balance of its risks and benefits under the Agreement has been materially adversely affected as a result of such misrepresentation (see EMA General Provisions § 6(1)(a)(iv)).

<u>Default under 'specified transaction'</u>. Under the EMA, where the parties so specify, the failure to make a payment under any transaction specified by the parties can constitute an event of default where the failure results in the close-out of that specified transaction or continues beyond any applicable grace period (or, if there is no such grace period, for at least three business days) after the last payment date of that specified transaction[6] (see EMA General Provisions § 6(1)(a)(v)). This provision in the EMA, for which there is no corresponding provision in the GMRA, would appear to allow the parties to specify that the failure to make payments under any transactions not governed by the EMA – for example, (a) transactions between a party and a third party or (b) transactions between the parties that are

[6] Provided that the failure is not caused by circumstances which, if occurring under the Agreement, would constitute a change of circumstances giving rise to a right to terminate the EMA. See EMA General Provisions § 6(2)(a)(ii), discussed below.

not governed by the EMA - can trigger an event of default where the payment failure leads to a close-out of such transaction or continues for three business days. It is noted that there is no threshold amount needed in order to trigger this cross-default. This provision is similar to the 'default under specified transaction' event of default under the ISDA Master Agreement (see ISDA § 5(a)(v)). Cross-default clauses have not been considered necessary for the GMRA because repos are self-collateralising transactions. However, there is some debate in the market on this point, and the Global Documentation Steering Committee (formed to continue the discussion begun by the Counterparty Risk Management Policy Group (CRMPG), the group of 12 major, internationally active [both North American and European] commercial and investment banks established in 1998 to enhance counterparty credit and market risk management after the market disruptions of 1997 and 1998) has made a recommendation urging TBMA to rapidly implement a cross-default provision in the various master agreements sponsored by TBMA.

Cross default. The EMA contains a cross-default clause whereby any payment obligation of a party in respect of borrowed money in an amount specified by the parties (or if not specified, 1% of that party's equity) can constitute an event of default where (a) the payment has become, or may be declared,[7] due and payable prior to its stated maturity as a result of any default or similar event (however described) which has occurred in respect of that party or (b) the payment has not been performed for more than seven days after its due date, and in either case the other party has reasonable grounds to conclude that the financial obligations of the party under the Agreement may not be performed (see EMA General Provisions § 6(1)(a)(vi)).

This cross-default provision with a materiality limitation in the EMA, for which there is no corresponding provision in the GMRA, is intended by the drafters of the EMA to protect against unjustified default terminations in certain technical default situations (e.g., the non-payment of debts to third persons incurred by a party through a foreign branch office due to intervening illegality or impossibility) by only allowing the cross-default to trigger an event of default under the EMA where the non-defaulting party determines on reasonable grounds that the defaulting party's obligations under the EMA may not be performed. This approach is viewed by the EMA's drafters as a compromise between the GMRA, which does not address cross-default at all, and the ISDA Master Agreement (see ISDA § 5(a)(vi)) which provides, albeit at the option of the parties, for a strict and rigid cross default termination clause which

[7] Note that the cross default is triggered if indebtedness is capable of being accelerated, but has not yet been accelerated. This is intended to give the non-defaulting party under the EMA leverage in early creditors' negotiations with the defaulting party.

would allow a party to close out in a technical default scenario in which the draconian sanction of a close out might not be justified. This compromise approach makes it a more difficult judgement to invoke this clause under the EMA where the defaulting party is in financial difficulties but not yet clearly insolvent.

Corporate restructuring without assumption. Under the EMA the failure by a successor entity to a party subject to a corporate restructuring (e.g., consolidation, amalgamation, merger, transfer of all/substantially all assets) to assume all of such party's obligations under the Agreement constitutes an event of default (see EMA General Provisions § 6(1)(a)(viii)).

This provision in the EMA, for which there is no corresponding provision in the GMRA, is similar to the 'merger without assumption' event of default applicable under the ISDA Master Agreement (see ISDA § 5(a)(viii)).[8]

Repudiation of obligations. Under the GMRA an admission by one party to the other that it is unable to, or intends not to, perform any of its obligations under the agreement and/or in respect of any transaction under the agreement can trigger a close-out (see GMRA § 10(a)(viii)).

Under the EMA a declaration by a party that it will not perform any material obligation under the agreement or under any transaction specified by the parties (otherwise than as part of a bona fide dispute as to the existence, nature or extent of such obligation) can trigger a close-out (see EMA General Provisions § 6(1)(a)(ix)).

The EMA 'repudiation of obligations' event of default is broader than the corresponding GMRA provision in some respects, and narrower in other respects. While the GMRA permits any repudiation of obligations to trigger a close-out, the EMA only permits a repudiation of 'material' obligations to trigger a close-out. On the other hand, while the EMA permits a repudiation of obligations under both the agreement itself and any other transaction specified by the parties, the GMRA only permits a repudiation of obligations under the agreement to trigger a close-out.

[8] It is noted that a take-over by acquisition of shares would not be covered by this clause under either the EMA or the ISDA unless followed by a merger or other restructuring, which would not necessarily always be the case.

Insolvency-related events of default. The GMRA and the EMA both contain lists of overlapping insolvency-related events of default, some but not all of which trigger an automatic close-out (see GMRA §§ 2(a), 10(a)(vi); EMA General Provisions §§ 6(1)(a)(viii), 6(1)(b)). A number of distinctions between the GMRA insolvency-related events of default and the corresponding provisions of the EMA should be noted.

Under the EMA insolvency-related events can only trigger a close-out if they occur in a party's home jurisdiction or other jurisdictions specified by the parties (which may be, e.g., one or more jurisdictions in which the party has its main asset base or activities). By contrast, insolvency events in the GMRA are not stated to have any territorial scope, and the GMRA may thus be interpreted to mean that insolvency proceedings in any country, whether or not the party is present or has significant assets there, can trigger a right to close out or even an automatic close out.

Under the GMRA only a winding-up petition or analogous proceeding or the appointment of a liquidator or analogous officer can trigger an automatic close-out. By contrast, under the EMA, unless the parties specify otherwise, a broader range of insolvency proceedings can trigger an automatic close-out, including the commencement by a counterparty or the competent authority of a mandatory or voluntary proceeding seeking a judgment, order or arrangement of insolvency, bankruptcy, composition, amicable settlement, rehabilitation, reorganisation, administration, dissolution or liquidation with respect to a party or its assets or seeking the appointment of a receiver, liquidator, administrator or similar official for that party or for all or any substantial part of its assets under any bankruptcy, insolvency or similar law or any banking, insurance or similar law governing the operation of the party.

The EMA provides that a competent authority taking any action under any bankruptcy, insolvency or similar law governing the operation of the party which is likely to prevent the party from performing its payment or delivery obligations under the agreement can trigger an event of default. The GMRA does not contain any analogous provision.

The EMA provides that the commencement of an insolvency proceeding by any person other than a competent authority will not trigger an event of default where such proceeding is obviously inadmissible or frivolous. The GMRA does not contain any analogous materiality limitation.

While the GMRA lists a party's written admission that it is unable to pay its debts as an event of default, under the EMA an event of default can be triggered where the party is "generally unable" to pay its debts.

Termination upon event of default. Under the GMRA, except with respect to insolvency-related events of default triggering an automatic close-out, a non-defaulting party may close out upon service of a default notice (see GMRA § 10(a)). The EMA provides in similar terms that, except with respect to insolvency-related events of default triggering an automatic close-out, a non-defaulting party may, by giving not more than 20 days' notice, close out with effect from a date designated by it in the close-out notice (see EMA General Provisions § 6(1)(b)). The EMA confers an additional amount of flexibility on the closing-out party insofar as it may close out with effect from a date that is different from the date on which the default/close-out notice is given.

17. Additional termination events

Termination due to tax event. Both the GMRA and the EMA give a special right of early termination to a party in respect of any transactions affected by any change in tax law or practice which, under the GMRA, has a material adverse effect (or, in the party's reasonable opinion, will have such an effect) or, under the EMA, subjects a party to withholding taxes or deductions (see GMRA § 11; EMA General Provisions §§ 6(2)(a)(i), 6(2)(b)). Several points of distinction between the GMRA and the EMA may be noted.

In contrast to the EMA, the GMRA 'termination due to a tax event' clause permits termination not only upon the occurrence of a tax event, but also upon the occurrence of any change in the regulatory regime having a material adverse effect on a party. In contrast to the EMA, under the GMRA the terminating party must indemnify the other party against any reasonable legal and other professional expenses incurred by the other party by reason of the termination, but the other party may not claim consequential losses or damages (for example, the cost of unwinding matching transactions).

The EMA 'early termination due to tax event' provision may be triggered by the payment of withholding taxes or tax deductions incurred as a result of any corporate restructuring of either party.

Termination due to illegality or impossibility. Under the EMA, if (a) as a result of any change in law or practice (i.e., the application or official interpretation of any law) or (b) if the parties so specify, as a result of an impossibility event (i.e., any catastrophe, armed conflict, act of terrorism, riot or any other circumstance beyond the party's reasonable control affecting the operations of the party), it becomes or is likely to become unlawful or impossible for a party to make or receive a payment or delivery in respect of such transaction when due or to punctually comply with any other material obligation under the agreement, either party may terminate the transactions affected by such illegality or impossibility (see EMA General Provisions §§ 6(2)(a)(ii), 6(2)(b)).

There is no corresponding provision under the GMRA for this termination event due to illegality or impossibility event under the EMA. The ISDA Master Agreement contains an 'illegality' termination event (see ISDA § 5(b)(i)), and ISDA is currently developing updated 'illegality' and new 'force majeure' provisions. Some market participants favour the introduction of a force majeure clause into the GMRA, although some oppose the introduction of a force majeure clause in repo agreements for the reason that force majeure events mainly affect counterparties in emerging markets, and they would prefer to be able to close-out against counterparties in such circumstances. It may be that the ISDA formula will be closely examined by market participants with a view to standardising across all market agreements. In this regard, it is understood that the CRMPG Global Documentation Steering Committee is working on the development of such a market standard proposal. It is noted that the EMA's impossibility termination event is only applicable if so specified by the parties.

Termination due to credit event upon corporate restructuring. If a party is subject to a corporate restructuring and the creditworthiness of the successor entity is materially weaker than that of the party immediately before the corporate restructuring, the other party may terminate the transactions affected by such credit event (see EMA General Provisions §§ 6(2)(a)(iii), 6(2)(b)). There is no corresponding provision under the GMRA for this termination due to credit event upon corporate restructuring under the EMA. The ISDA Master Agreement contains a similar 'credit event upon merger' as a termination event (see ISDA § 5(b)(iv)).

18. Applicability of events of default and additional termination events to guarantor

Under the EMA if a guarantee has been given with respect to a party the events of default and termination events under the EMA apply with equal force to any guarantor of a party, as well as to the party itself (see EMA General Provisions § 6(3)). In addition, under the EMA where a guarantee given with respect to a party is not in full force or effect, this can constitute an event of default (see EMA General Provisions § 6(1)(a)(x)). These provisions, for which there are no corresponding provisions in the GMRA, may be compared with the ISDA Master

Agreement, which similarly provides that the events of default and termination events apply with equal force to a party's 'credit support provider' (see ISDA § 5) and which also provides for a 'Credit Support Default' (see ISDA § 5(a)(iii)).

In the case of repo transactions, the presence of such provisions would not typically be significant as repo transactions are not typically guaranteed insofar as repos are settled on a dvp basis and repo exposures are generally collateralised through the application of the margin maintenance provisions.

19. Close-out mechanics

Close-out mechanics under GMRA. Upon the occurrence of an event of default, all outstanding transactions are accelerated so that the parties' obligations to pay the repurchase price, deliver securities on the repurchase leg, repay cash margin and deliver equivalent margin securities fall to be performed immediately, and these obligations are immediately settled by set-off. This set-off is effected by establishing the 'default market values' of the equivalent securities or equivalent margin securities to be transferred by each party and the cash amounts payable by each party (by way of repurchase price or repayment of cash margin) and taking an account of what is due from each party to the other on the basis of the resulting figures. The sums due are then set off against each other and only the balance is payable by the party with the lower aggregate amount due to it. For the purposes of this calculation, all sums not determined in the base currency are converted into the base currency at the spot rate of exchange quoted by Barclays Bank PLC in the London interbank market that is prevailing at the relevant time. (See generally GMRA §§ 10(b), (c).)

Close-out mechanics under EMA. Upon termination under the EMA, neither party is obliged to make any further payment or delivery under the terminated transactions which would have become due on or after the termination date or to provide or return margin or collateral which would otherwise be required to be provided or returned. These obligations are replaced by an obligation by either party to pay the 'final settlement amount' (i.e., the net close-out amount), which is required to be calculated as soon as reasonably possible by the non-defaulting party.[9]

> The 'final settlement amount' comprises the amount determined by the calculation party as equal to, as of the termination date, (a) the sum of all transaction values (comprising, at the option of the calculation party, either (i) losses incurred or gains realised as a result of the termination of such transactions or (ii) the arithmetic mean of the quotations for

[9] In the case of termination due to a change of circumstances due to a tax event, illegality, impossibility or credit event upon restructuring, the calculation is made by the non-affected party (or each party where there are two parties affected by such change or circumstances).

replacement or hedge transactions on the termination date (or in the event of an automatic termination, the date designated by the non-defaulting party, which is not later than the fifth business day after the day on which the non-defaulting party became aware of the event that caused such automatic termination) obtained by the calculation party from not less than two leading market participants); (b) the sum of (i) amounts required to be paid by the parties under any transaction, but not paid; (ii) the ‘default value’, as of the agreed delivery date, of each asset that was required to be delivered by such party under any transaction, but not delivered; and (iii) interest on these amounts from the due date of payment or delivery at the interbank rate for overnight deposits or, in the case of late payments, the default rate (which is equal to the higher of the interbank rate or the cost of funding); and (c) as of the termination date, the aggregate amount of cash paid and the ‘default value’ of securities transferred, as margin or collateral, by the party and not repaid or retransferred to it, plus any interest accrued on such cash at the rate agreed by the parties. Amounts not denominated in the base currency (which is the euro, unless otherwise agreed) are converted into the base currency at the arithmetic mean of the respective rates at which the person calculating/converting an amount is reasonably able to purchase and sell the relevant currency for the base currency on the relevant date. It is noted that the ‘final settlement amount’ may be either a positive or a negative amount (see generally EMA General Provisions §§ 6(4), 7).

<u>Comparison of close-out mechanics under GMRA and EMA</u>. The EMA appears to allow greater recovery than the GMRA, permitting recovery of either losses incurred or gains realised as a result of the termination of transactions or (at the calculation party’s option) the cost of (arithmetic mean of quotations for) replacement or hedge transactions. The method of calculation is broadly similar to the method provided under the ISDA Master Agreement (see ISDA § 6(d), (e)), with the calculation party having the choice between determining the amounts by reference to losses incurred or gains realised (comparable to ISDA’s ‘Loss’ method) or the arithmetic mean of quotations from at least two market participants (comparable to ISDA’s ‘Market Quotation’ method).

In contrast to the EMA close-out mechanism, which (like the ISDA) is generic in order to have the broadest possible application in view of its multi-product nature, the GMRA is tied more closely to the mechanics of repo transactions. The GMRA allows recovery of any loss or expense incurred in entering into replacement transactions or in unwinding hedging transactions, less the amount of any gain/profit made in connection with such replacement or unwinding, as calculated in good faith by the non-defaulting party (see GMRA § 10(k)). As noted below, there is no loss-based calculation option in the GMRA, and the GMRA provides less scope for the recovery of consequential losses.

Concept of 'default market value' under GMRA. Under the GMRA the concept of 'default market value' is defined in such a way that the non-defaulting party may choose whether to apply one of the three following formulae in calculating the default market values of securities:

(i) default market values calculated at any time during five dealing days following the default by reference to either the net proceeds of sale (after deducting fees, etc.) of securities sold by the non-defaulting party (in respect of closed-out transactions in which the non-defaulting party was due to deliver such securities to the defaulting party at the repurchase leg) and the cost (including fees, etc.) or the aggregate cost of purchase of securities purchased by the non-defaulting party (in respect of closed-out transactions in which the non-defaulting party was due to receive such securities from the defaulting party at the repurchase leg); or

(ii) default market values calculated at any time during five dealing days following the default by reference to offer or bid quotations from two or more market makers or regular dealers in the appropriate market, taking into account transaction costs; or

(iii) where the non-defaulting party has endeavoured but been unable to sell or purchase securities or to obtain quotations, or determines that it would not be commercially reasonable to obtain such quotations (e.g., where the position is so large that this will materially affect the quotations that could be obtained) or to use any quotations which it has obtained (e.g., where the securities are very illiquid and there is considerable disparity between the quotations obtained), default market values may be calculated at any time during five dealing days following the default by reference to such amount which, in the reasonable opinion of the defaulting party, represents their fair market value, having regard to such pricing sources and methods as the non-defaulting party considers appropriate, taking into account transaction costs.

In the absence of any choice by the non-defaulting party of any of the three options above, default market values will be calculated at the close of business on the fifth dealing day following the default (or as soon as reasonably practicable thereafter if the non-defaulting party determines that, owing to circumstances affecting the market in the securities in question, it is not possible to determine a fair market value of the securities which is commercially reasonable) by reference to such amount which, in the reasonable opinion of the defaulting party, represents their fair market value as set out in the third option above (see generally GMRA §§ 10(d), (e)).

Concept of default market value under EMA. Under the EMA 'default value' means, in respect of any assets (including securities) on any given date, an amount equal to (a) if the assets are/were to be delivered by the calculation party, the net proceeds (after deducting fees and expenses) which the calculation party has or could have reasonably received when selling assets of the same kind and quantity in the market on such date, (b) if the assets are/were to be delivered to the calculation party, the cost (including fees and expenses) which the calculation party has or would have reasonably incurred in purchasing assets of the same kind and quantity in the market on such date and (c) if a market price for such assets cannot be determined, an amount which the calculation party determines in good faith to be its total losses and costs or gains in connection with such assets.

Comparison of default market values under GMRA and EMA. The concept of 'default market values' of securities under the GMRA differs from the concept of 'default values' of assets under the EMA in the following respects.

First, under the GMRA default market values are calculated by the non-defaulting party at any time during five dealing days following the default, whereas under the EMA default values are calculated by the calculation party on such date as the assets are/were to be delivered.

Second, under the GMRA where the non-defaulting party has endeavoured but been unable to sell or purchase securities or to obtain quotations, or determines that it would not be commercially reasonable to obtain or use such quotations, default market values may be calculated at any time during five dealing days following the default by reference to such amount which, in the reasonable opinion of the defaulting party, represents their fair market value, having regard to such pricing sources and methods as the non-defaulting party considers appropriate. Moreover, in the absence of any choice by the non-defaulting party of the methodology to follow in calculating default market values, default market values will be calculated at the close of business on the fifth dealing day following the default by reference to such amount which, in the reasonable opinion of the defaulting party, represents their fair market value, having regard to such pricing sources and methods as the non-defaulting party considers appropriate. By contrast, under the EMA the default values of assets may only be calculated by reference to an amount which the calculation party determines in good faith to be its total losses and costs or gains in connection with such assets where a market price for such assets cannot be determined. Thus, there is less scope under the EMA for a non-defaulting party to choose to calculate default values by reference to sources other than available market sources.

Market participants appear to be in agreement that the different approaches of the EMA and the GMRA do not give rise to any 'basis' risk in this area.

20. Consequential losses and damages following close-out

Under the GMRA neither party may claim any sum by way of consequential loss or damage in the event of the failure of the party to perform any of its obligations, except that the GMRA allows recovery of any loss or expense incurred in entering into replacement transactions or in unwinding hedging transactions, less the amount of any gain/profit made in connection with such replacement or unwinding (see GMRA § 10(j), (k)). The GMRA also allows recovery by the non-defaulting party of all reasonable legal and other professional expenses incurred by the non-defaulting party as a consequence of the event of default, together with interest at one-month LIBOR for the currency in question (or, in the case of any expense attributable to a particular transaction, the repo rate if higher) (see GMRA § 10(f)).

The EMA appears to provide for a greater measure of recovery on the part of a non-defaulting party. The EMA close-out mechanics introduce the concept of valuing terminated transactions by reference to losses and gains, which provide a possible additional measure of recovery for a non-defaulting party. A defaulting party is required to indemnify the non-defaulting party for all reasonable expenses, including legal fees, incurred by the non-defaulting party for the enforcement of its rights in connection with an event of default (see EMA General Provisions § 10(2)). Finally, while the GMRA is stated to constitute a complete statement of the remedies available to either party in respect of any event of default (see GMRA § 10(g)), the rights and remedies provided in the EMA are stated to be cumulative and not exclusive of any rights and remedies provided by law (see EMA General Provisions § 10(5)).

21. Remedies for late deliveries of securities

As previously noted, settlement failures may, at the option of the parties, constitute an event of default under the GMRA, but not the EMA. The remaining remedies for late deliveries under the GMRA and the EMA are quite similar, including requiring the failing party to return the purchase/repurchase price (if paid) and/or terminating that transaction and recovering specified costs. The GMRA explicitly permits a party to make a cash margin call following a delivery failure, whereas this is not expressly provided for in the EMA, although it is assumed that a cash margin call is permissible under the provisions of the EMA Margin Maintenance Annex. Consequential losses (other than replacement transaction or hedging costs) are not, as a general matter, recoverable under the GMRA, including with respect to late deliveries. With the exception of certain specified costs, consequential losses are stated not to be recoverable for late deliveries in particular under the EMA (see generally GMRA § 10(g), (h), (j), (k); EMA Product Annex for Repurchase Transactions § 2(6)). One cost recoverable under the EMA, but not under the GMRA, is the excess borrowing cost (e.g., the cost which the non-defaulting party incurred or would have reasonably incurred in borrowing equivalent securities in the market for the relevant period). The ability to recover excess borrowing costs in the event of a failure to deliver under the EMA appear to have been received negatively by some market participants.

22. Default interest for late payments

Under the GMRA, if any sum of money is not paid when due the GMRA establishes a formula for default interest linked to the greater of the repo rate or one-month LIBOR for the currency in question, to the extent permitted by applicable law (see GMRA § 12). The EMA establishes a formula for default interest linked to the greater of (a) the inter-bank offered rate for overnight deposits in the relevant currency and place of payment or (b) the cost of funding certified by the other party, plus any interest surcharge agreed by the parties or (c) in respect of a late payment of the purchase or repurchase price, the repo rate (see EMA General Provisions § 3(5), Product Annex for Repurchase Transactions § 2(5)). In establishing any such interest surcharge/ penalty interest, market participants would need to have regard to the applicable legal restrictions under certain national laws prohibiting the imposition of penalty interest by means of a contract between the parties.

23. Business day convention for payments and deliveries

The EMA, unlike the GMRA, sets out the common practice when it comes to determining the date of payments or deliveries where the due date is not a business day, allowing the parties to elect to make the payment or delivery on the immediately preceding business day or the immediately following business day, unless such day falls in the next calendar month in which case the relevant payment or delivery will be made on the immediately preceding business day (see EMA General Provisions §3(6)).

24. Multibranch liability for obligations of booking offices

Similar to the multibranch party provisions of the ISDA (see ISDA § 10), the EMA contains provisions to the effect that if a party enters into a transaction through a booking office other than its principal office, its obligations in respect of that transaction shall constitute obligations of such party as a whole, to the same extent as if they had been entered into through such party's principal office (see EMA General Provisions § 9). The absence of a comparable provision in the GMRA may create some doubt regarding whether the political and credit risk would be specific to each branch or to the principal office. However, unlike the ISDA, the EMA further provides that a party will not be obliged to perform any obligations through any of its offices other than the booking office if performance through the booking office is unlawful or impossible as a result of any change of law, catastrophe, armed conflict, act of terrorism, riot or other circumstance beyond the party' reasonable control (see EMA General Provisions § 9).

25. Representations

The GMRA and the EMA contain a number of overlapping representations (e.g., representations as to due authorisation, each party having obtained governmental consents, no conflicts with party's laws or constitution, non-reliance on other party regarding the suitability of a transaction) (see generally GMRA § 9; EMA General Provisions § 5). The following points of distinction between the representations in the GMRA and the EMA are noted.

- Time of making of representations. While both the GMRA and the EMA deem each representation to have been made as of the date on which the party enters into the master agreement and each date on which a transaction is entered into, the EMA does not provide, as is provided under the GMRA, that the representations are repeated on each date on which securities are transferred under any repo transaction (e.g., on each date on which margin securities are transferred). This may be due to the fact that the GMRA, unlike the EMA, contains a representation to the effect that at the time of any transfer of securities it will have the full and unqualified right to make such transfer, and upon such transfer the other party will receive all right, title and interest in and to those securities free of any lien, claim, charge or encumbrance.

- Valid existence. The EMA, unlike the GMRA but like the ISDA Master Agreement (see ISDA § 3(a)(i)), contains a representation to the effect that each party is validly existing under the law of its organisation or incorporation.

- Obligations legal, valid and binding. The EMA, unlike the GMRA but like the ISDA Master Agreement (see ISDA § 3(a)(v)), contains a representation to the effect that each party's obligations are legal, valid and binding.

- No event of default/ change of circumstances has occurred. The EMA, unlike the GMRA, contains a representation to the effect that no event of default (or event which by the lapse of time or the giving of notice may become event of default) or change of circumstances (i.e., tax event or event rendering performance illegal or, at the option of the parties, impossible, or corporate restructuring rendering party's creditworthiness materially weaker) with respect to a party has occurred and is continuing. This is similar to the representation under the ISDA Master Agreement to the effect that no potential event of default has occurred and is continuing (see ISDA § 3(b)).

- No material litigation. The EMA, unlike the GMRA, but like the ISDA Master Agreement (see ISDA § 3(c)), contains a representation to the effect that there is not pending against a party or, to its knowledge, threatened against it any action, suit or proceeding before any court, tribunal, arbitrator or governmental or other authority that is likely to affect the enforceability of the Agreement or a party's ability to perform its obligations.

- Acting as principal. Under the EMA the parties do not represent, unlike the GMRA, that they will engage in transactions as principal.

- No conflict with agreements. Under the EMA the parties do not represent, unlike the GMRA, that the execution, delivery and performance of the agreement and transactions thereunder will not violate any agreement by which it is bound or by which any of its assets are affected.

- Tax implications have been checked. Under the EMA each party does not represent, unlike the GMRA, that it has satisfied itself and will continue to satisfy itself as to the tax implications of the transactions under the Agreement.

- Non-reliance. While each party represents under both the EMA and the GMRA that it is not relying on the advice of the other party, this representation is crafted in greater detail under the GMRA. The substance of the representation is, however, the same under each agreement.

- Applicability to guarantor. The representations made under the EMA apply with equal force to any guarantor of a party, as well as to the party itself. In the case of repo transactions, this would not typically be significant insofar as repo transactions are settled on a delivery-versus-payment basis and repo exposures are generally collateralised through the application of the margin maintenance provisions.

26. Entry into transactions, confirmations, notices

- Entry into transactions. While under the GMRA a transaction may be entered into orally or in writing (see GMRA § 3(a)), the EMA provides that a transaction may be entered into orally or by any other means of communication (see EMA General Provisions § 2(1)). It is assumed that 'written' agreements under the GMRA would cover all electronic forms of communication, whereas these are explicitly covered by the EMA's reference to 'any other means of communication'.

- Confirmations. Under the GMRA, upon entering into a transaction, either or both parties (as shall have been agreed) is/are required to promptly deliver a written confirmation which includes certain specified details. The confirmation constitutes prima facie evidence of the terms agreed between the parties for that transaction, unless objection is made with respect to the confirmation after its receipt (see GMRA §3(b)). While under the EMA each party is also required to promptly send to the other a confirmation, the absence of confirmations is explicitly stated not to affect the validity of the transaction (§ 2(2)) A suggested form of confirmation is attached to individual product annexes, including, e.g., the product annex for repurchase transactions, and no details regarding the contents of a confirmation are prescribed.

- Notices. Under the GMRA notices must be in the English language and may be given in various manners (i.e., in writing in person or by courier, by telex, by facsimile, by certified or registered mail or by electronic messaging system), and it is only necessary to specify the address, number or electronic messaging details in the annex to the GMRA (see GMRA § 14(a), (b)).

  Under the EMA, unless otherwise agreed, notices must be made by letter, telex, telefax or other electronic messaging system agreed by the parties in the special provisions to the EMA, and to the address specified by the addressee (see EMA General Provisions § 8(1)). A distinction between the GMRA and the EMA is that the GMRA contains a provision, for which there is no corresponding provision in the EMA, that is designed to take into account the practical difficulties experienced by parties seeking to serve default notices on defaulting parties in extreme market conditions, whereby a non-defaulting party who has been unable to serve a default notice after having made all practicable efforts to serve such a notice in one of the normal ways permitted under the GMRA may sign a 'special default notice', the effect of which is to deem an event of default to occur with effect from the date and time specified in such special default notice (see GMRA § 14(c)).

27. Modification/amendments

Any modification of the EMA General Provisions or any modified or new annex (e.g., a new product annex for derivatives) which the Banking Federation of the European Union (FBE) may promulgate from time to time may become effective between the parties by each party notifying its acceptance in the manner designated by the FBE (EMA General Provisions §1(5)). The EMA provision may prove convenient as it would facilitate an amendment to the EMA General Provisions and annexes otherwise than by individual, bilateral re-negotiations with counterparties to amend the contract. Following the example of the ISDA EMU Protocol, amendments could be effected by means of a multilateral adhesion to the new EMA General Provisions and/or annexes, with the FBE acting as central depository. One of the most interesting aspects of this approach is that it facilitates amendments to market standard master agreements by means of electronic execution over the Internet.

28. Termination of agreement

The EMA requires not less than 20 days' notice before the agreement may be terminated (see EMA General Provisions § 10(7)), whereas the GMRA provides that the agreement may simply be terminated by either party upon written notice to the other (see GMRA §§ 16(c), (d)).

29. Non-assignments

While both the GMRA and the EMA require the prior consent of the other party to the assignment or transfer of a party's rights and obligations under the agreement[10] (see GMRA §§ 16(a), (b); EMA General Provisions § 10(1)), under the EMA this consent is not required in the case of a transfer of all or substantially all the assets of a party in connection with a corporate restructuring which does not involve a change of tax status relevant to the agreement and which does not otherwise adversely affect the interests of the other party to any significant extent. In this respect, the EMA goes further than, for example, the ISDA Master Agreement, which only allows the ISDA Master Agreement itself, but not any interest or obligation in or under the ISDA Master Agreement, to be transferred pursuant to a consolidation, amalgamation, merger or transfer of all/ substantially all of a party's assets (see ISDA § 7(a)).

[10] Except that a party may assign amounts receivable from the other party arising upon termination because of default/ termination.

30. Severability

While each of the GMRA and the EMA contains a severability provision (see GMRA § 15; EMA General Provisions § 10(11)), the EMA provides that in the event that any provision of the agreement is invalid, illegal or unenforceable, the parties will in good faith negotiate a valid provision the economic effect of which comes as close as possible to that of the invalid, illegal or enforceable provisions.

31. Telephone recording

While the GMRA and EMA provide that the parties may electronically record all telephone conversations between them (see GMRA § 20; EMA General Provisions § 10(3)), the EMA further provides that (a) each party will give notice of such potential recording to its relevant personnel and obtain any consent that may be legally required before permitting such personnel to conduct such telephone conversations and (b) each party agrees that recordings may be submitted in evidence in any proceedings relating to the agreement or any potential transaction thereunder.

32. Previous transactions

The EMA contains a provision, for which there is no comparable provision in the GMRA, to the effect that transactions entered into prior to the effective date of the EMA will be subject to such EMA to the extent provided in the EMA Special Provisions (see EMA General Provisions § 10(9)).

33. Waiver of sovereign immunities

Each of the GMRA and the EMA contains an express waiver of sovereign immunities enjoyed by the parties (see GMRA § 19; EMA General Provisions § 11(4)).

34. Agency transactions

The provisions relating to the conduct of agency transactions under the GMRA and the EMA are broadly similar, allowing either party to enter into agency transactions as disclosed agent for an identified principal (see GMRA, Annex IV; EMA General Provisions § 10(10)). Although transactions with multiple principals are not excluded under the EMA, the EMA does not include the additional language now available under the GMRA regarding the allocation of agency transactions to multiple principals (e.g., in block transactions). This issue has been discussed by market participants, and it was agreed that the EBF working group would discuss this issue further.

35. Buy/sell back transactions

The GMRA and the EMA each contain specific provisions facilitating the documentation of buy/sell back transactions. (See generally GMRA Buy/Sell Back Annex; EMA Product Annex for Repurchase Transactions § 5). It is noted that under the GMRA it is explicitly provided that buy/sell backs are not terminable on demand. In the absence of any comparable provision in the EMA, it is assumed that buy/sell backs may be terminable on demand if the parties have specifically so agreed.

36. Italian Annex

The EMA does not contain provisions comparable to those applicable to the GMRA's annex containing supplemental terms and conditions for transactions in Italian domestic securities.