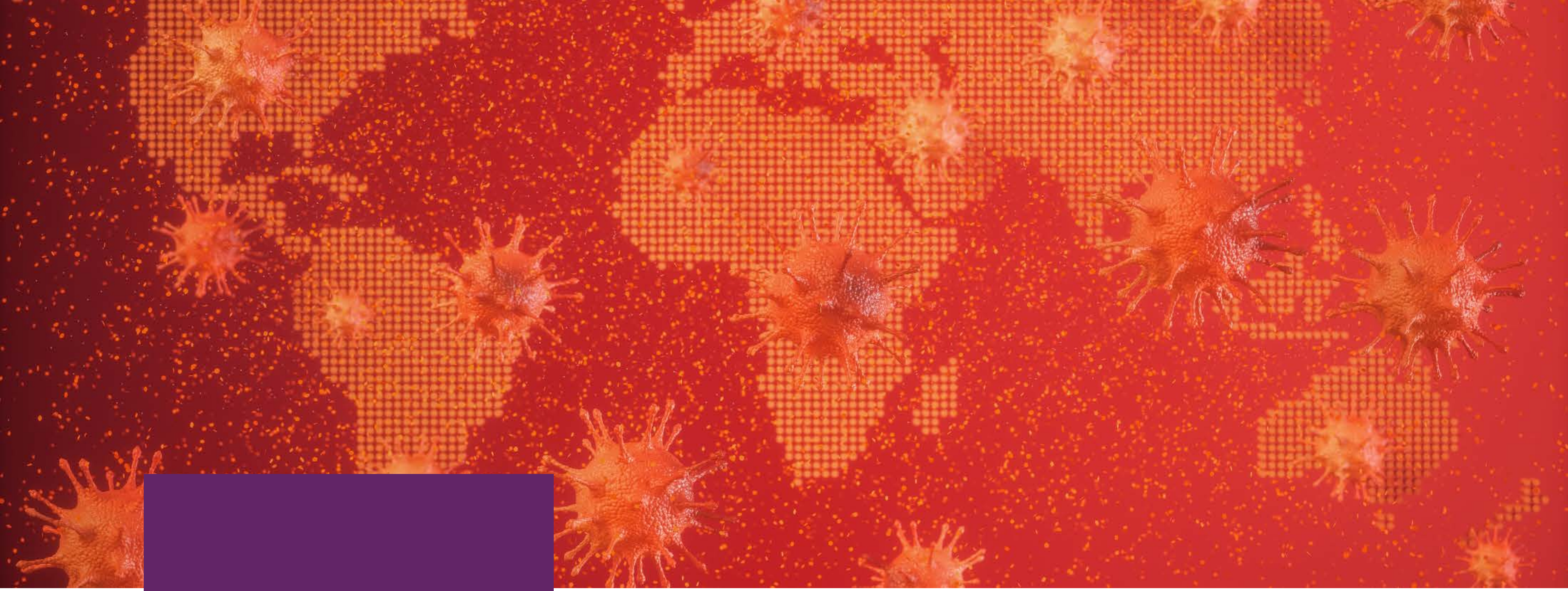

COVID-19: Key Issues for Swap and Repo Participants in a Difficult Market

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INTRODUCTION

- COVID-19
  - Impacts financial products and assets
  - Implications for financial stability
  - Challenges basic assumptions of swaps and repos
- Key issues discussed today
  - Understanding the documentation
  - Understanding performance issues and defenses
  - Legal issues under New York, US and English law

DOCUMENTATION

- Swaps:
  - 1992 vs. 2002 ISDA master agreement
  - Role of definitions, esp. disruption events
  - NY CSA vs. English CSA
  - Schedule contains negotiated terms and amendments
- Repos:
  - 2000 or 2011 GMRA (English law) v 1996 MRA (NY law)
  - Annex contains negotiated terms and amendments

THE MECHANICS OF MARGIN CALLS

Swaps

- Margin calls preserve collateral securing net mark-to-market amount on all transactions (the "Exposure")
- Minimum Transfer Amount
- "Valuation Agent"
- Margin calls subject to dispute resolution

Repurchase Transactions

- Margin calls preserve the agreed margin ratio (or haircut) on repo'd assets: *i.e.*, a % margin of the value of the repo'd assets above the contractual repurchase price
- Market value determination
- No dispute resolution provision

THE NEXT STEP: EVENTS OF DEFAULT OR TERMINATION EVENTS

- Overview of events of default and termination
- Solvency considerations:
  - Definitional differences in the master agreements
    - Older: 1992 ISDA, 1996 MRA, 2000 GMRA
    - Newer: 2002 ISDA, 2011 GMRA
  - But what is “insolvency” anyways?
- Force Majeure and COVID-19

THE NEXT-TO-LAST STEP: CALCULATING NET AMOUNTS DUE

Swaps

- Exposure is based on the early termination amount for the transaction in question.
- Depends on whether the transaction is documented under the 1992 ISDA master agreement ("loss" v. "market quotation") or the 2002 ISDA master agreement ("close-out amount").

Repurchase Transactions

- Exposure is based on the repurchase price: a fixed dollar amount equal to the original purchase price funded up-front plus the agreed price differential (akin to interest).
- MRA: Final claim is based on market price then obtainable for the repo'd assets.
- GMRA: "Default market value" approach

THE LAST STEP: LIQUIDATING COLLATERAL

- US law:
  - Commercial reasonableness under UCC Article 9
  - Impact of safe harbors
    - Bankruptcy Code
    - FDIC-insured financial institutions
    - broker-dealers
- English law:
  - Good faith
  - Close-out netting

CONCLUSION

- How is market value determined in volatile or illiquid markets?
- How and when is NAV determined?
- How to determine a fund's solvency?
- Is liquidation commercially reasonable / in good faith?

QUESTIONS?

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