Introduction

In November 1995 the International Securities Market Association ("ISMA") and the Public Securities Association ("PSA") published a revised version of the PSA/ISMA Global Master Repurchase Agreement (the "Agreement"), the first version of which was published in November 1992.

The Agreement is published with guidance notes which are designed to assist users of the Agreement and summarise all of the provisions of the Agreement. There have been significant changes from the 1992 version of the Agreement, and the purpose of this note is to explain the principal changes.

Definitions (paragraph 2)

Act of Insolvency

The definition of act of insolvency has been extended to include the convening of a creditors’ meeting for the purposes of considering a voluntary arrangement, or similar proceeding. The effect of this is to bring forward the time at which an act of insolvency occurs and thus the time at which an event of default may be called, thereby offering more protection to the other party.

Base Currency

The parties now specify a single base currency for the whole Agreement rather than separate currencies for the margin maintenance provisions and the set-off provisions.

Business Day

This definition has been amended to apply more precisely in relation to payments in different jurisdictions.

Designated Office

The revised draft Agreement requires parties to specify the branches or offices through which they will enter transactions to be governed by the Agreement. This will enable parties, for credit and regulatory capital purposes, to enter into transactions only through branches or offices in jurisdictions in respect of which legal opinions as to the efficacy of the netting provisions of the Agreement have been obtained.

If parties use a branch or office in another jurisdiction, supervisors may not recognise the netting provisions of the Agreement for capital adequacy purposes with the consequence that gross exposures to counterparties may be required to be taken into account.

Default Market Value

This definition has been expanded to provide that the default market value is calculated by reference to the "Default Valuation Time". This is defined as the close of business in the most appropriate market for the securities in question (as determined by the non-defaulting party) on the day following the day of default (if the default occurs during business hours on a dealing day in that market) or (if not) the following dealing day. The default valuation time may therefore differ (in absolute terms) between different securities traded in different time zones. The Agreement provides that if the non-defaulting party actually deals in that market before the default valuation time, the price which it obtains is the default market value. Otherwise the default market value is the best price reasonably obtainable on that market at the default valuation time.

This change was prompted by the Barings situation, where the event of default (the placing of Barings into administration) occurred on a Sunday.
Margin Ratio and Transaction Exposure

These new definitions are used in the margin maintenance provisions (paragraph 4) which are explained below.

New Purchased Securities

This new definition is used in the substitution provisions (paragraph 8) which are explained below.

Margin maintenance (paragraph 4)

These provisions have been changed radically in order to reflect market practice. The main changes are as follows:

- "Buyer’s Margin Amount" and "Seller’s Margin Amount" have been replaced by "Margin Ratio". This is defined as the market value of the purchased securities at the time the transaction was entered into divided by the purchase price, or such other proportion as the parties may agree. The effect of this is to fix the margin ratio at the time of the transaction by reference to the initial purchase price rather than setting different margin amounts for buyer and seller. Of course the parties are free to choose a different margin ratio for any or all transactions entered into under the Agreement.

- Instead of calculating the margin requirement for each transaction, margin is calculated on a global basis for all transactions to give an overall net exposure. There is no longer a requirement to attribute any provision of margin to particular transactions.

- A margin call is satisfied by making a "Margin Transfer" which may be by way of cash or securities. The combination of cash and securities which make up a margin transfer is at the option of the party providing margin, although any securities provided must be reasonably acceptable to the other party.

- Where a margin transfer is by way of cash, the parties may specify the currency, the rate at which interest is to accrue on that cash and the interest payment dates.

- The parties may elect not to include a particular transaction in the global margin calculation, but instead to provide margin separately in such manner as the parties may agree.

- The provision which enables the parties to specify a threshold which must be reached before a party may call for margin has been deleted but the parties may agree to provide for a threshold if they wish.

- The parties may elect to reprice a transaction rather than apply the margin maintenance provisions. Repricing may be effected by way of adjustment to the purchase price or to the securities. This may be applied to repos as well as buy/sell back transactions.

Payment and delivery (paragraph 6)

Paragraph 6(d) (which stated that where one party performs its obligation to pay money or transfer securities, but the other party fails simultaneously to perform a like obligation, the other party holds the money or securities which it has received on trust for the first party) has been deleted.

Substitution (paragraph 8)

This paragraph has been revised so as to make it clear that substitution is effected by the transfer to the seller of securities equivalent to some or all of the original purchased securities against the transfer of new securities ("New Purchased Securities") to the buyer.

Representations (paragraph 9)

A new representation (paragraph 9(g)) has been added to the effect that neither party is relying on the advice of the other, that each party has made its own decisions regarding the entering into of transactions under the Agreement and that it understands the risk, terms and conditions of each transaction.
Events of default (paragraph 10)
The events of default have been revised. Failure to deliver the purchased securities to the buyer on
the purchase date or to deliver equivalent securities to the seller on the repurchase date is no
longer an event of default, but the other party is entitled:

0 to require the repayment of the purchase price or repurchase price if it has paid it; or
0 if it has a transaction exposure in respect of the relevant transaction, to require the
payment of cash margin; or
0 by written notice, to declare that that transaction only shall be terminated.

Paragraph 10(a)(ii) (failure to comply with the margin maintenance provisions) has been amended
to remove the requirement for a second notice. The non-defaulting party is now entitled to serve a
default notice immediately on the other party failing to comply with the margin provisions.

Paragraph 10(g) contains a statement that the provisions of the Agreement contain a complete
statement of the remedies available to each party in respect of an event of default and paragraph
10(h) states that neither party may claim any sum by way of consequential loss or damage if the
other party fails to perform any of its obligations under the Agreement.

Withholding of payment or delivery (former paragraph 11)
This paragraph has been deleted.

Tax event (paragraph 11)
This paragraph provides that in the event of any action taken by a revenue authority or brought in
a court of competent jurisdiction or a change in tax law or practice which has a material adverse
effect on a party in the context of a transaction, that party may elect to terminate that transaction.
If it does so elect, the other party may override the election to terminate the transaction, but in so
doing will agree to indemnify the affected party against the adverse effect.

Notices and other communications (paragraph 14)
This paragraph has been rewritten.

Non-assignability; termination (paragraph 16)
A provision has been added (paragraph 16(b)) which permits a party to assign its right in a net sum
payable to it following termination after an event of default.

Recording (paragraph 20)
Each party consents to the tape recording of telephone calls between them. This is recommended

Buy/sell back transactions (Annex III)
This annex enables the Agreement to be used for buy/sell back transactions and contains the
amendments to the Agreement required for these transactions.

The transaction must be identified as a buy/sell back in the confirmation. The confirmation relating
to a buy/sell back may be in the form of a single document or two separate confirmations. The
confirmation (or at least one of them where there are two) must specify the pricing rate applicable
to the transaction.

Buy/sell back transactions are not terminable on demand. The purchase price and the sell back
price are to be quoted exclusive of accrued interest.

No manufactured payments are made on buy/sell back transactions.
Agency transactions (Annex IV)

An agency transaction is a transaction in which one of the parties is acting as agent for an identified principal. The Agreement does not cover transactions for unnamed principals, block transactions (i.e. single transactions which are allocated among two or more underlying principals) or transactions which are to be allocated to principals after they have been entered into. The annex does not permit transactions where both parties are acting as agents.

A party may only enter into an agency transaction if it is acting on behalf of a single principal and discloses the identity of the principal (either by name or by reference to a code or identifier). The agent must also have authority to enter into the transaction on behalf of the principal and authority to perform all of the principal’s obligations under the Agreement. The confirmation relating to an agency transaction must specify that it is an agency transaction.

If an event of default occurs in relation to the agent, the other party may elect that it shall be treated as an event of default in respect of the principal. This is because, although the non-defaulting party should be protected legally in the event of the insolvency of the agent (as the transaction is with the principal and not the agent), it may, as a practical matter, be difficult to enforce rights where the agent has defaulted.

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