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Master Securities Loan Agreement

Overview

The following discussion of The Bond Market Association Master Securities Loan Agreement (the "Agreement") provides and overview of the scope of the Agreement and a summary of its key provisions. The purpose of this discussion is to assist users of the Agreement in understanding the basic structure as well as certain of the more essential operational aspects of securities lending relationships governed by the Agreement. This discussion should not be relied upon by any party to determine, without appropriate legal, accounting, or other relevant professional advice, whether the Agreement is suitable to its particular circumstances and needs. Capitalized terms not otherwise defined in this discussion have the meanings ascribed to them in the Agreement.

I. Scope and Approach

The agreement is intended to provide a basic contractual framework, grounded in current market practice, for the rights and obligations of parties to securities loan transactions. The Agreement addresses many legal and regulatory concerns present in these transactions, but it allows the parties considerable flexibility, through the use of Schedule B, to address specific regulatory or other considerations and to structure the business aspects of their transactions. The Agreement has been prepared through extensive consultations with participants in the securities lending market and builds upon other securities loan agreements currently in use in the market, including the model agreements circulated in the past by the Securities Industry Association and by Robert Morris Associates.

The Agreement differs in its scope from existing model agreements in three principal respects. First, the Agreement was expressly designed to accommodate loans of both fixed income and equity securities. Although operational practices in these two markets tend to differ somewhat, the Agreement takes those differences specifically into account where feasible (e.g., in the calculation of fees under Section 4). In addition, it affords individual market participants sufficient flexibility to accommodate, through supplemental provisions in Schedule B, any differences in the practices of a firms fixed income and equity securities borrowing desks.

Second, the agreement contains a number of provisions designed to accommodate Loans of non-U.S. securities. In particular, the Agreement contains provisions addressing certain currency-exchange and international tax issues, as well as a definitional provision addressing variations in the definition of "Business Day" in different markets. The Agreement also contains a general provision relating to transfers of non-U.S. securities (in Section 16). Although the Agreement also contains a general provision relating to its use for Loans involving non-U.S. securities, it is important to recognize that the Agreement does not address comprehensively the individual legal and other considerations that must be taken into account in cross-border securities lending transactions. Most notably, it does not specify the means of transfer that are to be used for non-U.S. securities (which may have important operational and creditors' rights implications), nor does it address any special considerations arising under non-U.S. insolvency or other laws that may be applicable to a counterparty. These issues generally can be addressed fully only with knowledge of the specific non-U.S. securities and specific non-U.S. counterparties involved in a transaction and thus would be difficult to resolve in a master agreement that is intended to serve as a basic framework for a wide range of securities lending transactions.

Third, the Agreement has been drafted to permit either party to assume the role of Lender or Borrower. Thus, it may be used in transactions between Broker-Dealers or between Broker-Dealers and their customers, including customers represented by a bank or other Agent. Annex I to the Agreement contains special terms and provisions to govern transactions in which a Lender is represented by an Agent.

The agreement is being circulated in a printed form. The Bond Market Association (the Association) authorizes and encourages market participants to use the printed form of the Agreement if they wish to do so, but the Agreement is not intended, and should not be taken as legal advise. The Association will permit the use of an amended form of the Agreement only if the amendments to the Agreement are made in such a way as to be clearly identifiable, e.g., through the use of supplement to or mark-up of the printed form. Each party using the Agreement should assure itself, through review by its own counsel and the implementation of any necessary supplemental provisions in Schedule B, that it is authorized to enter into securities loan transactions and that, as a business and regulatory matter, the Agreement is appropriate for its use.

II. Specific Provisions

Section 1: Loans of Securities.

Pursuant to Section 1.1 of the Agreement, either party may orally seek to initiate a Loan, subject to the oral agreement of the other party to the basic terms of the Loan. Section 1.2 provides that a Loan shall not be deemed to have commenced until both the Loaned Securities and the Collateral have been transferred. In conjunction with Section 3.4, this provision is intended to confirm the absolute right of each party to the return of its property upon the other party's failure to perform its obligations at the initiation of a Loan. Section 1.3 provides the notice required by SEC Rule 15c3-3(b)(3)(iv) (governing Borrowers who are broker-dealers).

Section 2: Transfer of Loaned Securities.

Section 2.1 provides that, unless otherwise agreed, Lender must transfer the Loaned Securities to Borrower by the Cutoff Time on the agreed date for the commencement of the Loan.

Possible Use of Schedule B

The "Cutoff Time" is defined in Section 26.6 as a time agreed by the parties in Schedule B or otherwise orally or in writing. Parties may wish to specify a single Cutoff Time for all transfers or different Cutoff Times for different types of Loaned Securities, Collateral or currencies. In the absence of an agreement by the parties, the Agreement provides that the Cutoff Time shall be determined in accordance with market practice.

Under SEC Rule 15c3-3(b)(3)(ii) (governing Borrowers who are Broker-Dealers), a securities lending agreement must provide that Lender will be given a schedule of securities borrowed at the time of each Loan. Accordingly, under Section 2.2, unless otherwise agreed, Borrower must provide each lender that is a Customer with a form of schedule and receipt listing the Loaned Securities. This provision affords the parties flexibility in choosing among the different formats for schedules and receipts typically used by Borrowers and Lenders in securities lending relationships.

Section 3: Collateral.
Section 3.1 provides that, unless otherwise agreed, Borrower must deliver Collateral to Lender prior to or concurrently with the transfer of Loaned Securities to Borrower, but in no case later that the close of business on the day Lender transfers the Loaned Securities to Borrower. The market value of the Collateral must be equal to at least 100% of the market value of the Loaned Securities (or any higher Margin Percentage upon which the parties may have agreed).

> **Possible Use of Schedule B:**
> The parties may use Schedule B to specify alternative time for Collateral delivery or to choose a Margin Percentage greater than 100%. The Margin Percentage need not be the same for all Loans (e.g., different percentages may be desirable for different types of Loaned Securities or Collateral). Similarly, credit concerns in respect of particular counterparties may be addressed to some extent by means of the Margin Percentage.

In Section 3.2, Borrower grants Lender a security interest in the Collateral transferred by Borrower. The Collateral serves as a security for Borrowers obligations in respect of the loan to which it relates and any other obligations of Borrower to Lender. Unless Lender is a Broker-Dealer, it must segregate Collateral from other securities and assets in its possession. Lender may, however, invest any cash Collateral at its own risk. The Agreement specifically provides that Lender may retransfer or rehypothecate the Collateral only (a) if Lender is a Broker-dealer or (b) in the event of a Default by Borrower.

Section 3.3 obligates Lender to return the Collateral (as adjusted under the mark to market provisions) upon Borrower's return of the Loaned Securities at the termination of the transaction except as otherwise provided in the Agreement. At the initiation of a transaction, if one party transfers Collateral or Loaned Securities but the other party fails to make a reciprocal transfer, Section 3.4 provides the first party with an absolute right to the return of its Collateral or Loaned Securities, as the case may be.

Section 3.5 authorizes Borrower to substitute Collateral, upon appropriate notice to Lender. Substitution is only permitted, however, if (i) upon substitution the market value of all the Collateral for Loans in which the party substituting such Collateral is acting as Borrower is at least equal to the Margin Percentage of the market value of the Loaned Securities and (ii) the substituted Collateral falls within the categories of acceptable Collateral agreed upon by the parties prior to the Loan. If Borrower has provided letters of credit supporting its obligations under the Agreement and such letters are due to expire, Borrower must, before the Cutoff Time on their expiration date, obtain extensions of such letters of credit or provide substitute letters of credit in the appropriate amounts.

Section 3.6 provides express notice, as required by a 1989 SEC no-action letter, that the Collateral for a Loan may include, as permitted by applicable law, some Government Securities that are not backed by the full faith and credit of the U.S. Government (for example, securities issued or guaranteed by the Federal Home Loan Mortgage Corporation (Freddie Mac) or the Federal Mortgage Association (Fannie Mae)). See Public Securities Association (available March 2, 1989). See also Exchange Act Release No. 26608 (March 8, 1989) (proposed amendment to SEC Rule 15c3-3(b)(3)(iii) specifically permitting the use of certain agency securities as collateral).

Section 4: Fees for Loans.
Section 4.1 sets forth a framework in which the parties can agree upon fees consistent with common practice in the securities lending market. The parties must specify the actual fees themselves and may choose to do so on Schedule B. Section 4.2 specifies the date upon which such fees are due.

Section 5: Termination of the Loan.
Each Loan is terminable by Borrower at any time by giving notice and transferring the Loaned Securities to Lender by the Cutoff Time on any Business Day. Lender may terminate a Loan upon notice to Borrower, effective on a termination date no earlier than the standard settlement date applicable to transactions in the Loaned Securities entered into on the date of such notice. Thus, if a trade for a security is normally settled five days after the trade was made, Lender must provide five days' notice to Borrower before termination of a Loan with respect to that security. Unless Borrower and Lender agree otherwise, the termination date is defined as the next Business Day after notice for Government Securities and the fifth Business Day after notice for all other securities.

> **Possible Use of Schedule B:**
> Section 5 does not automatically provide for later (or earlier) termination dates for foreign securities unless specifically agreed by the parties. If the parties wish to specify periods longer than the standard settlement cycle of five Business Days or less, they should carefully review certain tax considerations, e.g., the possibility that a Loan may be treated as a taxable sale of securities, in the case of a taxable Lender, or that payment with respect to a Loan will be subject to unrelated business income tax, in the case of a tax-exempt Lender.

Section 6: Rights of Borrower in Respect of the Loaned Securities.
During the term of the Loan, Borrower has all incidents of ownership with respect to the Loaned Securities, including the right to transfer the Loaned Securities to others. Lender waives the right to vote or provide consent with respect to the Loaned Securities if the record date or deadline for such action falls during the term of the Loan. Borrower's rights under this Section are limited by Section 7, however, under which Lender retains the right to distributions on or in respect of the Loaned Securities.

Section 7: Dividends, Distributions, Etc.
Lender is entitled to receive all distributions on or in respect of the Loaned Securities to the full extent it would be so entitled if the Loan had not been made. So long as Lender is not in Default, Borrower is obligated to transfer to Lender cash in the amount of any cash distribution on the Loaned Securities which Lender is entitled to receive. Non-cash distributions are added to the Loaned Securities unless the Loan has terminated, in which case they are to be transferred

to Lender. Under Section 7.3, Borrower has the right to receive cash distributions on non-cash Collateral.

Section 7.4 provides for "gross-up" payments whenever a party obligated to make a distribution payment is required to withhold Tax on the payment. In general, the party entitled to receive a distribution payment is to be made whole to the extent that any Tax withheld on the payment exceeds the amount that would have been withheld if the party had received the distribution directly.

Possible Use of Schedule B:
Under Section 7.4(d), each party is deemed to represent that as of the commencement of any Loan no Tax would be imposed on it for any cash distribution paid to it with respect to (i) Loaned Securities subject to a Loan in which it is acting as Lender or (ii) Collateral for any Loan in which it is acting as Borrower. Parties, particularly foreign parties, should be aware of this deemed representation and should specify, in Schedule B or elsewhere, any Tax obligations known to be applicable to cash distributions on any Loaned Securities or Collateral.

Section 7.5 provides that if a transfer of a distribution on the Loaned Securities would give rise to a Margin Excess (i.e., the market value of all Collateral for Loans to Borrower would be greater than the Margin Percentage of the market value of the outstanding Loaned Securities subject to such Loans) or if a transfer of a distribution on Collateral would give rise to a Margin Deficit (i.e., the market value of all Collateral for Loans by Lender would be less than the Margin Percentage of the market value of the outstanding Loaned Securities subject to such Loans), the party that otherwise would have been required to make such transfer shall, instead, credit the other party's account by the amount of the distribution.

Section 8: Mark to Market.
Pursuant to SEC Rule 15c3-3(b)(3)(iii) and Regulation T of the Board of Governors of the Federal Reserve System, a Broker-Dealer Borrower must daily mark each Loan to market and maintain Collateral with a market value equal to at least 100% of the value of the Loaned Securities. Section 8.1, which implements these requirements, does not require notice from or any other action by Lender and applies regardless of any other agreements between the parties regarding the adequacy of Collateral.

Section 8.2 and 8.3 establish more general mark-to-market rights for both Lender and Borrower. In contrast to Section 8.1, these two Sections provide for marking to market based on the applicable Margin Percentage agreed upon by the parties (which may be greater than 100%). Further, neither Borrower nor Lender is required to "self-mark" under Sections 8.2 and 8.3; instead, each party's obligation to eliminate a Margin Deficit or Margin Excess arises only after the other party has given appropriate notice as specified in the Agreement. Margin Excess and Margin Deficit are to be calculated on an aggregate basis, unless the parties agree otherwise.

Section 8.4 expressly states that the parties may agree, with respect to one or more Loans, to mark to market the Loaned Securities and Collateral or exercise margin rights on a Loan-by-Loan basis. Section 8.5 recognizes that some parties may prefer to agree beforehand upon a minimum dollar or percentage threshold below which margin calls will not be permitted.

Possible Use of Schedule B:
Additional margin provisions deemed necessary by the parties, such as specific Cutoff Times, may be included in Schedule B.

Section 9: Representations.
Section 9 contains a number of general representations and warranties that are made by both parties, as well as certain specific representations and warranties made only by Borrower or Lender. Each party represents and warrants that it is authorized to engage in the Loans contemplated by the Agreement. Borrower represents and warrants that it at all times acts as principal for its own account. Borrower further represents and warrants that it is empowered to grant a first security interest in the Collateral and that it or the person to whom it relends the Loaned Securities is borrowing or will borrow the Loaned Securities for purposes permitted by Regulation T (except in the case of exempted securities, where the generally applicable provisions of Regulation T may not require tracking of the purpose of a Loan; see, e.g., 2 Fed. Res. Reg. Serv. 5-615.19). Lender represents and warrants that it acts as principal unless it has given notice to the contrary in writing and agrees, pursuant to Section 10.3(b), to complete and comply with the provisions of Annex I (which sets forth the terms and conditions under which an Agent may act on behalf of one or more Principals). Special representations applicable to Loans involving assets of ERISA Plans are provided in section 18.

Possible Use of Schedule B:
Some parties may wish to consider adding other representations as appropriate, particularly in cases where Lender is a regulated institution.

Section 10: Covenants.
Section 10.1 seeks to assist the parties in obtaining the benefits of certain Bankruptcy Code and Federal Deposit Insurance Act (“FDIA”) protections applicable to participants in securities lending transactions. Parties entering into the Agreement with an insured depository institution should be aware of the written agreement and related requirements under sections 11(d)(9), 11(n)(4)(I), and 13(e) of the FDIA that may apply in the event that the Federal Deposit Insurance Corporation (the “FDIC”) or the Resolution Trust Corporation (the “RTC”) is appointed conservator or receiver. In this regard, the FDIC and the RTC have issued policy statements under which a “qualified financial contract” (such as a loan of securities) will be deemed to satisfy the FDIA’s written agreement and related requirements if (i) it is evidenced by a writing that is sent reasonably contemporaneously with the parties’ agreement to enter into the transaction, (ii) the counterparty relies in good faith on evidence of the insured institutions corporate authority to enter into the transactions, which evidence may consist of a written representation in a master agreement by a vice president or more senior officer of the institution, and (iii) the counterparty maintains copies of records establishing the existence of the writing and the evidence of authority. See FDIC and RTC “Statements of Policy on Qualified Financial Contracts” (Dec. 12 1989). In view of these policy statements, it would be appropriate at a minimum for a party to require, when using the Agreement with a federally insured depository institution, that the Agreement by executed by an officer who is at least a full vice president of that institution.

Section 10.2 and Section 10.3 are convenants that operate in conjunction with the representations in Section 9 and the provisions of Annex I to address issues of principal/agent liability. Section 10.3 provides explicitly that Lender is liable as principal unless it executes and complies fully with the provisions of Annex 1. Pursuant to Section 10.4, upon request, Borrower must furnish Lender with its most recent publicly available financial statements. Under Section 10.5, the parties agree that the Loans are not "exchange contracts" and are not governed by buy-in or similar rules of any self-regulatory organization.

Possible Use of Schedule B:
The Agreement is designed to permit the parties in appropriate cases (e.g., where both parties are Broker-Dealers) to adopt buy-in procedures that may be established by a self-regulatory organization (e.g., the New York Stock Exchange or the National Association of Securities Dealers) or a trade association (e.g., The Bond Market Association or the Securities Industry Association). Such procedures could be specified in Schedule B.

Some parties may wish to consider adding other covenants as appropriate.

Section 11: Events of Default.
The events of default specified in Section 11 (each, individually, a "Default") are designed to be broad, consistent with market practice in this respect. The Defaults in the Agreement encompass the events of default in The Bond Market Association Master Repurchase Agreement as well as other events appropriate to the securities lending context. The non-defaulting party has the option (to be exercised, with some exceptions, by notice) of terminating a Loan upon the occurrence of any Default. This section was drafted to conform in substance to Rule 296 of the New York Stock Exchange.

Sections 12 and 13: Remedies.
Upon the occurrence of a Default, these Sections grant a non-defaulting party the right, in addition to any other rights arising under the Agreement and applicable law, (i) to purchase a like amount of Replacement Securities or Replacement Collateral to replace the Loaned Securities or Collateral it has transferred to a defaulting party, (ii) to take appropriate steps to sell any Collateral or a like amount of Loaned Securities it may hold, and (iii) to apply and set off Collateral or Loaned Securities, and any proceeds thereof (including amounts drawn under a letter of credit supporting any Loan), against the cost of such Replacement Securities or Replacement Collateral and any other obligation of the defaulting party under the Agreement. The defaulting party remains liable to the non-defaulting party for the difference, with interest thereon, between the cost of the Replacement Securities or Replacement Collateral (plus any other amounts due to the non-defaulting party) and the sales price received (or deemed received) by the non-defaulting party for the Collateral or Loaned Securities. As security for the defaulting party's obligation to pay such difference, the Agreement provides the non-defaulting party with a security interest in any property of the defaulting party then held by or for the non-defaulting party and a right of setoff with respect to such property and any other amounts payable by the non-defaulting party. At its discretion, the non-defaulting party may elect, in lieu of purchasing all or a portion of the Replacement Securities or Replacement Collateral or selling all or a portion of the Collateral or Loaned Securities, to be deemed to have made such purchase or sale on the terms specified in the Agreement.

Possible Use of Schedule B:
Sections 12 and 13 provide that the rate of interest on certain amounts remaining due by the defaulting party shall be LIBOR with respect to Foreign Securities and the Federal Funds

Rate with respect to any other securities. Some parties may wish to specify other rates of interest in Schedule B.

Section 14: Transfer Taxes.
Consistent with market practice, this Section obligates Borrower to pay any transfer taxes with respect to the transfer of Loaned Securities.

Section 15: Market Value.
Section 15 establishes the procedures for determining the market value of exchange-traded, OTC, government, and foreign securities for all purposes under the Agreement except the Default provisions. Unless otherwise agreed, the market value of a letter of credit is the undrawn amount thereof.

Possible Use of Schedule B:
Some parties may wish to consider specifying other sources for market value, depending on, e.g., the type of securities they contemplate lending or other relevant regulatory or business concerns.

All determinations of market value under Section 15 include accrued interest (other than interest previously transferred to the other party) except in those limited cases where there is a contrary market practice. Determinations of market value under Section 15 are generally made of the basis of the last sale, quotation, or bide (or other specified criteria) on the preceding Business Day. For purposes of market valuations that must be made at the close of trading on a particular Business Day (e.g., under Section 8), however, market value is calculated by reference to the value of the security at that day's close, not as of the close on the preceding day (by virtue of the second sentence of Section 15.6).

Section 16: Transfers.
Section 16 sets forth the requirements for transfers of cash, securities, and other property under the Agreement. In the case of securities, Section 16 requires the transferor to take all steps necessary to effect a "transfer" under Section 8-313 of the Uniform Commercial Code as Adopted in New York, or, where applicable, under U.S. federal regulations governing transfers of book-entry securities (e.g., 31 CFR (306.115 et seq.). Transfer of securities may be made by physical delivery, transfer on the books of a Clearing Organization, or such other means as Borrower and Lender may agree. Section 16.1 also requires that the transferor provide the transferee with rights under any applicable foreign law that are comparable to those available to a transferee under Section 8-313 or federal book-entry security regulations.

Possible Use of Schedule B:
The parties may wish to specify in Schedule B which methods of transfer are acceptable.

The parties may also wish to develop country-specific provisions governing transfers in order to accomplish the objectives of this Section in accordance with applicable foreign law or regulation.

Section 17: Contractual Currency.
Section 17 defines the Contractual Currency in which payments are to be made. The party entitled to receive a payment may, at its option, accept payment in a currency other than the

Contractual Currency, in which case Section 17 seeks to minimize the exchange risks to which the party receiving payment is subject. Payments made in any currency other than the Contractual Currency discharge the payor's payment obligation only to the extent of the amount of the contractual Currency the recipient is able to purchase with the amount tendered in the other currency. Except in the event of a Default by the payee, the party making payment remains liable for any shortfalls in amounts due in the Contractual Currency, including shortfalls after any judgments or orders against that party in another currency have been converted to the Contractual Currency. If the amount in the Contractual Currency received upon conversion of the tendered currency exceeds the amount due, the recipient, except in the event of a Default by the payor, must refund the difference. The enforceability of these provisions will be subject to applicable law and judicial practice.

Section 18: ERISA.

The objectives of Section 18 are (i) to identify transactions raising potential ERISA concerns, (ii) in the case of any Loan involving ERISA Plan assets, to comply with Department of Labor Prohibited Transaction Exemption 81-6, unless the parties have determined that they wish to rely on another exemption or proceed without an exemption, and (iii) to provide other requirements appropriate to securities lending transactions involving ERISA plan assets.

Under Section 18(b), Borrower represents and warrants that neither it nor any affiliate has discretionary investment authority or control over, or renders investment advice regarding, the assets of the Plan involved in the Loan. As a practical matter, Lender has exclusive access to the information necessary to permit Borrower reasonably to determine its status with respect to investment control over the Plan (and compliance with Prohibited Transaction Exemption 81-6). Consequently, Lender agrees to identify to Borrower at the outset of the transaction any persons with such discretionary authority or control or rendering such investment advice with respect to the assets of the Plan involved in the Loan. In the event Lender fails to communicate and keep current such information, the representation and warranty in Section 18(b) is deemed to be made by Lender rather than Borrower.

Section 19: Single Agreement.

Section 19 establishes that all Loans made under the Agreement are part of the same contractual arrangement and that payments and transfers under all Loans may be netted. In addition, default in the performance of any obligation under any Loan constitutes default under all Loans under the Agreement, and the non-defaulting party may set off claims and apply property held by it in respect of any Loan against obligations owed to it in respect of any other Loan with the defaulting party. It is contemplated that each party will still retain all other applicable legal remedies (e.g., damages as well as any common law or other setoff rights) against a defaulting party. Specific legal advice should always be sought in regard to the availability of right of setoff, particularly in regard to an insolvent foreign entity.

Section 20: Applicable Law.

The choice of New York law is based upon a determination that, among the jurisdictions in the United States, the greatest number of securities lending agreements occur within New York. New York also has an extensive body of commercial and securities law and by statute has indicated that it will respect the parties' contractual choice of law in transactions involving an amount of at least $250,000 (see New York General Obligations Law, ß 5-1401), thus providing market participants with certainty regarding applicable law.

Sections 21-23: Waiver, Remedies, Notices.
Sections 21-23 contain standard provisions regarding forbearance by a party, survival of remedies, and notice procedures typically included in securities lending agreements. Parties should specify proper addresses for notice in Schedule A.

Section 24: Submission to Jurisdiction.
Submission to the jurisdiction of state and federal courts located in New York City is designed to address in particular the possibility that foreign parties using the Agreement might not otherwise be subject to such jurisdiction. The submission to jurisdiction is non-exclusive, so a party may initiate proceeding in any other court of competent jurisdiction.

Section 25: Miscellaneous.
Section 25 contains a variety of provisions customarily contained in agreements of this type. Assignment is not permitted without the prior written consent of the non-assigning party. Although the Agreement may be terminated by written notice, outstanding obligations under the Agreement survive under this Section and under Section 22.

Section 26: Definitions.
Section 26 defines the principal terms used but not elsewhere defined in the Agreement.

Section 26.2 generally defines Business Day on a Loan-by-Loan basis, with a Business Day being a day on which regular trading occurs in the principal market for the Loaned Securities subject to such Loan. This general rule is subject to two specific qualifications relating to market valuations (Section 15) and mark-to-market obligations (Section 8). Because market valuations can most reliably be determined on days on which there is trading activity, a Business Day is defined for purposes of Section 15 as any day on which regular trading occurs in the principal market for the securities whose value is being determined. For purposes of mark-to-market valuations under Section 8, it is important to measure any Margin Deficit or Margin Excess that results from fluctuations in the value of either the Loaned Securities or Collateral. Thus, with respect to Section 8, Business Day means any day on which regular trading occurs in the principal market for any Loaned Securities or for any securities Collateral under any outstanding Loan. In addition, to clarify the timing of Borrower's and Lender's respective obligations to eliminate a Margin Deficit or Margin Excess, "next Business Day" is defined for purposes of Section 8 as the next day on which Collateral could be transferred to the other party in accordance with the Agreement. Saturdays and Sundays are never considered Business Days. (A related provision of the Agreement worth noting in this context, Section 23, provides that notices received on a day on which a party is not open for business will be deemed received on the next day on which such party is open for business.)

The definition of Collateral under Section 26.4 includes (i) any property which the parties agree will be acceptable Collateral before engaging in a Loan and which is transferred to Lender pursuant to Section 3 or 8, (ii) any property properly substituted for such Collateral, (iii) all accounts in which such property is deposited and all securities in which any cash collateral is invested, and (iv) any proceeds of the above. For purposes of return of Collateral by Lender or purchase or sale of securities pursuant to the remedies provisions of the Agreement, Collateral includes securities of the same issuer, class, and quantity as the Collateral initially transferred by Borrower to Lender. For definitional purposes only, letters of credit mutually acceptable to Borrower and

Lender are treated as Collateral, although they are a form of credit support that is not "collateral" under commercial or bankruptcy law.

The definition of "Foreign Securities" in Section 26.10 turns on the location where securities are principally cleared and settled. This approach is designed to facilitate the practical application of the definition by permitting the parties readily to determine whether particular securities are "Foreign Securities."

The definition of LIBOR is a standard definition, based on the Reuters Screen LIBO page.

Possible Use of Schedule B:
If the parties wish to use the reference bank method of calculating LIBOR, they may amend the LIBOR definition by using Schedule B.

III. Annex I

Annex I adapts the terms of the Agreement to govern a securities loan relationship between a Borrower and a bank or other entity acting as Agent for one or more Principals. Annex I addresses a number of practical and legal issues in this context, to some extent breaking new ground by dealing explicitly with certain issues that have not been addressed in similar agreements currently used in the market. In light of the potential ambiguity regarding when an Agent is liable for its Principals' obligations, the central objective of Annex I is to assist parties entering into securities loan transactions in determining who, as between the Agent and its Principals, is liable for performance under the Agreement. Annex I has been prepared in consultation with a number of Agent banks and representatives of Robert Morris Associates, but no endorsement of Annex I by any of these entities is implied.

Section 1: Additional Representations and Warranties.
Under Section 1, the party acting as Agent represents and warrants, in addition to making the representations and warranties in the Agreement, that its Principal has authorized it to execute and deliver the Agreement, to enter into Loans and to perform the obligations of Lender thereunder. This is a standard representation in agency transactions in the securities markets generally.

Section 2: Identification of Principals.
Pursuant to this Section, Agent agrees to provide Borrower, prior to any Loan under the Agreement, with a written list of Principals for whom it intends to act as Agent and to inform Borrower, no later than the close of business on the next Business Day after a Loan is agreed upon, of the specific Principal or Principals for whom it is acting. Such disclosure protects both Borrower and Agent. Borrower comes to "know its counterparty" (a particularly important fact in the event the counterparty is an ERISA Plan). Agent's identification of its Principal or Principals also plays an important role in achieving a release of Agent from liability under Section 10.3 of the Agreement and traditional common law rules governing transactions by an Agent on behalf of undisclosed or partially disclosed Principals. If Agent fails to identify the Principal or Principals prior to the time provided, or if Borrower determines that the Principal or Principals so identified are not acceptable, Borrower may reject and rescind the Loan. In this event, the parties must retransfer any Collateral or Loaned Securities that have changed hands. To the extent that either party has performed under the Loan prior to such rejection, that party is entitled to any applicable fees or other amounts that would otherwise have been payable in respect of such performance.

The Bond Market Association understands that some securities lending Agents do not currently identify their Principals on a Loan-by-Loan basis and may not wish to do so in the future. In such cases, the parties may wish to modify Annex I, through Schedule B, to reflect their agreement not to identify Principals on a Loan-by-Loan basis. This determination, however, will have important potential credit (and ERISA) implications. In particular, if Agent does not identify its Principals on a Loan-by-Loan basis, Borrower effectively must assume that Agent is acting for the least creditworthy Principal on the list of permissible Principals agreed upon in advance. In addition, Borrower and Agent must agree upon how the mark-to-market obligations and the rights of the parties in the event of a Default will be implemented (If a Default has occurred with respect to one Principal, can all Loans entered into with Agent be terminated? If not, should it not be made clear that all transactions will be marked to market on a Loan-by-Loan basis, since setoff rights might otherwise be adversely affected?) Parties that elect not to adopt the approach set forth in Section 2 of Annex I likely will find it highly desirable to address each of the foregoing issues, as well as related regulatory and legal concerns that may arise where Agent's Principals are not identified on a Loan-by-Loan basis.

Section 4(c) of Annex I, as discussed below, addresses these issues in cases where Agent agrees to identify its Principals on a Loan-by-Loan basis, but is not able or does not wish to inform Borrower of the specific dollar amount of each Loan applicable to each Principal.

Section 3: Limitation of Agent's Liability.

This Section sets forth the general rules limiting Agent's liability under the Agreement. Where Agent has, through compliance with the provisions of the Agreement, taken the steps necessary to permit Borrower to assess the creditworthiness of its Principal or Principals, Agent's obligations do not include a guarantee of performance by its Principal or Principals, and Borrower's remedies do not include a right of setoff with respect to any obligations between Agent, acting for its own account, and Borrower.

Section 4: Multiple Principals.

When an Agent acts on behalf of multiple Principals, the Agreement presumes that the Loans will be treated as multiple transactions on behalf of separate Principals, unless the parties agree in writing to treat the Loans as if they were transactions by a single Principal.

If the parties agree to treat the Loans as separate transactions, Agent must specify the portion of each Loan allocable to each Principal, the portion of any individual Loan allocable to each Principal shall be deemed a separate Loan under the Agreement, the mark-to-market obligations under the Agreement will be determined on a Loan-by-Loan basis (unless the parties agree to determine them on a Principal-by-Principal basis), and the remedies upon a Default will be determined as if Agent had entered into a separate Agreement with Borrower on behalf of each of its Principals. Any transactions by Agent on behalf of separate Principals and are marked to market on a Loan-by-Loan basis.

If the parties agree to treat Loans as if they were transactions by a single Principal, Agent must specify the names of the Principals (but not the portion of the Loan allocable to each Principal), the mark-to-market obligations under the Agreement will be determined on an aggregate basis for all Loans entered into by Agent on behalf of any Principal, and the remedies upon a Default will be determined as if all Principals were a single Lender.

Section 5: Interpretation of Terms.

This Section sets forth a general rule of construction for the term "Lender" in the Agreement in the context of agency transactions, subject to the limitation of an Agent's liability in Section 3 of Annex I. This Section explicitly acknowledges that each Principal has the rights, responsibilities, privileges, and obligations of a "Lender" that enters directly into Loans with Borrower, and that Agent has been designated as the sole agent of each Principal for performance of Lender's obligations to Borrower and for receipt of performance by Borrower of its obligations to Lender. The terms "party" or "either party" are deemed to refer to both Agent and Principal, including, inter alia, in the context of Defaults. The effect of this construction of the term "party" is that a bankruptcy or similar Default by Agent will also be deemed a Default by Principal.