TEIGLAND-HUNT LLP

CLIENT ALERT
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Eurozone Contingency Planning: ISDA's Illegality/Force Majeure Protocol

- *In response to Eurozone concerns, ISDA recently published its Illegality/Force Majeure Protocol, which is now open for adherence.*
    - *What It Does: This Protocol enables **parties to 1992 ISDA Master Agreements** to incorporate the illegality and force majeure provisions of the 2002 ISDA Master Agreement.*[1]
    - *Why: This Protocol is intended to provide parties transacting under 1992 ISDA Master Agreements with improved remedies should the Eurozone crisis result in either the **imposition of exchange controls** in a member state (e.g., following its withdrawal from the Eurozone/replacement of the euro with a new national currency) or other legal developments that might render it illegal or impracticable for a party in a member state to fulfill its scheduled payment or delivery obligations in respect of OTC derivatives transactions.*
    - *When/How to Adhere: There currently is **no cut-off date** for adherence to this Protocol; however, ISDA reserves the right to designate a cut-off date by giving 30 days' notice on its website. In order to adhere to this Protocol, a party must submit an adherence letter to ISDA in accordance with the Protocol's procedures.*

Overview

The ISDA Illegality/Force Majeure Protocol (the "Protocol") offers market participants an efficient way to amend their 1992 ISDA Master Agreements to incorporate the more refined Illegality Termination Event and additional Force Majeure Termination Event provisions of the

[1] Capitalized terms used in this Client Alert that are not otherwise defined have the meanings specified in the relevant ISDA Master Agreement.

2002 ISDA Master Agreement. In doing so, the Protocol is intended to give parties improved means of addressing issues that might arise if the Eurozone crisis were to result, for example, in (i) the imposition of exchange or other forms of capital controls in a member state following a withdrawal from the euro and the creation of a new national currency, (ii) the declaration of additional bank holidays to give time to effect the withdrawal and a redenomination of euro obligations into a new national currency, or (iii) other developments that might prevent parties in an affected member state from performing their scheduled obligations under existing OTC derivatives transactions.

This Protocol is part of ISDA's ongoing Eurozone contingency planning effort, and its development was formally announced as part of ISDA's May 25, 2012 Eurozone Contingency Planning Update.[2]

Benefits of Adherence to ISDA's Illegality/Force Majeure Protocol

Refined Illegality Provision

Many observers believe that the approach taken to the Illegality Termination Event in the 2002 ISDA Master Agreement is an improvement over the corresponding provision in the 1992 ISDA Master Agreement. The key changes and benefits of the Illegality provision contained in the 2002 ISDA Master Agreement include:

- **Preservation of Transaction-specific fallbacks.** The 2002 version clarifies that provisions in the Master Agreement addressing illegality may only be invoked after any transaction-specific fallback provisions have been taken into account.

- **No obligation to transfer Transactions.** The 2002 version removes the obligation to attempt to use all reasonable efforts to transfer Affected Transactions to another Office or Affiliate of a party before relying on the Illegality Termination Event. In practice such a transfer can be difficult to achieve and may delay termination for up to 30 days under the 1992 ISDA Master Agreement. The 2002 version allows parties to terminate Affected Transactions sooner by eliminating the obligation to attempt a transfer over a specified period.

- **Waiting Period.** In certain circumstances the 2002 version provides for the deferral of payments and deliveries during a waiting period before termination

[2] See ISDA's Eurozone Contingency Planning page at http://www2.isda.org/functional-areas/legal-and-documentation/eurozone-contingency-planning/.

may take effect.[3] The waiting period allows an opportunity to wait and see whether the event giving rise to termination rights might be resolved.

Incorporation of an Express Force Majeure Provision

- Although the 1992 ISDA Master Agreement addresses illegality as a Termination Event, it does not expressly address other types of force majeure or act of state events. Without the benefit of this Protocol, parties to the 1992 ISDA Master Agreement could be left having to rely on limited common law remedies upon the occurrence of a force majeure/act of state event and would not have an express right to terminate or claim a termination payment in respect of Transactions that are affected by such an event.[4]

Conclusion

Market participants should consider whether their trading documentation adequately addresses the issues that are the subject of this Protocol as well as other potential Eurozone events.

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If you have any questions regarding Eurozone contingency planning or ISDA's Illegality/Force Majeure Protocol, please contact one of the following:

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[3] The concept of a Waiting Period also applies in relation to the Force Majeure Termination Event. Where it applies, the Waiting Period in the case of Illegality is three (3) Local Business Days; in the case of Force Majeure, it is eight (8) Local Business Days.
[4] It should be noted in this regard that, under New York law, if a contract does not contain a force majeure clause, the affected party may not be excused from performance as a result of an unanticipated event unless it can invoke the more limited common law doctrine of impossibility.

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