JULY 2024

GMRA Handbook

An introductory professional reference to GMRA 2011 anchored in the repo transaction life-cycle

frontclear
financial market development

Disclaimer

The information in this GMRA Handbook is for education purposes only and is not intended to be considered as legal advice. When entering into a GMRA, the input of a qualified lawyer is required.

I. GMRA handbook

This handbook has been written for non-lawyers who need to understand how the GMRA governs the start, end and intervening life-cycle of a repo, both day-to-day and in exceptional circumstances. However, the handbook is also intended to be useful as an introduction for new lawyers, or lawyers in new markets, who have no experience of master agreements but who have been tasked for the first time with negotiating and documenting repos under the GMRA 2011.

Before reading this handbook, the reader should familiarise themselves with the type of transaction that the GMRA is designed to document, in other words, they need to understand what repo is and how it works. An introduction to repo follows. Instructive resources about repo, in document and video formats, can be found both on the Frontclear Academy and on the ICMA website.

Understanding repo

Developing both onshore local currency markets and global offshore funding markets, are important facilitators for domestic financial development in support of economic growth, poverty alleviation and financial resilience. A developed onshore swap and repo market will ensure that domestic and global counterparties are able to perform risk management and fulfil funding needs.

Because repo is low risk — as a result of being collateralised, insulated from the statutory insolvency regime, able to benefit from close-out netting in default and protected by the GMRA — it is a source of cheap cash. Cheap cash from repo makes low-margin but essential activities such as market-making in securities viable and is therefore vital to secondary bond market liquidity. The cash borrowed in repo is often used to finance long positions in securities that are used to hedge other securities and derivatives. Consequently, the repo rate is a key factor in the pricing of these instruments. As a secure means of borrowing and lending, repo also plays a key role in the development of the domestic local currency money markets. It facilitates funding and liquidity management by banks and allows investors to cover temporary cash shortfalls without having to permanently sell off and later repurchase securities in their investment portfolios.

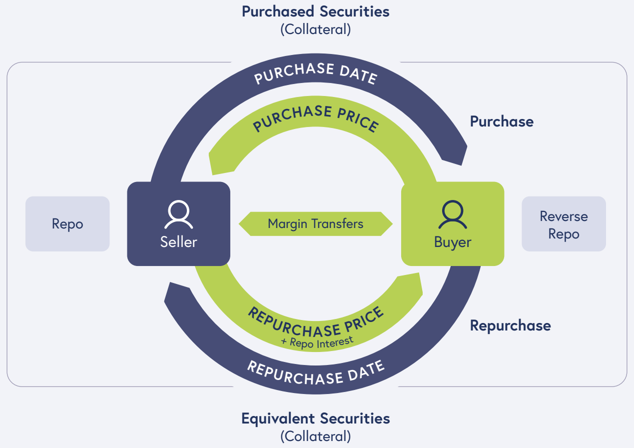
The definition of a repo — which is an abbreviation of "repossession" (the idea of giving and taking back) — is a sale of an asset and a simultaneous commitment to repurchase the same or a similar asset at the sale price plus a premium. The premium is informally called "repo interest". It represents a return on the use of the cash proceeds. The most common type of asset sold and repurchased in repo is a fixed-income security, usually a government bond. The asset sold and repurchased in a repo is usually called the "collateral". This is legally incorrect, as that term strictly-speaking only applies to what is pledged in a secured loan, but it is nevertheless widely used in the repo market. In practice, in the case of a collateral security, "the same or a similar" typically means part of the same issue, a security with the same ISIN as that sold.

Repo vs pledge

Notwithstanding the economic reality that a repo is equivalent to a secured loan, from a legal point of view a repo involves "true sales" of securities from one party to the other, meaning that title to the securities is transferred. The buyer is owner of the securities during the life of a repo and, if the borrower defaults or at any other time, can immediately sell the collateral.

In a secured loan, the cash borrower pledges collateral in the form of an intangible movable asset. The collateral is encumbered to secure the transaction on behalf of the lender of cash. In an event of the borrower defaulting, the lender will try to seize and liquidate the collateral, but access is likely to be subject to restrictions including a stay of enforcement on the rights of the lender while the insolvency process is in progress.

The party selling collateral in exchange for cash at the start of a repo is called the seller and the other party is the buyer. The seller may be said to sell or "repo out" collateral. The buyer may be said to buy or "reverse in" collateral and to be transacting a **reverse repo**. Reverse repo is also used by most central banks as a secure means to refinance the money market in open market operations to control interest rates. The repo market is thus central to monetary policy transmission.



The reason why a repo transfers collateral by sale (transfer of legal title) rather than providing collateral through the traditional method of creating a security interest (such as pledging the collateral) is that, by giving the cash lender ownership of the collateral from the start, a repo:

- Avoids the collateral becoming subject to the statutory insolvency regime in the event of one of the parties becoming insolvent, which would be the case with a security interest. Statutory insolvency processes are typically slow, uncertain and expensive, and therefore unsuitable for short term transactions like repo.
- Allows the buyer to use the collateral at any time. For example, the buyer can refinance during the life of a repo in the event of an unexpected liquidity need. The buyer could also trade the collateral for profit, if such an opportunity arose.
- Allows close-out netting of mutual obligations in the event that a party defaults. This swiftly reduces gross exposures between the parties to a much smaller single net amount. This is vital for a transaction like repo, which is traded in large volume and would be exposed to the volatility of the market price of the collateral while a default is being resolved, making it difficult to hedge the exposure to a defaulting counterparty.

Repurchase transaction vs buy/sell-back

A buy/sell-back (or sell/buy-back) is another type of repo, in addition to the repurchase transaction (which is sometimes called a "classic repo"). The key difference with a repurchase transaction centres on the consequences of a coupon or dividend payment.

- In the case of a repurchase transaction, the buyer is contractually obliged to make an immediate equal payment to the seller. This payment is widely known in the market as a "manufactured payment".
- In the case of a buy/sell-back, no manufactured payment is triggered. Instead, when negotiating a buy/sell-back, the parties agree to reduce the repurchase price of the transaction by the amount of the scheduled coupon plus some reinvestment income. In other words, the seller pays less to repurchase. The reinvestment income is to compensate the seller for the fact that he will not receive the benefit of the coupon or dividend until the repurchase date, which is later than the coupon or dividend payment date on which a repurchase transaction would pay a manufactured payment.

Note that all repurchase transactions are documented but buy/sell-backs have historically been undocumented (see buy/sell-back annex to the GMRA).

II. The GMRA

The GMRA is a model contract for documenting the terms and conditions of repos executed directly between two parties. The GMRA is the most widely-used repo contract in the world. It was originally created for cross-border repo in Europe but is now also employed for cross-border business globally and to document domestic transactions in an increasing number of emerging markets and in the lion's share of developed markets.

The GMRA is an example of a type of contract called a standard master agreement. A master agreement is often described as a framework agreement. This means it records generic terms and conditions for a certain class of financial transaction which two parties intend to execute with each other from time to time. In the case of the GMRA, that class of transaction is repo. A standard master agreement is a template that is intended to be the basis of all business in a certain class of financial transaction in a particular market.

Widespread usage yields network economies of scale by reducing the need for completely fresh legal analysis when executing an agreement with a new counterparty. A standard master agreement also helps to harmonise the rights and obligations of parties. This ensures that, when a party buys from one counterparty and makes a matching sale to another, it is not exposed to any inconsistency in its legal position in one transaction compared to the other. For example, the payment obligations in one transaction will be the mirror of the payment obligations in the other. In addition, where two parties buy and sell from each other, a standard agreement ensures that these exposures are contractual mirror images, which facilitates efficient netting, particularly in the event of a default by one of the parties.

Of course, a standard master agreement cannot document every possible type of transaction between every possible type of counterparty in every possible set of circumstances. The terms and conditions in a master agreement must therefore cover the most commonly-transacted variant of a particular class of financial instrument. The particular variant of repo that is documented in the GMRA is:

- the type of repo called a repurchase transaction;
- between two professional counterparties (that is, market intermediaries such as banks or securities brokers or dealers);
- for a short term-to-maturity (less than one year but usually much shorter);
- collateralised with a simple and/or low-risk asset (typically, a domestic government fixed-income security);
- collateralised with an asset which pays coupons or dividends gross of withholding tax (that is, without deduction of tax before payment); and
- governed by the laws of and subject to the exclusive jurisdiction of the courts of England and Wales.

To accommodate less common and more complex variants of repos, users need to make amendments to the standard agreement. Some variants common to emerging and developing markets that would require such amendments include:

- the alternative form of repo called a buy/sell-back;
- repos against securities paying coupons or dividends net of withholding tax; and
- repos not governed by the laws of and/or not subject to the exclusive jurisdiction of the courts in England and Wales.

Two consequences of the fact that the GMRA is designed to govern repos between two professional counterparties against a simple, low-risk asset which pays coupons or dividends gross are that the GMRA deliberately lacks:

- dispute-resolution mechanisms, which are seen as unnecessary, given that professionals are more likely to seek to resolve disagreements between them by negotiation, in order not to jeopardize established business relationships, and that disputes are less likely over repos of simple collateral; and
- anything other than basic tax provisions, given that the typical collateral is a government bond, on which coupons are usually (although with some major exceptions) paid gross of withholding tax.

The legal rights and obligations of the contracting parties laid out in the GMRA include important risk and operational management procedures, such as how variation margin should be calculated, what should happen when a coupon, dividend or other income is paid on collateral during the term of a repo and how to terminate a repo where there is an option to do so. These operative provisions are essential reading for non-lawyers such as traders, risk managers and operations teams. Relevant tutorials, courses and resources available on the Frontclear Academy.

Legal opinions

ICMA annually commissions legal opinions from expert counsel on the enforceability of the standard (English law) GMRA in over 65 jurisdictions, although only for its members. The core questions addressed in a legal opinion on the GMRA concern the ability to give collateral by title transfer and the enforceability of close-out netting against an insolvent counterparty.

Annually-updated legal opinions meet the requirement under the Basel rules, which states that, in order for the mitigation of credit risk by collateralization to be recognized for the purpose of capital calculations (capital relief), institutions must have a demonstrably well-founded confidence on the enforceability of contracts based on up-to-date analysis.

Where a country is awarded a positive opinion in a legal opinion, there is opportunity to develop the cross-border repo market by adopting the standard GMRA, allowing parties to focus on market development versus costly review of bespoke legal documentation.

Where the standard GMRA is to be used to document a repo which involves an element foreign to England and Wales — for example, a counterparty located or collateral issued in another country — it is essential for the contracting parties to seek expert opinions from qualified legal counsel on the enforceability of English law contracts and English court judgements in the relevant foreign jurisdictions.

Where the governing law of and jurisdiction over the GMRA has been changed from English law and the English courts, ICMA's legal opinions will not apply.

III. GMRA architecture

Like master agreements for other markets, the GMRA has three layers:

1 Pre-printed Form

This is the text that you are able to download from the ICMA website. The **pre-printed form** is the core of the standard GMRA in that it lays out, in detail, the terms and conditions listed in section II.

This should never be edited, as it would make it difficult for each party to identify amendments proposed by the other during negotiation. Instead, amendments should be made in Annex I.

Generic to Market

2 Annexes

Annexes I and II are attached to the pre-printed form but other annexes are published as separate documents. Annexes are off-the-shelf standardised amendments designed to accommodate the most common variants of the type of repo documented in the pre-printed form and are applied by making references to them in Annex I.

Buy/Sell-back Annex | Agency Annex | Equity Annex | Other Annexes

Annex I (entitled Supplemental Terms and Conditions) is pivotal to the operation of the GMRA. It has two parts:

- Part I is a list of basic questions that must be answered by the parties and of options that must be switched on or off (elections), if the GMRA is to function.
- Part 2 is a miscellany. It contains amendments needed to accommodate forward repos. It is also where any bespoke amendments to the pre-printed form should be recorded (in other words, amendments that are not available in the form of other annexes).

Annex II represents an exception to the definition of annexes as amendments to the pre-printed form. Its role is to provide an example of a short-form confirmation (in other words, a confirmation that refers to — rather than repeats — the terms and conditions in the pre-printed form). Parties are free to use or ignore Annex II when constructing confirmations. Note that the mandatory minimum content of a confirmation is actually set out in paragraph 3 of the pre-printed form.

Other annexes can be divided into what can be called product or country annexes. A country annex typically amends or adds to the list of Acts of Insolvency in the GMRA in order to capture all local insolvency legislation and to ensure consistency with local definitions. It sometimes changes the governing law and jurisdiction to local law and courts, where a new repo market has adopted the GMRA as their local standard.[1] This raises questions as to how well an English law construct such as the GMRA, and the concepts it contains, are compatible with local law, and whether local courts have the experience to interpret what is likely to be an unfamiliar agreement governing an unfamiliar contract in a way that gives sufficient legal certainty to persuade market participants to transact under a GMRA governed by local law and courts. Cross-border parties to such agreements need to seek expert legal advice on whether these foreign-law versions of the GMRA are safe to use.

Mandatory requirements to use the local law jurisdiction and language in contracts would be an additional complication, given the legal risks and risks in interpretation and translation, particularly of legal concepts.

Anyone is free to draft a country annex but only those drafted by ICMA, or those drafted by others and formally adopted by ICMA, are published on its website[2] and covered by the legal opinions on the enforceability of the GMRA published and updated annually by ICMA (the role and importance of legal opinions is explained on page 5).

While there are a number of **product annexes** to the GMRA 2011, the most relevant to emerging and developing markets is the Buy/Sell-Back Annex, which applies where the repo takes the form of a buy/sell-back.

Specific to Relationship

3 Confirmations

This is the third layer of the GMRA. They are a type of post-trade message which at least one party should send to the other in order to provide, at a minimum, a record that can be checked of the terms and conditions of a transaction (other than those standard provisions in the pre-printed form) and the details of agents and accounts to be used to settle the transaction.

Confirmations perform three functions:

- In substance, they list the economic terms of a repo, such as purchase price, repo rate and term, as well as settlement details such as account names and numbers.
- Legally, confirmations bring together individual repos between two parties under the same GMRA to create a single position in each currency and in each issue of securities given as collateral, for purposes such as: settlement; the calculation of variation margins; and the termination of outstanding repos after a default by one of the parties.
- Whereas annexes are used to customise the GMRA to accommodate common variants of the standard type of repo that is enshrined in the pre-printed form, confirmations can be used to customise the GMRA (and any applicable annexes) but only in respect of the individual transaction being confirmed. Accordingly, terms and conditions in confirmations override any conflicting provisions in the pre-printed form or annexes.

The GMRA requires that a confirmation should be sent by one or both parties promptly after execution and that the confirmation should be checked promptly by the receiving party or parties. It does not define "promptly" but market best practice is to interpret this as meaning confirmation by the end of the transaction date. Prompt checking of confirmations is prudent. This is because the confirmation (together with the pre-printed form) constitutes prima facie evidence of the terms of a transaction, unless there is a prompt objection by the other counterparty that is supported by contrary evidence. And, as noted, confirmations override any conflicting provisions in the pre-printed form or annexes, so it is important to ensure that any such amendments in the confirmation have been agreed.

ICMA also publishes **templates of notices** that parties may have to deliver to each other under the terms of the GMRA:

- to confirm amendments to an existing GMRA or to a confirmation;
- for the buyer to give notice to the seller of his intention to exercise the so-called "mini close-out" remedy in respect of a repo on which the seller has failed to return collateral on the Repurchase Date (provision 15 of the table below); and
- to give notice to terminate a GMRA.

Specific to Transaction

1 From this point, for convenience, reference will be made to English law and English courts but should be taken to mean the laws and courts of England and Wales.

2 Country annexes to the GMRA 2011 that are currently published on the ICMA website (as at the date of this handbook) are: Canadian, Italian, Japanese, Russian Annexes. There are also country and product annexes to the GMRA 2000, including those used in Australia.

IV. A standard GMRA

The table lists the terms and conditions of the GMRA's pre-printed form in a typical operational sequence. The table deals with the execution of a repo, from pre-trade through repurchase settlement, management of the transaction collateral through the life-cycle and what happens following a default by one of the parties. The table sections are organized per the illustration below and each highlights and explains key provisions and identifies the paragraphs of the GMRA where each provision appears. It is suggested that the reader has the pre-printed form to hand and consults the actual text of each paragraph of the agreement as they read through the table.

GMRA reference table and the Repo Lifecycle

Repo	Pre-trade Origintation and negotiation	Trade Execution	Post-trade Verification	Settlement Purchase	Life-cycle Management of transaction and collateral	Settlement Repurchase
GMRA table provisions	1	12	13	14		15
	2			16		
	3			17		
	4				18	
	5				19	
	6				20	
	7				21	
	8				22	
	9				23	
	10				24	
	11					

Pre-trade
ORIGINATION AND NEGOTIATION

1 what transactions are governed by the GMRA?

Repos under the GMRA include both **repurchase transactions** and **buy/sell-backs**, although these are neither defined nor differentiated. 1(b)

Buy/sell-backs only come within the scope of the GMRA if their potential use has been pre-agreed by the parties and this agreement has been recorded in Annex I(1)(a), in which case, the **Buy/Sell-Back Annex** would automatically apply whenever a repo is identified as a buy/sell-back when being negotiated. 1(c)(i)

A repo is described as involving Seller selling and Buyer buying "securities or other financial instruments" provided these are not **equities** or **Net Paying Securities** (see the definition of Net Paying Securities in provision 1.1). 1(a)

The exclusion of equities is intended to prompt the parties to apply the Equities Annex.

The exclusion of Net Paying Securities is to protect the Buyer from paragraph 6(b) and the second clause of paragraph 5(b), which require Buyer to compensate Seller for any tax deduction when making onward payments to Seller (these tax "**gross-up**" clauses also apply to securities given as margin — see provision 20.2). However, Net Paying Securities may be included under the GMRA, if expressly pre-agreed by the parties and that agreement is recorded in Annex I(1)(b). 6(b) 5(b)

1.1 definition of **Net Paying Security**

This is GMRA terminology for a security in respect of which any **Income** that is paid by the issuer of a security to Buyer during the life of a repo (see the definition of Income in provision 1.2) which would trigger a **manufactured payment** by Buyer to Seller that would be subject to withholding tax (see the definition of manufactured payment in provision 19). 2(hh)

1.2 definition of **Income**

This is GMRA terminology for: 2(y)

- all payments of coupons, dividends and other **Distributions** on collateral securities paid by the issuer to Buyer or, on securities given as margin and paid by the issuer to the margin-holder;
- manufactured payments triggered by income payments on securities and made by Buyer to Seller or by a margin-holder to the margin-giver.

Broadly speaking, a "Distribution" is a payment of income such as interest. 2(q)

1.3 ensuring **transfer of title**

Each party is required to take all necessary steps to ensure that all **right, title and interest** in any securities delivered to the other party are free of all liens, claims, charges and encumbrances (except liens granted to securities settlement systems — these are often used to secure intraday credit extended by system operators to a party to fill temporary shortfalls in cash in order to allow the settlement of a particular transaction to proceed. 6(e)

It is made clear in the GMRA that the intention of the parties is to deliver all right, title and interest in securities or cash, notwithstanding any terminology in the GMRA which might be construed as suggesting the repo is a secured loan. 6(f)

This is a fundamental obligation in the GMRA, given that title transfer is of the essence to the working of a repo.

2 **authority** to execute a transaction

Each party makes representations (statements of fact) to the other to provide assurance about its legal and professional ability to sign a GMRA, to transact repo and to take the risk on such transactions. Such assurances are intended to give each party confidence that the other will not try to renege on any loss-making transactions by claiming it was acting beyond its powers or had relied on advice from the other party. The standard representations by each party are:

- It has the authority to sign the GMRA, to execute transactions and to perform the consequent obligations under the GMRA. 9(a)
- Other than transactions for which it expressly declares that it is acting as an agent for a third party, it will be acting as a principal. 9(b)
- Any person signing the GMRA and executing a transaction on its behalf will have been given due authorisation to do so. 9(c)
- It has obtained all official authorisations required to execute repo and confirms that such authorisations are still in full force and effect. 9(d)
- The execution, necessary deliveries and other actions will not violate any applicable law or regulation or agreement by which it or any of its assets are bound. 9(e)
- It has and will continue to satisfy itself about the tax implications of its transactions. 9(f)
- Absent a written agreement to the contrary and excepting the other party's representations, it is not relying on advice from the other party. 9(g)(i)
- It has and will continue to make its own decisions about transactions, based on its own judgement and any professional advice it has sought. 9(g)(ii)
- It understands the terms, conditions and risks of each transaction and is willing to assume those risks. 9(g)(iii)
- When delivering securities to the other party, it will ensure that it has the full right to make such a delivery. This means that it is able to give all **right, title and interest** in these securities, free of all liens, claims, charges and encumbrances. The only exceptions are liens granted to securities settlement systems — these are often used to secure credit extended by system operators to a party in order to facilitate settlement by extending intraday credit to fill temporary shortfalls in cash. 9(h)
- On the date that a new transaction is executed, each party will be deemed to have repeated all its representations under the GMRA. 9(h) final clause
- Notwithstanding any arrangements with third parties (e.g. triparty agents), it accepts that it is liable as principal for its obligations under each transaction.

3 **Governing Law**

The GMRA and any related non-contractual obligations (e.g. the accuracy of representations) are governed by the laws of England and Wales. 17 first clause

The courts of England and Wales have **exclusive jurisdiction** of all disputes related to the GMRA, including those not relating to contractual obligations, and the parties irrevocably submit to the jurisdiction of the English courts. This provision is intended to avoid the uncertainty that would be engendered by "jurisdiction shopping", that is, parties being able to litigate in a jurisdiction of their choice which is likely to treat them more favourably. 17 second clause

Each party should appoint an **agent for service of process** in England and record the name in Annex I. The purpose of this agent is to receive documents on behalf of the party that are required for litigation in England and Wales. 17 third & fourth clauses

Should a party fail to appoint an agent, the other party is entitled to appoint one on behalf of the first party. 17 fifth clause

Each party must deliver to the other, within 30 days of the GMRA being signed, proof of acceptance of appointment by the agent named in Annex I and, in the case of the appointment of a new agent, within 30 days of appointment.

If the governing law has been changed from English law, an agent for service of process will not be required.

4 No waivers

If a party expressly or (by inaction) implicitly waives an Event of Default, this would not constitute a waiver of any other Event of Default.	18
If a party does not exercise an available remedy under the GMRA, this would not constitute a waiver of its right to exercise any other remedy.	
No modification or waiver of any provision of the GMRA, and no consent to a departure from any provision, would be effective unless made in writing and duly executed by both parties.	

5 Waiver of Immunity

Each party waives, to the fullest extent permitted by applicable law, all immunity from jurisdiction to which it might be entitled in any action or proceeding relating to the GMRA or any repo in the courts of England or elsewhere.	19
This provision only applies where one of the parties has sovereign immunity.	

6 Third Party Rights

This paragraph abrogates third party rights to enforce contractual provisions which are available under English law. This is to protect close-out netting from interference by third parties but is not relevant outside England and Wales.	21

7 Single Agreement

The parties agree that a portfolio of repos under the GMRA constitutes a single business and contractual relationship, and that each transaction is made in consideration of each other transaction. Accordingly, a default in the performance of any obligation in relation to one repo would constitute a default on all repos and payments. Similarly, deliveries and transfers made in respect of one repo are deemed to have been made in consideration of all payments, deliveries and transfers in respect of all repos.	13
This clause is intended to prevent a liquidator from "cherry-picking" profitable repos and rejecting loss-making transactions. He must accept or reject all the repos under a GMRA.	

8 Non-assignability

Except in the case of a close-out amount, neither party may alienate (that is, give away or sell) its rights or obligations under the GMRA, or under any repo, without the prior written consent of the other party.	16(b), 16(a)
This provision is to protect the efficacy of close-out netting by maximising the assets and liabilities to be included.	

9 change in **tax treatment or tax regime**

This paragraph applies if one party notifies the other that, in its reasonable opinion, it will suffer a material adverse effect in relation to a particular transaction as a result of a court action by a tax authority or a change in the fiscal or regulatory regime (but not a change in the rate of an existing tax).	11(a)
If requested, the party giving notice must provide a supporting opinion from a qualified adviser.	11(b)
The party claiming the adverse effect of a tax event may give notice of not less than 30 days that it wishes to terminate the affected repo. In doing so, it is deemed to indemnify the other party against any reasonable or legal and other professional expenses incurred as a result of termination but not against any consequential (further) loss or damages.	11(c) 11(e)
However, if the other party wishes to retain the repo, it may over-ride the termination notice by giving a counter-notice but, in doing so, will be deemed to have indemnified the party seeking termination against the tax loss.	11(d)

10 **urgency** of performance

Time is said to be of the essence in the GMRA. However, important provisions in the GMRA have specific deadlines attached.	6(g)

11 **termination of the GMRA**

Either party may terminate the GMRA by giving written notice to the other.	16(c)
Notwithstanding notice of termination, any repos outstanding at the time of notice remain subject to the terms of the GMRA until they mature or have been terminated.	16(d)
Remedies being exercised by one party following failure by the other to perform obligations will remain in place after the termination of the relevant repo or of the GMRA until satisfied.	16(d)

Trade
EXECUTION

12 **execution** of a transaction

This can be agreed orally or in writing (see the definition of writing in provision 12.1).	3(a)
The basic details of a repo that need to be agreed in order to form a contract are listed in provisions 12.4 to 12.15.	

12.1 definition of **writing**

All written notices must be in English and must be delivered using any of the four methods of communication specified in paragraph 14(b).	14(a)(i)-(ii) 14(b)(i)-(iv)
Electronic messaging, such as e-mail, is expressly included in the definition of writing, except for giving notice of a waiver of rights (see the definition of waiver in provision 19). Notice of waivers must be sent on paper or by fax.	2(s) 2(yy) 18

12.2 permissible written **communication** with a counterparty

All written notices must be sent to the addressee and address in Annex I(1)(n).	14(a)(iii)
Addresses can subsequently be changed by written notice.	14(d)
Notices are only effective if received or delivered while commercial banks are open in the place of delivery (that is, during the banking business day).	14(b) last clause

12.3 **recording** oral communications

The parties agree to permit the electronic recording of conversations between them.	20
The recordings would be available as evidence where, for example, a dispute arises about the terms of a repo negotiated over the telephone.	

12.4 **list of questions** to be addressed

See Annex 1: Applying Annex 1 when negotiating a GMRA (pre-trade).

12.5 definition of **value date**

The date on which cash and securities are first due to be exchanged between the parties is called the **Purchase Date**.	2(mm)

12.6	definition of **maturity date**	
	The date on which the Repurchase Price is due to be paid by Seller to Buyer and, in exchange, collateral securities are due to be delivered by Buyer to Seller, is called the **Repurchase Date**.	2(qq)
12.7	definition of **duration** of repo	
	The number of days between the Purchase Date and the Repurchase Date is called the **Term** of a repo.	2(uu)
12.8	definition of **securities** to be delivered by Seller on value date	
	The securities given by Seller to Buyer on the Purchase Date, which are called "collateral" in the market, are called the **Purchased Securities** in the GMRA. This is in order to distinguish these securities from **Equivalent Securities**, which are those to be delivered by Buyer back to Seller on the Repurchase Date (see provision 15.1). In a title transfer transaction, such as a repo, the Buyer or margin-holder do not have to return exactly the same security, only another part of the same issue (with the same ISIN).	2(oo)
12.9	definition of **cash currency**	
	The currency of the start-cash (see provision 12.10) is called the **Contractual Currency** in the GMRA.	7(a)
	The end-cash (see provision 12.13) must be paid in the same currency as the start-cash, unless the payee agrees to accept another currency. But in that case, to the extent allowed by applicable law, the payment in the other currency, when actually converted into the Contractual Currency for spot value and net of any costs, must be equal to the amount of the start-cash.	
	Any shortfall in the Contractual Currency after conversion must be made up by the payor on the same day.	7(b)
	Any surplus of Contractual Currency after conversion must be repaid by the payee on the same day.	7(c)
12.10	**start-cash**	
	The start-cash is called the **Purchase Price** in the GMRA. However, it is not a traditional price per unit but a sum of money.	2(nn)
12.11	**repo rate**	
	The repo rate is called the **Pricing Rate** in the GMRA. This is to avoid the risk that the term "repo rate" might lead to a repo being seen as a loan rather than a sale.	2(ll)
12.12	**repo interest**	
	Repo interest is called the **Pricing Differential** in the GMRA. This is also to avoid the risk that the term "repo interest" might lead to a repo being seen as a loan rather than a sale.	2(kk)
12.13	definition of **end-cash**	
	The end-cash is equal to the Purchase Price plus repo interest and is called the **Repurchase Price** in the GMRA. However, it is not a traditional price per unit but a sum of money.	2(rr)
	Note that the Repurchase Price can be calculated for every day during the Term of a repo and is the Purchase Price plus the repo interest that has accrued up to the date of calculation. The term is therefore used in the GMRA to describe the amount of cash owed by Seller to Buyer on a particular day, whether that is a day during the Term of a repo or on the Repurchase Date. The Repurchase Price during the Term of a repo has to be calculated in order to determine the exposure to be margined or when there is a default or other termination event.	
12.14	definition of **initial margin**	
	The parties may agree that the market value of Purchased Securities on the Purchase Date of a particular repo will be more or less (usually less) than the Purchase Price and that this cash/collateral ratio should be maintained between the current market value of the collateral and the Repurchase Price during the Term of the repo.	2(bb)
	This ratio is commonly called an "**initial margin**" in the market but is called a **Margin Ratio** in the GMRA.	2(xx)(A)
	The purpose of an initial margin is to cover any loss in value that the Buyer might suffer if collateral had to be liquidated.	
	The method of applying a Margin Ratio to the Purchase Price in order to calculate the exposure on a repo is called Transaction Exposure method A in Annex I of the GMRA (see paragraph 2(xx)).	
12.15	definition of **haircut**	
	The parties may agree that the market value of Purchased Securities on the Purchase Date of a particular repo will be more or less (usually less) than the Purchase Price and that this percentage difference should be maintained between the current market value of collateral and the Repurchase Price over the Term of the repo.	2(xx)(B)
	The percentage difference is called a "**haircut**" in the market but this term is not employed in the GMRA.	
	The purpose of a haircut is the same as that of an initial margin, which is to cover any loss in value that the Buyer might suffer if collateral had to be liquidated.	
	The method of applying a haircut to the market value of Purchased Securities in order to calculate the exposure on a repo is called Transaction Exposure method B in Annex I of the GMRA (see paragraph 2(xx)).	

Post-trade
VERIFICATION

13	**Confirmation** of a transaction	
	Buyer or Seller or both, as pre-agreed, must deliver a written Confirmation of a new repo promptly after execution.	3(b)
	Parties receiving a Confirmation are expected to check its details against their book of record to detect any errors in or misunderstandings about the terms and conditions of the new repo.	Annex II 3(b) last clause
	A Confirmation must describe at least the details listed in paragraph 3 of the GMRA. Parties are free to use the specimen Confirmation in Annex II.	
	A Confirmation, together with the pre-printed form and any annexes activated by reference in Annex I, constitutes prima facie evidence of the terms of a repo, unless the recipient makes a prompt objection which is supported by evidence (such as a recording).	
	The terms of a Confirmation prevail over any conflicting terms in the rest of the GMRA, allowing the terms to be varied just for a single repo.	

Settlement
PURCHASE

14	settlement of **Purchase**	
	On the Purchase Date, Seller shall deliver Purchased Securities to Buyer (or his agent) against payment of the Purchase Price by Buyer.	3(c)
	Deliveries and payments must take place only on Business Days, as defined in the GMRA, and during business hours (see the definition of Business Day in provision 14.1).	

14.1	definition of **Business Day**	
	A business day in the GMRA is defined as a business day in the place of settlement and payment. Business hours are therefore the opening hours of settlement and payment institutions. This definition applies only to payment and settlement and not to other obligations such as notifications. In the case of notifications, a business day is a day when commercial banks are open in the place of delivery (see 14(b)). However, commercial bank business hours are not specified in the GMRA. A 2016 court judgement in England advised parties to pre-agree the time of the close of business for the purpose of serving notices in a default.	2(f)
14.2	**convertibility** of cash	
	All payments under the GMRA must be made in immediately-available, freely-convertible funds.	6(a)
14.3	**transfer** of securities	
	The GMRA provides for a wide range of settlement options:	6(a)
	Physical securities in a suitable form and accompanied by necessary documentation for delivery.	
	Dematerialised securities delivered through an agreed book-entry or other clearing system.	
	Delivery by another method agreed by the parties.	
14.4	payment **taxes**	
	Unless otherwise agreed, payments in respect of any repos must be "free and clear of, and without withholding or deduction for, any taxes or duties…unless required by law."	6(b)
	Where a tax or duty is withheld or deducted, the paying party must make up the tax or duty. As noted already, this is commonly referred to as a "gross-up" obligation. Where this clause is a problem, parties may agree to delete it.	
14.5	**delivery versus payment (DVP)** on the Purchase Date	
	Unless otherwise agreed in writing between the parties, the payment of the Purchase Price shall be made simultaneously against the delivery of Purchase Securities, in other words, by delivery-versus-payment (DVP) settlement.	6(c)
	However, the parties are permitted, "from time to time in accordance with market practice and in recognition of the practical difficulties", to waive the requirement for DVP for a particular transaction, without permanently waiving that requirement on subsequent transactions.	6(d)
	Opposite payments in the same currency due on the same day are to be netted into a single payment.	6(h)
	Opposite deliveries of the same security due on the same day are to be netted into a single delivery.	6(i)
	This type of netting is sometimes called "technical netting". It is for operational convenience and does not legally net down multiple payments and deliveries into a single obligation, so could be unwound in a default.	

Settlement
REPURCHASE

15	**settlement** of **Repurchase**	
	On the Repurchase Date, Buyer must deliver Equivalent Securities to Seller (or his agent) against payment of the (final) Repurchase Price by Buyer (see the definition of Equivalent Securities in provision 15.1).	3(f)
	Seller has the right to deduct any unpaid manufactured payments from the final Repurchase Price (see the definition of manufactured payment in provision 19).	
	Deliveries and payments must take place on Business Days and during business hours, as defined in the GMRA.	
15.1	**securities** to be delivered by Buyer on maturity date	
	The securities to be delivered by Buyer on the Repurchase Date are called the **Equivalent Securities** in the GMRA.	2(v) first clause
	Equivalent Securities should be part of the same issue as the Purchased Securities (and therefore have the same ISIN). In a title transfer transaction, such as a repo, Buyer or margin-holder do not have to return exactly the same security.	

Settlement problems
PURCHASE AND REPURCHASE

16	rights in the event of a **failure to deliver** securities	
	The rights of Buyer, if Seller were to fail to deliver Purchased Securities on the Purchase Date, include the right to terminate the affected repo at any time and receive the difference between the Purchase Price and the Repurchase Price as it is on the date of termination, which means Buyer is entitled to the payment of accrued repo interest, regardless of the fact that no cash has been paid to Seller up to that point. This is intended to compensate Buyer for the failed settlement and encourage Seller to remedy the failure as soon as possible.	10(h)
	If Buyer decides not to terminate and allows the repo to run to the Repurchase Date but still no delivery is made, Buyer is entitled to the difference between the Purchase Price and the final Repurchase Price, which means Buyer is entitled to the full amount of repo interest, regardless of the fact that no cash has ever been paid to Seller.	
	The rights of Seller, if Buyer were to fail to deliver Equivalent Securities on the Repurchase Date, include the remedy known colloquially as a "**mini close-out**". This is the termination of the affected repo and the payment of cash compensation (that is, the difference between contractual and the latest value). This would be calculated as the difference, on the termination date, between the Repurchase Price owed by Seller on that date and the Default Market Value of the Equivalent Securities owed by Buyer (see the definition of Default Market Value in provision 23.1).	10(i)
	Where a party that has suffered a failure to deliver collateral decides to terminate the affected transaction, any costs incurred in entering into a replacement transaction or in hedging its exposure to the affected transaction can be included in the calculation of the resulting cash compensation (see provision 24).	10(l)(i)
17	treatment of **late payments**	
	Money not paid when due is treated as a separate debt and accrues interest at the higher of (1) the Pricing Rate (repo rate), if the late payment can be attributed to a particular repo, and (2) the **Applicable Rate** (see the definition of Applicable Rate in provision 17.1), although only to the extent permitted by applicable law.	12
17.1	definition of **Applicable Rate**	
	The Applicable Rate is an interest rate applied to a late payment. The way in which it is determined depends upon the context of the late payment:	2(c)
	• The Applicable Rate on a late payment to the Non-Defaulting Party after a default shall be selected by that party acting in a commercially reasonable manner.	2(c)(i)
	• The Applicable Rate for other purposes shall be the rate agreed by both parties acting in a commercially reasonable manner.	2(c)(ii)

Life-cycle
MANAGEMENT OF TRANSACTION AND COLLATERAL

18 substitution of collateral during the Term of a repo

The parties may agree, at any time, to modify a repo by allowing Buyer to substitute the original collateral and/or margin securities. This would involve Buyer transferring Equivalent Securities to Seller. In exchange, Seller would transfer to Buyer securities of a type agreed by the parties. These would be called the **New Purchased Securities**. They should have a Market Value, on the date of settlement, at least equal to the Market Value of the Equivalent Securities transferred to Seller. But note, in practice, it is unusual and possibly impracticable to leave the valuation of securities to their settlement date (values are normally agreed in advance). 8(a)

This method of substitution represents a modification of the terms of the original repo and does not create a new transaction. 8(b), 8(d)

The parties can also agree to substitute Margin Securities. The Market Value of the new margin securities must be at least equal to the Market Value of the original margin securities on the date of agreement to substitute (in contrast to the date used in the substitution of Purchased Securities). 8(d)

The GMRA envisages that the exchange of securities would be effected by simultaneous deliveries. 8(b)

Where the delivery of securities in a substitution takes places on a securities settlement system that requires a counter-payment of cash against any delivery of securities (in other words, it does not allow free-of-payment or FOP delivery), the party delivering substituting securities and therefore receiving a counter-payment and the substituted securities must make an offsetting cash payment directly to the other party on the same day. 8(d)

19 what happens when income is paid on collateral?

If a security that is being used as collateral in a repo pays a coupon or other income, Buyer (who should receive this payment from the issuer, given that he has legal title) must immediately pay an equal amount in the same currency to Seller. The payment due to Seller is commonly known as a **manufactured payment**. 5(a)

Manufactured payments must also be made if a coupon or other income is paid on a Margin Security, in this case, by the issuer to the margin-giver. 5(b)

Should a manufactured payment be subject to a withholding tax, the party making the manufactured payment is required to make ("gross") up the tax. 5(b) last clause

A manufactured payment is due on the **Income Payment Date** of the relevant security. 5(a)-(b)

20 procedures to eliminate one party's uncollateralised exposure to the other

Either party is entitled to call upon the other to eliminate some or all of any uncollateralised exposure to credit risk that the first party has to the other party. The call can be made at any time such an exposure is outstanding. 4(a)

The process of calculating and eliminating an uncollateralised exposure is called **Margin Maintenance** in the GMRA. 4(b)

The credit exposure on an individual repo is called a **Transaction Exposure** in the GMRA (see the definition in provision 20.1). 2(xx)

The credit exposure on the whole portfolio of repos under the same GMRA is called a **Net Exposure** in the GMRA (see the definition in provision 20.7). 4(c)

The GMRA envisages that parties will usually calculate and eliminate the Net Exposure.

However, parties can agree to calculate and eliminate Transaction Exposures on a transaction-by-transaction basis (see the procedures described in provision 20.10). 4(j), 4(k), 4(l)

A third option is to carve out a selected repo from the Net Exposure by calculating its Transaction Exposure separately, in order to eliminate its exposure separately from the Net Exposure on the other repo. This is usually done for structured transactions that are more complex than repo in the rest of the portfolio and, as a result, are calculated by specialists rather than the usual repo revaluation team. 4(i)

A party with a Net Exposure or, where it is agreed to split up Margin Maintenance, a party with a Transaction Exposure can make a call for Margin Maintenance by issuing a notice to the other party orally or in writing. 4(b)

20.1 definition of Transaction Exposure

The Transaction Exposure on an individual repo is based on the difference between the **Market Value** of the Equivalent Securities (see the definition of Market Value in provision 20.2) on the day of the Margin Maintenance calculation and the Repurchase Price on the same day (the Repurchase Price being the cash owed by Seller on that date). 2(xx)

20.2 definition of Market Value

In the case of Equivalent Securities, Market Value is the value calculated, in the case of fixed-income securities, using a dirty price (including accrued interest) agreed by the parties or as obtained from a generally-recognised source agreed by the parties. It must be converted, if required, into the Contractual Currency at the **Spot Rate** (see the definition of Spot Rate in provision 20.3). 2(ee) 2(ss)

In the case of **Margin Securities** (see the definition of Margin Securities in provision 20.4), the Market Value is less any agreed **Margin Percentage**, which is a haircut applied to Margin Securities. 2(cc) 2(aa)

Margin Percentage is an unusual haircut concept. Normally, a haircut is the difference between the Market Value of collateral and the cash being paid in exchange for them. However, in the case of Margin Securities, no cash is paid in exchange. Rather, the haircut in the case of Margin Securities is the amount of the exposure that a given market value of Margin Securities is deemed to offset.

20.3 definition of Spot Rate

This is the spot exchange rate used to convert from one currency to another, usually into the Base Currency. 2(ss)

For default calculations, the Spot Rate is from a generally-recognized source such as the central bank of the country in question or data providers (e.g. Bloomberg, Reuters, etc.) as specified by the non-defaulting party. 2(ss)(i)

For other calculations, including Margin Maintenance, the Spot Rate is from a generally-recognized source such as the central bank of the country in question or data providers (e.g. Bloomberg, Reuters, etc.) and accepted and agreed by contracting parties.

20.4 definition of Margin Securities

These are securities given by one party to the other in response to a Margin Maintenance call, in order to eliminate a Net Exposure or a Transaction Exposure (see the procedure to eliminate an exposure is described in provision 20.10). 2(cc)

To the extent that Margin Securities have been given by one party to the other, when those securities are returned, legally-speaking, this will be in the form of **Equivalent Margin Securities**, that is, part of the same issue as the Margin Securities initially transferred.

20.5 calculation of Transaction Exposure where there is a Margin Ratio

The Transaction Exposure of a repo (denoted in the GMRA by the letter E) on which a Margin Ratio has been agreed is calculated as the difference between (1) the Repurchase Price multiplied by the Margin Ratio and (2) the Market Value of the Equivalent Securities. This adjustment is called **Transaction Exposure method A** in Annex I. 2(xx) first clause 2(xx)(A)

20.6 calculation of Transaction Exposure where there is a haircut

The Transaction Exposure of a repo (denoted in the GMRA by the letter E) on which a haircut has been agreed is calculated as the difference between (1) the **Adjusted Value** — which is the Market Value of the Equivalent Securities multiplied by one minus the haircut — and (2) the Repurchase Price. This adjustment is called **Transaction Exposure method B** in Annex I. 2(xx) first clause 2(xx)(B)

20.7 definition of **Net Exposure**

Net Exposure should be calculated by both parties but it is expected that only the party with the Net Exposure will actually make a Margin Maintenance call (since it will be the beneficiary). 4(c)

Net Exposure is the difference between:

- the gross exposure of party A to party B — which is the sum of the aggregate Transaction Exposures of party A to party B plus any late manufactured payments owed to party A by party B, less an amount called the **Net Margin**, if this held by party A (see the definition of Net Margin in provision 20.8); and
- the gross exposure of party B to party A — which is the sum of the aggregate Transaction Exposures of party B to party A plus any late manufactured payments owed to party B by party A, less the **Net Margin**, if this held by party B.

Amounts denominated in different currencies must be converted into the **Base Currency** for the purpose of calculating Net Exposure (see the definition of Base Currency in provision 20.9) at the current Spot Rate.

20.8 definition of **Net Margin**

This is the excess of (1) the Market Value of Margin Securities and Cash Margin held by one party over (2) the gross value of margin held by the other. 2(gg)

Only the party with Net Margin benefits from a reduction in Net Exposure.

20.9 definition of **Base Currency**

This is the currency or currencies specified as such in Annex I. 2(e)

- For Margin Maintenance calculations, the Base Currency pre-agreed by the parties is the currency in which the Market Value is calculated for Margin Maintenance and (unless otherwise agreed) the currency in which Cash Margin must be paid.
- For default management calculations, the Base Currency is the pre-agreed currency into which the Default Market Value of collateral securities would be converted and in which the close-out amount would be calculated.

The GMRA envisages one Base Currency per agreement. However, parties are free to agree more than one Base Currency, for example, one for the calculation of Market Value and another for Default Market Value.

20.10 how are uncollateralised exposures eliminated?

Typically, a Net Exposure or Transaction Exposures are eliminated by the transfer of a variation margin to the exposed party. 4(a)

The GMRA terminology for a variation margin is a **Margin Transfer**. 2(dd)

Margin Transfers can be transfers of Margin Securities or **Cash Margin** or both (see the definition of Cash Margin in provision 20.11).

After receiving a Margin Maintenance call, a party must make a Margin Transfer "within the minimum period specified in Annex I or, if no period is specified, such minimum period as is customarily required for the settlement or delivery of money" and for the settlement or delivery of the relevant securities. 4(g)

Instead of Margin Transfers, parties can opt to eliminate Transaction Exposures on a transaction-by-transaction basis by terminating individual repos and replacing each with a new transaction in which either the cash or collateral value has been changed to eliminate the exposure. These alternative methods are called **Repricing** and **Adjustment** (see the definitions in provisions 20.12 and 20.13). 4(j), 4(k), 4(l)

Note that failure to initiate Margin Maintenance when a party has a Net Exposure, and is entitled to call margin, does not constitute a waiver of the right to do so later. 18

20.11 definition of **Cash Margin**

This is GMRA terminology for a Margin Transfer in the form of cash. 2(h)

Cash Margin must be paid in the currency agreed by the parties but, if none has been agreed, it must be paid in the Base Currency. 4(e)

Cash Margin represents a debt on which interest has to be paid at a rate and at times pre-agreed by the parties and recorded in Annex I but the parties are free to subsequently agree another rate and other times. 4(f)

20.12 definition of **Repricing**

In Repricing, the parties agree to terminate any repo with a material Transaction Exposure and execute a replacement repo with terms that are identical to the original repo, other than the Purchase Price of the replacement repo, which will be set to equal the current Market Value of the Equivalent Securities of the terminated repo. 4(j), 4(k)

The payment and delivery to settle the termination of the original repo is netted against the payment and delivery to settle the replacement repo, which means that there only needs to be a net cash payment, but no delivery of securities. This is economically analogous to a Cash Margin. 4(k)(vii)

20.13 definition of **Adjustment**

The parties agree to terminate any repo with a material exposure by executing a replacement repo with the Market Value of the Purchased Securities in the replacement repo equal to either the Purchase or Repurchase Price of the terminated repo. The opportunity can be taken to substitute the collateral, which might require a change in any initial margin or haircut. 4(j), 4(l)

The payment to settle the termination of the original repo is netted against the payment to settle the replacement repo, which means that there does not need to be any cash payment. 4(l)(v)

It is unlikely that the Adjustment method has ever been used in practice.

20.14 **failure to deliver** Cash Margin or Margin Securities when called

To the extent that a party calling for a Margin Transfer has previously paid Cash Margin that has not yet been repaid or has delivered Margin Securities in respect of which Equivalent Margin Securities have not yet been returned, that party may require that its call for a Margin Transfer should be satisfied first by the repayment of the outstanding Cash Margin or the delivery of the outstanding Equivalent Margin Securities. 4(d)

Otherwise, the composition of a Margin Transfer is at the option of the party receiving the margin call.

Where a party receiving a margin call is required to satisfy that call by first repaying Cash Margin or delivering Equivalent Margin Securities which it has not yet returned but that party, despite making all reasonable efforts and for reasons relating to the securities or the settlement system, is unable to deliver Equivalent Margin Securities, , it must immediately pay a temporary Cash Margin equal to the Market Value of the Margin Securities. No interest is due on this type of Cash Margin. 4(h)

If a failure to deliver Equivalent Margin Securities continues for more than two Business Days, the failed party may, by notice, require the failing party to permanently settle the call for the return of the securities by paying an amount equal to their Default Market Value (see the definition of Default Market Value in provision 23.1). This amount is called the **Cash Equivalent Amount**.

If a party receiving a margin call is required to satisfy that call by first repaying Cash Margin or delivering Equivalent Margin Securities but is unable to do so because it has failed to make all reasonable efforts or for reasons not relating to the securities or the settlement system, it will be in default for failing to make the Margin Transfer.

21 what is a **default**?

The GMRA lists ten **Events of Default**. These are: 10(a)

- all failures to pay cash, including the Purchase Price, Repurchase Price and manufactured payments; 10((a)(i)-(v)
- failure to make Margin Transfers in response to Margin Maintenance calls;
- failure to make deliveries or payments relating to Repricing or Adjustment;
- misrepresentation (see provision 2 above for a list of representations); 10(a)(vii)
- admission of unwillingness or inability to perform obligations; 10(a)(viii)
- loss of access to securities trading because of a regulatory sanction in response to insufficient financial resources or a credit rating downgrade; 10(a)(ix)
- failure to deliver securities but only if the parties have pre-agreed that this optional Event of Default should apply; 10(a)(ii)
- most critically, the occurrence of an **Act of Insolvency**, of which, there are seven, which are listed separately in paragraph 2(a); and 10(a)(vi) 2(a)
- "failure to perform any other obligations", where the failing party "does not remedy such failure within 30 days after notice is given by the Non-Defaulting Party" — this is the only **grace period** allowed in the standard Events of Default. 10(a)(x)

Note that a party in default or potentially in default is obliged under the GMRA to notify the other party. Defaulting parties usually observe this obligation in order to avoid charges of fraudulent trading. 10(m)

22 what happens when a party **defaults**?

If the Event of Default is an Act of Insolvency involving either the filing of a winding-up petition or analogous document or the appointment of a liquidator or analogous official, and the parties had pre-agreed to treat these acts as **Automatic Early Termination Events** and had recorded this agreement in Annex I, their occurrence would automatically trigger an **Early Termination Date**. 10(b) 2(r) 10(b)-(c)

An Automatic Early Termination Date would be deemed to occur "at the time immediately preceding the occurrence" of the Act of Insolvency. This is to try to pre-empt the intrusion of the insolvency regime and the over-riding of contractual measures.

Automatic Early Termination should only be used where there is a risk of the insolvency regime intruding, as it gives the Non-Defaulting Party no time to prepare itself to manage the consequences of the termination of repos with the Defaulting Party (e.g. arranging to replace, hedge or unwind existing hedges on defaulted transactions).

Other Events of Default (not involving an Act of Insolvency) would give the Non-Defaulting Party the following options:

- do nothing;
- suspend the performance of all obligations to the Defaulting Party, provided the parties have pre-agreed, and recorded their agreement in Annex I, that each party's obligations is subject to the **condition precedent** that the performance of obligations by either party is dependent on the other party not being in default; and 6(j)
- when it is ready, send a **Default Notice** (see the definition of this notice in provision 22.1) giving the Defaulting Party not more than 20 days' notice of the Early Termination Date fixed by the Non-Defaulting Party. 2(n)

22.1 definition of **Default Notice**

This is not a notice placing the other party in default (under the GMRA 2011, default is automatic upon the occurrence of an Event of Default). A Default Notice under the GMRA 2011 is in fact a notice of the Early Termination Date chosen by the Non-Defaulting Party (see provision 23). 2(n)

In an Event of Default, if the non-defaulting party has been unable to serve a Default Notice, despite making all practicable efforts, it can self-certify notification and deliver the notice later. This is called a **Special Default Notice**.

23 what happens on the **Early Termination Date**?

The Early Termination Date is the day on which the process of "close-out netting" starts under the GMRA. This means that it is the day on which transactions with the Defaulting Party are deemed to be terminated by the Non-Defaulting Party and to which the outstanding obligations between the parties are accelerated in order to be aggregated (set off) into a net amount. Specifically, the Early Termination Date is the day on which it is deemed that: 10(c)

- Repurchase Prices become due;
- Cash Margin and Cash Equivalent Amounts become repayable; and
- Equivalent Securities and Equivalent Margin Securities become deliverable.

The Non-Defaulting Party determines the amounts of cash and collateral due on the Early Termination Date, including the **Default Market Value** of the collateral securities (see the definition of Default Market Value in provision 23.1).

Repurchase Prices (the amount of cash owed) on the Early Termination Date are simply the agreed Repurchase Prices less the repo interest that was due to have been accrued until the original Repurchase Dates.

There are three valuation methods for determining Default Market Value: 10(f)(i)

- Dealing prices — using the net proceeds of sales of **Receivable Securities** (see the definition in provision 23.2) and the aggregate cost of **Deliverable Securities** (see the definition in provision 23.3) made "on or about" the Early Termination Date. 10(f)(i)(A) 10(f)(i)(B) 10(f)(ii)
- Quotes — an average bid price for Receivable Securities or an average offer price for Deliverable Securities quoted "on or about" the Early Termination Date by two or more market-makers or regular dealers in the **Appropriate Market** (see the definition of the Appropriate Market in provision 23.4) in commercially-reasonable size, using a pricing methodology which is customary for the particular security. The customary methodology is determined by the Non-Defaulting Party. It includes adding the accrued interest to clean prices.
- **Net Value** (see the definition of Net Value in provision 23.5). Unlike dealing prices and quotes, which are "mark-to-market" methods of valuation, Net Value is a "mark-to-model" method, which is useful for valuing illiquid securities for which dealing opportunities and quotes may be difficult or impossible to find. In other words, it is a theoretical estimate of value. It can employ whatever data and methods are deemed suitable by the Non-Defaulting Party. The choice of this method is only allowed if the Non-Defaulting Party has been unable to buy or sell the securities or to obtain quotations; or if buying or selling at such prices would not be commercially reasonable; or if it would not be commercially reasonable to use or even to obtain quotations. 10(f)(iii)

All amounts not denominated in the **Base Currency** must be converted into that currency at the **Spot Rate** determined by the Non-Defaulting Party. 10(d)(ii)

The values determined by the Non-Defaulting Party are then set off against each other to produce a balance, which is payable by the party with the lower gross claim. The balance is usually known as a "close-out amount". 10(d)(iii)

As soon as reasonably practicable after the above calculations have been made, the Non-Defaulting Party must present a statement to the Defaulting Party showing the calculations in "reasonable detail". The balance is due to be paid on the next Business Day.

From and including the date on which the Non-Defaulting Party presents a statement to the Defaulting Party, to the extent allowed by the applicable law, interest starts to accrue on the close-out amount at the Applicable Rate determined by the Non-Defaulting Party up to but excluding the date of payment.

23.1 definition of **Default Market Value**

This is the value of the Equivalent Securities or Equivalent Margin Securities "as at the Early Termination Date", as determined by the Non-Defaulting Party, "on or as soon as practicable after the Early Termination Date" using one of the three specified valuation methods. 10(d)(i) 10(e)

23.2 definition of **Receivable Securities**

Where actual dealing prices or quotes are being used to determine the Default Market Value of Receivable Securities: 10(e)(iv)

- Receivable Securities are the Equivalent Securities or Equivalent Margin Securities that were due to be delivered to the Defaulting Party, that is, the collateral and margin securities to be returned. 10(f)(i)(A)
- The Default Market Value of Receivable Securities can be the net proceeds of the sale of the Equivalent Securities or Equivalent Margin Securities, where these are still being held by the Non-Defaulting Party, or the net proceeds of the sale of the same issue that has been acquired by the Non-Defaulting Party in other transactions with other parties.
- If the quantity of Receivable Securities sold (e.g. 5 million) is smaller than the quantity that needs to be valued (e.g. 12 million), the Non-Defaulting Party can seek other dealing prices or quotes to value the excess or it can imply the average proceeds of the whole amount (12 million) from the smaller amount of securities actually sold (5 million).
- The net proceeds of sales of Receivable Securities should be net of "all reasonable costs, commissions, fees and expenses" incurred in the sale. 10(f)(ii)(A))

Where quotations are being used to determine the Default Market Value of Receivable Securities:

- Prices should be converted by the Non-Defaulting Party, where necessary, to dirty prices (by adding accrued interest) and, where appropriate, adjusted for any **Pool Factor Affected Security** (a reduction in the nominal amount of securitized assets due to prepayment), in both cases, in a commercially reasonable manner; 10(e)(v)
- **Transaction Costs** (see the definition in provision 23.6) must be deducted from the sale proceeds of Receivable Securities.

23.3 definition of **Deliverable Securities**

Where actual dealing prices or quotes are being used to determine the Default Market Value of Deliverable Securities: 10(e)(ii)

- Deliverable Securities are the Equivalent Securities or Equivalent Margin Securities that were due to be delivered by the Defaulting Party, that is, the collateral and margin securities due to be received by the Non-Defaulting Party. 10(f)(i)(B)
- If the quantity of Deliverable Securities purchased (e.g. 5 million) is smaller than the quantity that needs to be valued (e.g. 12 million), the Non-Defaulting Party can seek other dealing prices or quotes to value the excess or it can imply the average proceeds of the whole amount (12 million) from the smaller amount of securities actually bought (5 million).
- The aggregate cost of purchases of Deliverable Securities should include "all reasonable costs, commissions, fees and expenses" incurred in the purchase. 10(f)(ii)(A)

Where quotations are being used to determine the Default Market Value of Deliverable Securities:

- Prices should be converted by the Non-Defaulting Party, where necessary, to dirty prices (by adding accrued interest) and, where appropriate, adjusted for any **Pool Factor Affected Security** (a reduction in the nominal amount of securitized assets due to prepayment), in both cases, in a commercially reasonable manner; 10(f)((ii)(B)
- **Transaction Costs** (see the definition in provision 23.6) must be deducted from the sale proceeds of Receivable Securities.

23.4 definition of **Appropriate Market**

The market which is "**most appropriate**" for the securities being valued. 10(e)(i)

The Appropriate Market is assumed to be the market with the fastest turnover, which is usually located in the country in which they were issued.

23.5 definition of **Net Value**

Net Value is the "**fair market value**" of Receivable and Deliverable Securities in the reasonable opinion of the Non-Defaulting Party, having regard to such pricing sources and methods as that party considers appropriate, and taking account of **Transaction Costs**. 10(e)(iii)

Note that "fair market value" in the GMRA differs from the meaning of that term in accounting standards such as IFRS. In the GMRA, it means a mark-to-model valuation as opposed to a mark-to-market valuation.

23.6 definition of **Transaction Costs**

Transaction Costs means "reasonable costs, commissions, fees and expenses (including any mark-up or mark-down or premium paid for guaranteed delivery) incurred or reasonably anticipated in connection with the purchase of Deliverable Securities or sale of Receivable Securities, calculated on the assumption that the aggregate…is the least that could be reasonably expected to be paid". This includes the immediate costs of execution. 10(e)(v)

24 **other costs** that can be included in the close-out calculation

In addition to Transaction Costs, the Non-Defaulting Party is entitled to charge "all reasonable and legal and other professional expense…in connection with or as a consequence of" a default. This is taken to include the cost of external legal advice and collateral valuation agents. 10(g)

If a Non-Defaulting Party replaces repos on which there has been a default or hedges the exposure arising from the default, it is entitled to include in its default calculations its estimate (made in good faith) of any net loss or expense incurred in entering into those transactions (including all fees, costs and other expenses). But any net profit has to be attributed to the Defaulting Party in the close-out netting calculation. 10(l)(i)

On the other hand, acting reasonably, the Non-Defaulting Party can decide not to replace defaulted transactions, but to replace or unwind existing hedges and include in its default calculations its estimate (made in good faith) of any net loss or expense incurred in entering into replacement transactions or in unwinding (including all fees, costs and other expenses). But any net profit has to be attributed to the Defaulting Party in the close-out netting calculation. 10(l)(ii)

Note that these costs are also applied to the calculation of amounts due when a repo on which there has been a failure to delivery collateral is terminated by the affected party (see provision 16 above).

The costs described in this section and the Transaction Costs described in the previous section are the only costs that can be charged to the Defaulting Party. This means that **consequential loss or damage** cannot be charged. These are "knock-on" costs not arising in the close-out process but as a consequence of default. 10(j)

Annex I

Applying Annex I when negotiating a GMRA (pre-trade)

Annex I is pivotal to the working of the GMRA. Part 1 of Annex I is where decisions are recorded on matters that are essential to the operation of the GMRA. These standard elections are listed in Part 1. They can be grouped into four themes.

Counterparty and communication

- who sends confirmations — one or both parties ..... (1(h))
- addresses for communications ..... (1(n))
- agents for service of process ..... (1(o))

Activation of other annexes and scope of the GMRA

- Buy/Sell-Back Annex ..... (1(a))
- Agency Annex ..... (1(c))
- Net Paying Securities ..... (1(b))
- other applicable annexes ..... (1(d))

Margin and default calculation inputs and implementation

- what is the Base Currency ..... (1(e))
- Transaction Exposure method ..... (1(g))
- interest rate index and dates on cash margin ..... (1(i))
- delivery period for margin ..... (1(j))

Default triggers

- will condition precedent apply ..... 1((k))
- will failure to deliver be an Event of Default ..... (1(l))
- will Automatic Early Termination apply and to which party or to both ..... (1(m))

Part 2 of Annex I is where all agreed amendments and additions to and deletions from the pre-printed form are recorded, along with agreement to attach other annexes. As explained, locating such bespoke changes in the pre-printed form makes it easier for the parties to monitor their negotiations.

Annex II

Provisions not covered in the Handbook

- Designated Offices ..... (1(a) and 2(p))
- Open repo ..... (1(a) and 3(d)-(e))
- Corporate events ..... (2(u)-(v))
- Definition of Income Payment Date for registered securities ..... (2(z))
- Conversion to the Base Currency using the Spot Rate ..... (2(ss))
- Treating payments and repayments of principal (as opposed to redemptions) as ..... (2(yy)) Distributions for payment as manufactured payments rather than the Repurchase Price
- Cash Equivalent Amount ..... (4(h))
- Change in the Contractual Currency ..... (7(b)-(c))
- Dealing with mandatory cash payments when substituting collateral ..... 9(d)
- Pool Factor Adjustment in the calculation of the Default Market Value of ABS ..... (10(f)(ii)A))
- Adoption of the Euro will not affect the terms of the GMRA ..... (16(e))
- One party acting as agent ..... (Annex I (1)(c))
- Failure to delivery securities where repo rate is negative ..... (Annex I (2)(b))
- Forward repo ..... (Annex I (2)(c))

Authored by Richard Comotto
Edited by Ingrid Hagen, SVP Strategic Projects, Frontclear

Richard Comotto is Senior Consultant to the International Capital Market Association (ICMA) and its European Repo and Collateral Council (ERCC) for whom he authors the Guide to Best Practice in the European Repo Market. He is also a technical expert to Frontclear, the IMF, and other international financial institutions on money market and repo market development. He has worked with Frontclear in Georgia, Ghana, Honduras, Kenya, Mongolia, Tanzania, Uganda and Zambia, and has published a study for Frontclear on exchange-traded repo. Richard is course director for the ICMA's Professional Repo Market Course and other ICMA training and his courses and tutorials are readily available on the Frontclear Academy. Richard was formerly Visiting Fellow at the ICMA centre at the University of Reading. He acts as an independent consultant providing research, support and training on the institutional money, securities and derivatives markets to a wide range of clients, including professional market associations, government agencies, regulatory authorities, multilateral development banks, banks, brokers and information services, both in the City of London and outside the UK. Special interests include securities financing, collateral management and electronic trading in OTC markets. He served for 10 years in the Bank of England, including the Bank's Foreign Exchange Division and on secondment to the IMF in Washington DC.

Frontclear

Mauritskade 63
1092 AD Amsterdam
The Netherlands

FRONTCLEAR.COM

Our investors

European Bank for Reconstruction and Development
PROPARCO Groupe Agence Française de Développement
BMZ Federal Ministry for Economic Cooperation and Development
AFD Agence Française de Développement
Foreign, Commonwealth & Development Office
KFW
FMO Entrepreneurial Development Bank
fsdafrica
TCX
CARDANO DEVELOPMENT
fsdafrica Investments
Sida Swedish International Development Cooperation Agency