International Swaps & Derivatives Association, Inc.

May 1989 Addendum to Schedule to Interest Rate Swap Agreement

Interest Rate Caps, Collars and Floors

(1) As used in this Agreement or in a Confirmation, (i) “Rate Protection Transaction” will mean any Rate Swap Transaction that is identified in the related Confirmation as a Rate Protection Transaction, Rate Cap Transaction, Rate Floor Transaction or Rate Collar Transaction and (ii) “Specified Swap” means, notwithstanding Section 14 of this Agreement but subject to Section 1(c) of this Schedule, any rate swap, rate cap, rate floor, rate collar, currency exchange transaction, forward rate agreement, or other exchange or rate protection transaction, or any combination of such transactions or agreements or any option with respect to any such transaction now existing or hereafter entered into between one party to this Agreement (or any applicable Specified Entity) and the other party to this Agreement (or any applicable Specified Entity).

(2) Notwithstanding anything to the contrary in this Agreement, the following provisions will apply with respect to a Rate Protection Transaction:

> (a) the Floating Rate applicable to any Calculation Period will be (i) with respect to a Floating Rate Payor for which a Cap Rate is specified, the excess, if any, of the Floating Rate calculated as provided in this Agreement (without reference to this paragraph 2(a)) over the Cap Rate and (ii) with respect to a Floating Rate Payor for which a Floor Rate is specified, the excess, if any, of the Floor Rate over the Floating Rate calculated as provided in this Agreement (without reference to this paragraph 2(a));
>
> (b) “Cap Rate” means, in respect of any Calculation Period, the per annum rate specified as such for that Calculation Period; and
>
> (c) “Floor Rate” means, in respect of any Calculation Period, the per annum rate specified as such for that Calculation Period.

(3) For purposes of the determination of a Market Quotation for a Terminated Transaction in respect of which a party (“X”) had, immediately prior to the designation or occurrence of the relevant Early Termination Date, no future payment obligations, whether absolute or contingent, under Section 2(a) of this Agreement with respect to the Terminated Transaction, (i) the quotations obtained from Reference Market-makers shall be such as to preserve the economic equivalent of the payment obligations of the party (“Y”) that had, immediately prior to the designation or occurrence of the relevant Early Termination Date, future payment obligations, whether absolute or contingent, under Section 2(a) of this Agreement with respect to the Terminated Transaction and (ii) if X is making the determination such amounts shall be expressed as positive amounts and if Y is making the determination such amounts shall be expressed as negative amounts.

(4) Notwithstanding the terms of Sections 5 and 6 of this Agreement and Section 11.6 of the Code, if at any time and so long as one of the parties to this Agreement (“X”) shall have satisfied in full all its payment obligations under Section 2(a) of this Agreement and shall at the time have no future payment obligations, whether absolute or contingent, under such Section, then unless the other party (“Y”) is required pursuant to appropriate proceedings to return to X or otherwise returns to X upon demand of X any portion of any such payment, (a) the occurrence of an event described in Section 5(a) of this Agreement with respect to X or any Specified Entity of X shall not constitute an Event of Default or a Potential Event of Default with respect to X as the Defaulting Party and (b) Y shall be entitled to designate an Early Termination Date pursuant to Section 6 of this Agreement only as a result of the occurrence of a Termination Event set forth in (i) either Section 5(b)(i) or 5(b)(ii) of this Agreement with respect to Y as the Affected Party or (ii) Section 5(b)(iii) of this Agreement with respect to Y as the Burdened Party.

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COMMENTARY

May 1989 Addenda to ISDA Schedules for Interest Rate Caps, Collars and Floors

The International Swaps Dealers Association, Inc. ("ISDA") has published two addenda – one each for the Interest Rate Swap Agreement and the Interest Rate and Currency Exchange Agreement – designed to enable swap counterparties to include caps, collars and floors and similar products under such Agreements. The Addenda reflect the input and suggestions of many ISDA members after open Documentation Committee Meetings held in London, New York and Paris.

USE OF ADDENDA

Before the provisions are analyzed in detail, a word on their suggested use is warranted. Some swap counterparties with existing master swap agreements may simply amend them by adding the appropriate Addendum, so that all caps, collars and floors between the parties are included with swaps under a single master agreement and will, subject to the provisions in the Addendum, be treated uniformly under the agreement. Other counterparties may prefer to separate the documentation of caps, collars and floors from the documentation of swaps. The Documentation Committee considered preparing a separate master agreement for caps, collars and floors, but decided this was not necessary because the appropriate Addendum could be attached to an existing ISDA form and used exclusively for caps, collars and floors. Parties that prefer separate documentation would thus have two master agreements with the same counterparty – one for swaps and one for caps, collars and floors.

Participants should consult their own legal advisors to determine which approach is appropriate for them. In making such determination, Participants should read the discussion of the Optional Paragraph below.

ANALYSIS OF ADDENDA

1. *Paragraph 1.* This provision adds definitions which are used elsewhere in the Addenda or may be used by participants in confirmations relating to caps, collars and floors. To implement the definition of "Rate Protection Transaction", the parties should add a line item in their confirmations, preferably toward the beginning, to the following effect:

"[Type of Transaction: Rate Protection/Cap/Collar/Floor Transaction]"

The expanded definition of "Specified Swaps" anticipates the parties' probable intent that performance under an ISDA agreement is conditioned on each party's continuing performance under *all* similar transactions between the parties, and not simply rate swap and currency exchange transactions.

2. *Paragraph 2.* This provision redefines certain terms contained in the 1987 Interest Rate and Currency Exchange Definitions (the "Definitions") and the Code of Standard Wording, Assumptions and Provisions for Swaps, 1986 Edition (the "Code"). In so doing it uses capitalized terms which are defined in the Definitions and the Code.

Paragraph 2(a) overrides the standard definition of "Floating Rate" when applied to caps, collars and floors (as well as any other transactions for which a Cap Rate or a Floor Rate is specified).

Under paragraph 2(a) the Floating Rate becomes either (i) if a Cap Rate is specified, the excess of the rate determined under the applicable Floating Rate Option (*e.g.*, LIBOR) over the specified Cap Rate or (ii) if a Floor Rate is specified, the excess of the specified Floor Rate over the rate determined under such Floating Rate Option.

Paragraph 2(b) and 2(c) provide defined terms for the specified rate at which a party buys a cap, collar or floor. These terms are used most significantly in the Floating Rate definition referred to above. It is anticipated that parties would add one or more line items to their swap confirmations, perhaps in proximity to the Floating Rate Option item, as follows:

[Cap Rate:]	[%]
[Floor Rate:]	[%]

3. *Paragraph 3*. This provision is intended to clarify the application of the definition of Market Quotation to fully paid caps and floors. In the standard definition, the quoting market maker is requested to give quotes for a transaction which would have the effect of preserving for the parties the economic equivalent of the payment obligations of both parties under the Terminated Transaction from and after the Early Termination Date to the originally scheduled Termination Date. Paragraph 3 of the Addenda simply recognizes that with a fully paid cap or floor, only one of the parties has any remaining payment obligations. Thus, it is more accurate with respect to such transactions to specify that the quotes obtained should reflect the preservation of the economic equivalent of the payment obligations of the one party still obligated to make payments.

The remainder of this provision recognizes that upon early termination a fully paid transaction can never have a negative value to the buyer because the buyer has no further payment obligations thereunder. It will cost the buyer some amount to replace a terminated cap or floor. Conversely, upon early termination a fully paid transaction will always have a negative value to a seller because the seller has potential future payment obligations. The seller will receive some amount to replace a terminated cap or floor.

4. *Paragraph 4*. It is anticipated that some parties may conduct business in such a way that from time to time one will consistently be only a purchaser of caps or floors from the other. This may be the case because one or both parties do not as a rule enter into swap transactions, because the creditworthiness of one party is such that the other would not accept the risk associated with purchasing a cap or floor from the first party or because of other reasons. If two parties do conduct such a "one-way" business, the consistent buyer might argue, not unreasonably, that it would be inappropriate for the consistent seller to designate an Early Termination Date with respect to such transactions, at least so long as the buyer has satisfied in full all its payment obligations, because the seller does not have any exposure to the credit of the buyer. On the other hand, the occurrence of certain of the Termination Events may adversely affect the seller in that it may become unduly burdensome if, for example, the seller must gross up payments as a result of a Change in Tax Law. Similarly, a change in law making it illegal for the seller to perform should enable it to designate an Early Termination Date. In such event, the buyer is not disadvantaged because the ISDA agreements call for two-way payments, thus permitting the buyer to receive the market value of all the transactions subject to the termination notice.

To give effect to the foregoing points, Paragraph 4 specifies that so long as a party ("X") has satisfied in full its basic payment obligations (and the other party is not obligated to or does not return such payments), then (a) neither an Event of Default nor a Potential Event of Default can occur with respect to X as Defaulting Party and (b) the other party ("Y") shall only be entitled to designate an Early Termination Date as a result of certain specified Termination Events.

Some parties in the position of the consistent seller may feel justified in expanding the list of events entitling it to designate an Early Termination Date to include for example, Default under Specified Swaps 9Section 5(a)(v) or Cross Default (Section 5(a)(vi)). In such a situation, Y may be disadvantaged if it must continue to perform the caps and floors it sold under an ISDA agreement even though X has failed to perform under other agreements between the same parties.

As an alternative or in addition to the foregoing, parties may wish to consider the desirability of including contractual "set-off' provision to cover other transactions between them not included under the ISDA agreement.

OPTIONAL PARAGRAPH

Parties which use, or are contemplating the use of, limited "two-way" payments (paragraph 6(e)(i) of the ISDA agreements) may wish to include in the appropriate Addendum the following provision:

"(5) For purposes of calculating payments due in respect of an Early Termination Date (including any payments under Section 6(d) and any Unpaid Amounts), an Event of Default specified in Section 5(a)(vii) of this Agreement (Bankruptcy) shall be treated as if it were a Termination Event with the Defaulting Party as the Affected Party (and for such purposes the proviso to the definition of "Settlement Amount" shall be deemed to be of no force and effect)•. Such Event of Default treated as a Termination Event shall take precedence over any other Event of Default which is existing at the time of the designation or deemed occurrence of such Early Termination Date."

This optional provision reflects the views of a number of ISDA members that it is inappropriate to use the limited two-way payments provision contained in the standard form Agreements – at least in the case of a bankruptcy of a party – if an ISDA agreement covers caps and floors, as well as swaps. These members believe this optional provision should be included because it produces a result that would be the outcome if the trustee or receiver in a bankruptcy or insolvency case were to challenge the early termination payment provisions on the grounds that fully paid-for caps and floors are assets of the debtor, the value of which cannot be denied to the debtor. In addition, this optional provision is supported by those members who believe that bankruptcy should in all cases (swaps as well as caps and floors) be treated as a Termination Event rather than as an Event of Default.

At the same time, however, other ISDA members believe that this optional provision should not be included because they believe that limited two-way payments is a valid approach for an ISDA agreement that covers caps and floors, as well as swaps, and that bankruptcy should remain an Event of Default. These members believe that a court would uphold such contractual provisions, particularly when agreed to by two sophisticated, commercial parties.

Other ISDA members believe that other approaches are appropriate when an ISDA agreement covers caps and floors. As noted above, Participants are urged to consult with their legal advisors to determine which approach is appropriate for them.

• This parenthetical clause need only be included in the Addendum relating to the Interest Rate and Currency Exchange Agreement.