

## PART 15 - RECIPROCAL PURCHASE AGREEMENTS

### What is a REPO?

[15.01] A reciprocal purchase agreement (REPO) involves an agreement for the sale by one entity (A) to another entity (B) of securities having agreed features entered into at the same time and related to another agreement for the sale by B to A of securities having the same features. The second transaction is settled on a day after the first transaction is settled.

**\*\*This part of the guide deals only with REPOs which are documented under an ISDA Master Agreement. See part 26 if you want to document REPOs under the PSA/ISMA Global Master Repurchase Agreement.\*\***

### How to use this part of the guide

[15.02] **Have you used ISDA documents before?** If you are not familiar with the ISDA documents, we recommend that you:

- (a) read the User's Guide (~~see [Volume 2.02]~~) and the ISDA Master Agreement (~~see [Volume 2.01]~~);
- (b) read parts 3 and 5 of this guide;
- (c) read this part of the guide.

If you are familiar with the ISDA documents, we recommend that you start by reading this part and refer to the other parts as necessary.

As stated previously, this guide is prepared on the assumption that you use the 1992 ISDA Master Agreement.

### Preliminary issues

[15.03] **Do you want a separate ISDA Master Agreement?** Participants have the choice of using one ISDA Master Agreement for all Transactions including REPOs or using a separate ISDA Master Agreement for REPOs only.

We consider that using one agreement has the following attractions:

- (a) using one agreement for all Transactions simplifies documentation and reduces the number of agreements required;
- (b) it gives the parties the option of specifying net payments for corresponding payment dates for all Transactions, giving them the ability to reduce the settlement risk with the counterparty; and

- (c) as all Transactions would then be regulated by the same agreement, the amount payable on early termination will be payable by reference to aggregate net exposures under all Transactions and therefore would not exclude amounts payable in connection with REPOs.

However, even where separate ISDA Master Agreements are used in respect of different kinds of Transactions, it is possible for the parties to provide that a single net amount will be payable between the parties should an Early Termination Event occur. Suggested wording to achieve this is contained in [18.22].

**Regulation.** See [6.04A] for commentary on the regulation of derivatives in Australia.

**Tax consequences.** This guide has not been prepared with a view to participants being able to achieve any particular tax consequence in entering into Transactions. Accordingly, participants must separately consider the tax consequences of following the recommendations in this guide. In particular, participants wanting to rely on section 26BC of the Income Tax Assessment Act should take advice as to the requirements of, and consequences of the application of, that section.

## How to document REPOs

[15.04] To document REPOs using an ISDA Master Agreement under Australian law you should ensure that you have executed an ISDA Master Agreement with your counterparty. Recommendations for completing the schedule to an ISDA Master Agreement are set out in part 5 of this guide. **Care!** Ensure that you use the 1992 ISDA Master Agreement and not the 1987 version. The 1987 version does not allow for deliveries of securities.

[15.04A] Until 1 January 2002 AFMA recommended using Australian Addendum No. 9 - Reciprocal Purchase Agreements. **This is no longer recommended for the following reasons:**

No longer recommended because the majority of market participants entering into these transactions use the PSA/ISMA Global Master Repurchase Agreement.

[15.05] **For historical comparison purposes**, behind the yellow sheet at [15.09] is a copy of Australian Addendum No. 9.

Our commentary on certain paragraphs in Australian Addendum No. 9 **that applied up to 31 December 2001** is as follows:

- (a) **Paragraph (1).** This states that by incorporating Australian Addendum No. 9 in their ISDA Master Agreement the parties agree that every REPO between them is governed by the ISDA Master Agreement whether or not its Confirmation refers to the Master Agreement or Australian Addendum No. 9 and whether or not the parties state in their confirmation that the REPO is governed by the terms of any other master agreement.

The wording of paragraph (1) recognises the practical issues involved in making a change from either not documenting REPOs under any master agreement or documenting REPOs under an existing master agreement. It is drafted on an assumption that once two parties agree to add Australian Addendum No. 9 to their ISDA Master Agreement, all future REPOs between them are intended to be governed by the ISDA Master Agreement. Paragraph (1) recognises that at an operational level, there may still be instances, after the changeover, when

Confirmations for REPOs either do not refer to the ISDA Master Agreement or continue to state that the REPO is governed by the terms of another master agreement. Paragraph (1) states that even in those circumstances the REPO will be governed by the ISDA Master Agreement and not any other master agreement.

If you want REPOs entered into before you incorporate Australian Addendum No. 9 into your ISDA Master Agreement also to be governed by Australian Addendum No. 9, then you should include the following provision in part 5 of the Schedule to your ISDA Master Agreement:

"(#) Despite anything contained in the attached September 1992 Australian Addendum No. 9 - Reciprocal Purchase Agreements, each REPO (as defined in that addendum) entered into between the parties before that addendum is incorporated in this Agreement is deemed to be a Transaction governed by the terms of that addendum and this Agreement. Clause 1 of that addendum applies to each such REPO as if it were a REPO referred to in that clause."

## Guide for completing Confirmations for REPOs

### [15.06] Preliminary comments

- (a) **Care! The comments in [15.06] and the suggested confirmations in [15.07] assume that Australian Addendum No. 9 is attached to your ISDA Master Agreement. See [15.04A]**

A REPO involves two related transactions. The first transaction usually is settled on the Trade Date when one party sells securities to the other for an agreed price.

If the first transaction is settled immediately (eg through Austraclear or RITS) it is unnecessary to otherwise confirm it. However, if the first transaction is not settled on the Trade Date (this is relatively rare), it is preferable to confirm it if it has not been entered in Austraclear or RITS. We have provided optional wording below to provide for this possibility.

This section of the guide has been prepared on the basis that the first transaction is treated as a normal sale of securities. However, the second transaction should be confirmed concurrently with the first transaction being settled, entered in Austraclear or RITS (if settlement is after the Trade Date) or confirmed.

The second transaction is the agreement by the buyer under the first transaction to sell on a future date to the seller under the first transaction securities equivalent to those sold under the first transaction. It is critical to the categorisation of a REPO as a sale and purchase that the buyer under the first transaction obtains absolute title to the securities sold to it under the first transaction. The buyer is not obliged to resell the actual securities sold under the first transaction and is free to deal with those securities as it sees fit. Its obligation in the second transaction is to sell equivalent securities (ie securities of the type and having the precise features as the securities sold under the first transactions). The definition of "Reciprocal Purchase Price" in Australian Addendum No 9 explains how the purchase price under the second transaction is calculated.

- (b) Using the confirmation set out at [15.07] as a guide, the information to be inserted in the confirmation is as follows:

- (i) The second paragraph is optional because the wording of clause 1 of Australian Addendum No. 9 achieves the same result. However, it is included because some participants may prefer to specifically refer to the Master Agreement in their confirmations. If so, ensure that the date of the Master Agreement is stated.
- (ii) **Trade Date.** The date the REPO is entered into (ie the date the first transaction is agreed).
- (iii) **Reciprocal Seller.** The party obliged to sell securities on the Reciprocal Purchase Date (ie the buyer under the first transaction).
- (iv) **Reciprocal Buyer.** The party obliged to buy securities on the Reciprocal Purchase Date (ie the seller under the first transaction).
- (v) **Agreed Features of securities.** Describe the agreed features of the securities subject to the REPO by reference to the issuer, the coupon rate, the maturity date and face value.
- (vi) **First Purchase Price.** The purchase price paid for securities under the first transaction on the First Purchase Date.
- (vii) **Contract Rate.** The rate to be applied to the First Purchase Price to calculate the Reciprocal Purchase Price under the second transaction where the Reciprocal Purchase Price is not agreed on the Trade Date.
- (viii) **Reciprocal Purchase Date.** It is not essential to specify a Reciprocal Purchase Date in the Confirmation. Many REPOs require settlement "on demand". Clause 4 of Australian Addendum No 9 sets out wording which provides for this.

However, if a Reciprocal Purchase Date is agreed on the Trade Date, it can be set out in the Confirmation.

(c) **Confirming variations to a REPO.**

**Contract Rate.** Paragraph (5) of Australian Addendum No. 9 provides that the Contract Rate agreed on the Trade Date applies for the Trade Date and each following date until otherwise agreed. By agreement, the parties can change the Contract Rate. It is for the parties to agree how they will confirm changes to the Contract Rate. For those parties wanting to confirm agreed changes in writing, there is a suggested form of supplementary confirmation at [15.08].

**Reciprocal Purchase Date.** If the parties set out an agreed Reciprocal Purchase Date in the Confirmation and later agree to change it, the variations can also be recorded in a supplementary confirmation.

**First Purchase Price.** Australian Addendum No. 9 has been prepared on the basis that if there is a change in the underlying value of the securities the subject of a REPO, the parties may agree to settle the existing REPO and enter into a new one where the First Purchase Price reflects the change in value of the securities.

(d) **Confirmation methods.** The following methods can be used to confirm. It is up to the parties to agree which method or methods will be used.

Electronic clearing house system (if available)  
Telephone  
Letter  
Telex  
Reuters direct dealing system  
Telerate trading service  
Facsimile

In [15.07] there is a recommended procedure for letter. However, this wording and all confirmation procedures must be completed in accordance with market conventions.

- (h) **Have you signed an ISDA Master Agreement?** Although not recommended, it is recognised that Transactions might be entered into before the parties have signed an ISDA Master Agreement. If that is the case, we recommend that you insert the following in the Confirmation or exchange letters agreeing to the substance of the following:

"You and we agree promptly to negotiate and sign a 1992 multicurrency - cross border version of the ISDA Master Agreement (as published by International Swaps and Derivatives Association, Inc.). Once an agreement based on that document is signed, this Confirmation is to supplement, form part of, and be subject to that agreement as amended and supplemented from time to time. All provisions contained in that agreement govern this Confirmation except as expressly modified below.

Until the agreement is signed, this Confirmation supplements, forms part of, and is subject to the terms contained in that document as if you and we had signed that document without amendment except that:

- (a) the Termination Currency is to be Australian dollars; and
- (b) the Governing Law is to be the laws of the state of [New South Wales]; and
- (c) September 1992 Australian Addendum No. 9 - Reciprocal Purchase Agreements as published in the AFMA Guide to OTC Documents is deemed to be incorporated in the document."

You must appreciate that this is not a complete substitute for signing an ISDA Master Agreement because there are numerous variables in the ISDA Master Agreement which will not operate until an election has been made. These are easily identified by looking through the Schedule to the ISDA Master Agreement. You should negotiate and sign an ISDA Master Agreement as soon as possible after adopting this approach.

[15.07] **Letter**

Suggested forms of letter. Version 1 is for when you only want to confirm the second transaction (generally, this is acceptable unless the first transaction does not settle on the Trade Date). Version 2 is for when you want to confirm both the first and second transaction.

<b>Version 1 - for confirming only second transaction</b>	
[Letterhead of Party A/B]	[Date]
Name and Address of Party B/A	
Dear	
<b>Reciprocal Purchase Agreement Confirmation</b>	
The purpose of this letter is to confirm the terms and conditions of a reciprocal purchase agreement entered into between us on the Trade Date specified below. This Confirmation supplements, forms part of, and is subject to, the Master Agreement dated as of [date], as amended and supplemented from time to time.	
Our reference:	
Trade Date:	
Reciprocal Seller:	
Reciprocal Buyer:	
Agreed Features of securities:	
Issuer:	
Coupon Rate:	
Maturity:	
Face Value:	
First Purchase Price:	
Contract Rate:	
[Reciprocal Purchase Date:]	
[Other provisions:]	
Yours sincerely [name of party preparing Confirmation]	
By:	
Name:	
Title:	

**Version 2 - for confirming  
first and second transaction**

[Letterhead of Party A/B]

[Date]

Name and Address of Party B/A

Dear

**Reciprocal Purchase Agreement Confirmation**

The purpose of this letter is to confirm the terms and conditions of a reciprocal purchase agreement entered into between us on the Trade Date specified below. This Confirmation supplements, forms part of, and is subject to, the Master Agreement dated as of [date], as amended and supplemented from time to time.

Our reference:

**FIRST TRANSACTION**

Trade Date:

Buyer:

Seller:

Agreed Features of securities:

Issuer:

Coupon Rate:

Maturity:

Face Value:

First Purchase Date:

First Purchase Price:

**SECOND TRANSACTION**

Reciprocal Seller:

Reciprocal Buyer:

Contract Rate:

[Reciprocal Purchase Date:]

[Other provisions:]

Yours sincerely

[name of party preparing Confirmation]

By:

Name:

Title:

[15.08] **Supplementary confirmations**

Variations to REPOs can be confirmed with a supplementary confirmation. Following is a suggested format for confirming as a letter. It should be appropriately amended if other forms of confirmation are used.

[Letterhead of Party A/B]		[Date]
Name and Address of Party B/A		
Dear		
<b>Reciprocal Purchase Agreement Supplementary Confirmation</b>		
The purpose of this letter is to confirm a variation to apply from the Variation Date specified below for the specified REPO.		
This Confirmation supplements, forms part of, and is subject to, the Master Agreement dated as of [date], as amended and supplemented from time to time.		
REPO Reference Number:	Reciprocal Seller:	
	Reciprocal Buyer:	
Reciprocal Seller:		
Reciprocal Buyer:		
Variation Date:		
Variations:		
	[New Contract Rate:]	
	[New Reciprocal Purchase Date:]	
	[Other]	
	Yours sincerely	
	[name of party preparing Confirmation]	
	By:	
	Name:	
	Title:	