

**February 9, 2007**

**MASTER FX GIVE-UP AGREEMENT AND COMPENSATION AGREEMENT**  
**USER'S GUIDE**

**I. INTRODUCTION**

The Master FX Give-Up Agreement (the “Agreement”) and Compensation Agreement are the products of in-depth discussions among participants in the foreign exchange prime brokerage market and represent an effort to standardize to the greatest extent possible the practices in this market. In response to the growth of the foreign exchange prime brokerage market, the Financial Markets Lawyers Group (“FMLG”) began a project in 2002 to prepare a master give-up agreement to document the relationship between a dealer that executes a foreign exchange transaction (the “Dealer”) and a prime broker which is intended to become the party to that transaction (the “Prime Broker”). After substantial initial efforts, the FMLG deferred its project so as to give market practice an opportunity to further develop. In 2005, the FMLG resumed its project. Each of the FMLG members who participated in this drafting effort worked closely with the prime brokerage, trading and operations personnel at his or her firm in order to reflect in the drafting process the many aspects of a prime brokerage business. These diverse contributions shaped the ultimate direction of the project and the provisions of the Agreement and Compensation Agreement. The Foreign Exchange Committee published the Agreement and the Compensation Agreement in April, 2005.

Foreign exchange prime brokerage refers to a process in which a party designated by the prime broker (defined as the “Designated Party” in the Agreement) executes a foreign exchange transaction with a dealer. The transaction is entered into with the expectation that the Prime Broker will be the party to the transaction with the Dealer in place of the Designated Party. The acceptance by the Prime Broker of the transaction executed by the Designated Party and Dealer is sometimes referred to as the give-up of the trade to the Prime Broker. Contemporaneous with the give-up of the trade, the Prime Broker will enter into an offsetting trade with either the Designated Party or one or more funds or accounts for which the Designated Party acts as trading manager.

The Agreement documents the relationship between the Prime Broker and the Dealer. It contains standard provisions that reflect generally accepted market practice for this relationship. In addition, with respect to several provisions, the Agreement allows the parties to select which of several clearly defined alternatives they want to apply to their bilateral agreement. Parties specify the alternatives that they choose in a Schedule that is a part of the Agreement.

Importantly, the Agreement has been designed as a single agreement that would be used by the Prime Broker and Dealer for their give-up relationship with respect to any Designated Party for which the Prime Broker would serve in that capacity. As a result, once the Agreement is signed by the parties, they would not sign another give-up agreement each time the Prime Broker obtains a new client that would be executing foreign exchange trades with that Dealer. In that situation, the Prime Broker and Dealer instead would sign a one page Give-Up Agreement Notice (the “Notice”) in the form attached to the Agreement as Exhibit 1. The Notice would contain all the necessary details (limits, types and tenors of trades) for the give-up of trades

executed by that new client with the Dealer. All of the terms of the Agreement, including those alternatives selected by the parties in the Schedule, would apply to the give-up of trades executed by each of the Prime Broker's clients. The Designated Party is not a party to either the Agreement or the Give-Up Agreement Notice. Rather, the Prime Broker and the Designated Party enter into a separate detailed agreement between them specifying the terms of their relationship, including the fees charged by the Prime Broker for its services. That agreement is not a part of the Master FX Give-Up Agreement and, due to the proprietary and confidential nature of its provisions, usually would not be provided to the Dealer.

The Compensation Agreement is an agreement between the Dealer and the Designated Party. It specifies that if a transaction is executed by the Designated Party with the Dealer that is not accepted by the Prime Broker, the Dealer can require that compensation be paid for any cost or expense that is incurred upon close-out of the position that resulted from the executed trade. In determining whether to seek to use the Compensation Agreement, Dealers should evaluate the likelihood that Prime Brokers will reject transactions when they enter into Master FX Give-Up Agreements and assess the possibility that they will incur trading losses as a result. In so doing, Dealers should evaluate the controls they have in place to reduce the chance of incurring such losses, which controls can include internal procedures designed to reduce the possibility of executing trades that may be rejected, use of the Compensation Agreement or some combination of methods. While the risk of a trade being rejected by the Prime Broker has generally been considered by market participants to be minimal, Dealers should consider the execution of a Compensation Agreement as a means of addressing that risk. Parties asked to sign a Compensation Agreement should recognize and understand the reasons a Dealer would ask them to do so.

This Guide in no way constitutes a part of, or should be interpreted as modifying, any contractual term contained in either the Agreement or Compensation Agreement. It is intended to explain the provisions of the Agreement and Compensation Agreement and the significance of their inclusion in the documents. Capitalized terms in the Guide have the respective meanings given them in the Agreement and Compensation Agreement unless specified otherwise.

## **II. MASTER AGREEMENT PROVISIONS**

### **Section 1. Construction and Definitions.**

The Agreement consists of three parts that are designed to be used together to document the contractual relationship between the Dealer and Prime Broker. The body of the Agreement, consisting of sections 1 through 9, contains the standard terms that reflect prevailing market practice and are intended to be applicable to all give-up relationships. The two parties sign this part of the Agreement on the signature page at the end. Attached to this part of the Agreement is the Schedule. The Schedule contains nine parts through which the parties select the alternatives that they want to apply to their Agreement and specify details applicable to their particular relationship such as the date of an applicable netting agreement and notice details. As it is part of the Agreement and should always be attached to it, the Schedule does not have to be signed separately.

Exhibit 1 to the Agreement completes the agreement and consists of the form of the Notice. The Prime Broker and Dealer would sign a Notice each time the Prime Broker designates a new client to execute trades for give-up to it. This Notice would identify the Designated Party

and contain the details of the types of trades and trading limits applicable to that specific Designated Party. The Notice represents an important document in the give-up relationship because the Prime Broker is obligated to accept transactions only if that are of the type and within the limits specified in the Notice.

Section 1 of the Agreement specifies the applicable rules in the event that any of these three parts of the documentation contain inconsistent provisions. It provides that in the event of any inconsistency between the provisions of sections 1 through 9 of the Agreement and the Schedule, the provisions of the Schedule prevail. This reinforces the principle that the parties use the Schedule to tailor the Agreement to their particular bilateral relationship. Furthermore, in the event of any inconsistency between the provisions of a Notice and the other provisions of the Agreement (including the Schedule), the Notice prevails. This provision gives flexibility to the parties to use the Notice to customize the give-up relationship for a particular Designated Party, although customary market practice is to use it only to specify products and trading limits.

#### **A. General Rule Applicable to Definitions.**

The general practice in the foreign exchange markets is to document transactions under a master agreement such as the ISDA Master Agreement or an IFEMA, ICOM, FEOMA or IFXCO agreement and to provide that the terms of the 1998 FX and Currency Option Definitions, including any supplements (the “FX Definitions”) apply to those transactions. Accordingly, section 1 specifies that any capitalized term that is used in the Agreement without being separately defined in the Agreement will have the meaning set forth in the Master Agreement and Definitions.

#### **B. Specific Definitions.**

1. Accepted Transaction. Accepted Transaction is defined in Part 5 of the Schedule. While Part 5 contains three alternative provisions, one of which will be selected by the parties to an Agreement, all three contain the same definition of Accepted Transaction as a transaction accepted by the Prime Broker upon satisfaction of the applicable conditions in Section 4(a) of the Agreement. Once a transaction has become an Accepted Transaction it is a binding transaction between the Prime Broker and the Dealer. Accordingly, Accepted Transaction is a key term in development of the rights and obligations of the parties to a give-up relationship.

2. Counterparty Transaction. Counterparty Transaction is defined in Section 2 of the Agreement to mean foreign exchange transactions executed by the Designated Party with the Dealer on behalf of the Prime Broker. These are transactions entered into with the express intention of the Designated Party and Dealer that they be submitted for give-up to the Prime Broker.

3. Counterparty FX Transactions. Counterparty FX Transactions are Counterparty Transactions that are spot, tom next or forward transactions.

4. Counterparty Option Transactions. Counterparty Option Transactions are Counterparty Transactions that are options.

5. Dealer Notice. Dealer Notice is defined in Section 4(b) as the notice that the Dealer sends to the Prime Broker with respect to each Counterparty Transaction that it executes with the Designated Party. This notice contains the economic terms of the transaction and is

provided so that the Prime Broker can match the details with the notice it receives from the Designated Party and determine whether the transaction is of a type and within the limits specified in the Give-Up Agreement Notice.

6. Designated Party. Each client of the Prime Broker identified in a Notice becomes a Designated Party for purposes of the Agreement. These are the parties for which the Prime Broker has agreed to accept the give-up of transactions executed with the Dealer.

7. Designated Party Notice. The Designated Party Notice is the notice given by the Designated Party to the Prime Broker with respect to each transaction that it has executed with the Dealer. The Designated Party specifies the economic terms of the transaction in the same manner as the Dealer does in the Dealer Notice (although as discussed below the Agreement does not require them to be specified in the same format). This notice should not be confused with the Give-Up Agreement Notice, which is the notice that specifies the name of the Designated Party and the trading limits applicable to it. The Give-Up Agreement Notice is signed once by the Prime Broker and Dealer prior to the Prime Broker commencing the acceptance of give-ups for a Designated Party. In contrast, the Designated Party Notice, which does not need to be signed by the Designated Party or the Prime Broker, is given by the Designated Party each time it enters into a new trade with the Dealer. In the agreement between them, the Prime Broker and Designated Party may want to agree on the methods by which a Designated Party can send a Designated Party Notice to the Prime Broker, such as fax or electronic transmission.

8. Dollar Value. For purposes of determining compliance with the trading limits in the Agreement, the measurement of outstanding positions under the Counterparty Transactions that have been executed for give-up is done in U.S. Dollars. Dollar Value refers to the U.S. Dollar equivalent of an amount specified in another currency and the definition specifies the method of determining this amount. The definition states that if the amount of currency in question is U.S. Dollars, the Dollar Value is that amount. If the currency is an amount of a currency other than U.S. Dollars, the Dollar Value is the amount of U.S. Dollars that could be purchased at the prevailing market rate with such other currency. The prime broker determines the applicable market rate, which is required to be the mid-market rate available to the Prime Broker in a foreign exchange market reasonably selected by the Prime Broker. That market would presumably be one in which the applicable foreign currency is widely traded. The parties specify in Part 1 of the Schedule whether this market rate is either a spot rate or forward rate. If the parties specify that it is the forward rate, the rate would be the forward rate for a transaction settling on the Settlement Date of the transaction for which the Dollar Value is being determined. It is expected that for most currencies, the Prime Broker will be able to obtain a mid-market rate based on trading in a recognized market. However, the definition further provides that if it is unable to do so, it will determine the rate in good faith and a commercially reasonable manner.

9. Master Agreement. Master Agreement means the master agreement used by the Dealer and Prime Broker to document the transactions entered into between them. This could be an ISDA Master Agreement or an IFEMA, ICOM, FEOMA or IFXCO agreement. Typically, the Master Agreement would be used by the Dealer and Prime Broker for direct trades between them as well as trades given up to the Prime Broker under the Agreement.

10. Material Terms. When a Counterparty Transaction is executed by the Designated Party and Dealer, each party will need to inform the Prime Broker of the economic terms of the transaction so that the Prime Broker can determine if the transaction is of the type and within the limits that it has specified in the Notice for that Designated Party. These economic terms are

referred to as the Material Terms. They include the terms specified in the definition, such as Settlement Date and the amount of currency to be delivered by each party, in the case of a spot or forward trade, and any other terms considered material in the market. As a result, in a barrier option trade, the barrier level and the characterization of the option as either knock-in or knock-out would need to be specified in the notices by the Dealer and Prime Broker as these terms are material to knowing the rights and obligations of the parties to the transaction. In addition, parties may wish to specify in the Schedule to the Agreement any other Material Terms that would be required for exotic options or other structured trades.

11. Net Daily Settlement Amount. To control their credit exposure to their clients, Prime Brokers typically specify a Settlement Limit or Net Open Position Limit or both as applicable to the Designated Parties for which they are acting. They would specify these limits in the Notice for the Designated Party. As a result, a Prime Broker does not have to accept the give up of a Counterparty Transaction if the Net Daily Settlement Amount exceeds the Settlement Limit. The Net Daily Settlement Amount is calculated with respect to all Counterparty Transactions executed by a particular Designated Party for a particular Settlement Date. As prime brokerage limits are specified under the Agreement for each Designated Party, a separate Net Daily Settlement Amount is determined for each Designated Party without any netting or aggregation of trades among several Designated Parties. The calculation with respect to a particular Settlement Date reflects the fact that the Net Daily Settlement Amount is a measure of daily settlement risk and not an indicator of overall position size or mark-to-market exposure.

In order to determine the Net Daily Settlement Amount applicable to a Designated Party, for each currency that is the subject of a Counterparty Transaction, the parties add the amounts payable by each of the Dealer and Prime Broker on the Settlement Date for which the calculation is being done. These amounts are then netted so that there is a single amount payable by either the Dealer or Prime Broker in the currency on the particular Settlement Date. The Dollar Value is then determined for the net amount for each currency. Lastly, the Dollar Values for the currencies in which the Dealer owes the Prime Broker a net amount are then added together to determine the Net Daily Settlement Amount. In effect, the definition provides for the calculation of the sum of the long positions, from the perspective of the Prime Broker, by currency bucket. Importantly, the Dollar Values for the currencies in which the Prime Broker owes the Dealer a net amount are not used in the calculation, and are not netted, against the Values in the currencies in which the Dealer owes an amount to the Prime Broker.

The calculation of Net Daily Settlement Amount involves several assumptions that are used in the calculation. Specifically, the calculation does not include option premia that may be owed to the Prime Broker and assumes that (i) Counterparty Option Transactions will be exercised on the Expiration Date of the Transaction, and (ii) Non-Deliverable Counterparty FX Transactions will settle through actual exchange of the currencies rather than a net payment in the Settlement Currency. While the definition includes these assumptions, it does not change the actual terms of the Transactions which are governed by the applicable confirmations, FX Definitions and Master Agreement.

12. Net Open Position. The second measure of trading limits is the Net Open Position. Unlike the Net Daily Settlement Amount, the Net Open Position represents an aggregate calculation for all Counterparty Transactions executed by a Designated Party irrespective of which day they are settling. However, in a manner similar to the Net Daily Settlement Amount, the Net Open Position is determined separately for each Designated Party because the trading limits under the Agreement apply separately to each Designated Party. The

definition is intended to operate in conjunction with Part 2 of the Schedule in which the parties elect the methodology to use for determining the Net Open Position for options.

The Net Open Position equals the aggregate amount owed by the Dealer to the Prime Broker, calculated in accordance with a formula that has several steps:

(A) First, for each Counterparty FX Transaction, which includes spot, tom next and forward transactions, the Dollar Value of each payment owed by either the Dealer or Prime Broker is calculated. This calculation assumes that under a Non-Deliverable Forward each party would actually deliver the currency amount that it sold rather than settle in a single net payment.

(B) Next, for each currency, the net Dollar Value of the amounts owed by the Dealer and Prime Broker to each other is determined.

(C) In the case of Counterparty Option Transactions, the Dollar Value of the Transaction is determined in accordance with the method specified in the Schedule, and

(D) The net Dollar Value amounts determined in accordance with clause (B) for Counterparty FX Transactions are aggregated with the amounts determined for Counterparty Option Transactions in clause (C) pursuant to the method specified in the Schedule.

13. Netted Option. The provisions of Part 2 of the Schedule that specify the method for determining the Net Open Position for Counterparty Option Transactions exclude Netted Options from the calculation. This approach reflects the market practice that Transactions that are offsetting and, which do not present any market or credit risk should not be counted in Net Open Position calculations. In order for two Transactions to be treated as Netted Options, they should be offsetting buys and sells with the same material terms that are executed by the same Designated Party. The only exception to this principle is that where the currency amounts are different, a partial discharge and termination shall occur for purposes of the Net Open Position definition and only the portion that is discharged and terminated will be considered a Netted Option. The Netted Option provision of the Agreement applies to the Net Open Position calculation irrespective of the presence of any discharge and termination provisions in the applicable Master Agreement.

14. Notice. The term "Notice" means the Give-Up Agreement Notice that a Prime Broker and Dealer sign to specify that a Designated Party is authorized to execute certain Counterparty Transactions in the name of the Prime Broker.

15. Notice of Barrier Event. Most barrier options are transacted under terms that require the calculation agent to give notice to the other party to the trade if a barrier is touched or breached under the option. The Agreement refers to such a notice as a Notice of Barrier Event and contains provisions addressing such notices in Section 5(c).

16. Proceedings. Proceedings means any suit, action or other proceedings related to this Agreement.

## **Section 2. Authorization.**

Section 2 contains the general provision in which the Prime Broker authorizes the Designated Party to execute trades with the Dealer for give up. It provides that this authorization is a limited one in, that the Counterparty Transactions which the Designated Party is authorized to execute are limited to the types, maximum tenors, currencies and Specified Offices of each party as specified in the Notice for that Designated Party. The authority given to a Designated Party is customarily for the execution of transactions only. To clarify one aspect of that limit on a Designated Party's authority, this Section specifies that the Designated Party's authority does not extend to the settlement of any transaction. In particular, it provides that the Designated Party may not make or receive deliveries of currencies on behalf of the Prime Broker or give any direction in respect of delivery of currencies. In this regard, Section 2 distinguishes a Designated Party from a typical investment manager which can both execute transactions and manage the settlement of those transactions. Section 2 would not, however, restrict the Designated Party's ability to execute an offsetting transaction that may reduce or eliminate the amounts payable by either the Dealer or Prime Broker in settlement of an existing transaction.

As discussed above, the Prime Broker and Dealer evidence the authority given to a Designated Party through a Notice. Section 2 provides that this Notice will be in the form of Exhibit 1 to the Agreement. This Section also specifies that any Counterparty Transactions entered into under this Agreement and given up to the Prime Broker will be subject to the Master Agreement between the Dealer and Prime Broker. The parties typically will not execute a separate Master Agreement for give up trades but will generally use the existing Master Agreement that would govern their direct trades with each other. This approach maximizes the netting benefits to both the Dealer and Prime Broker and reflects the view in the market that once a trade is given up to a Prime Broker, it will be treated in the same manner and give rise to the same rights and obligations as any other trade between the Prime Broker and Dealer.

### **Section 3.      Limits.**

When a Prime Broker authorizes a Designated Party to execute trades for give up to it, the Prime Broker specifies trading limits in addition to the product and office limits referenced in Section 2. The provisions of Section 3 establish the general rule that the authority given to a Designated Party is limited to a Net Daily Settlement Amount not to exceed the Settlement Limit and a Net Open Position not to exceed the Net Open Position Limit. The Prime Broker would specify the Settlement Limit and Net Open Position Limit in the Notice. The Agreement does not require a Prime Broker to use either limit, and some Prime Brokers use only a Settlement Limit. A Prime Broker may be willing to accept give-ups without a Net Open Position Limit when its credit line with a Dealer is very large or its trades with that Dealer are collateralized. This could occur in a situation in which the Prime Broker and Dealer are each collateralizing their positions with each other. In that case, the Prime Broker may not deem it necessary to limit the use of its credit lines with a Net Open Position Limit. Both the Settlement Limit and Net Open Position Limit are specified for each Designated Party and apply only to trades executed by that Designated Party with the Dealer.

### **Section 4.      Accepted Transactions.**

(a) Sections 2 contains the fundamental agreement by the Prime Broker that it has granted authority to the Designated Party to execute Counterparty Transactions with the Dealer on its behalf, subject to certain limits described in that Section and Section 3, together with the Notice. Based on those concepts, Section 4(a) establishes the basic rule that a Prime Broker is not liable for any Counterparty Transaction unless certain specified conditions are met. These

conditions are the terms that must be complied with in order for a Counterparty Transaction to become an Accepted Transaction. Specifically, the Section specifies six conditions:

- (i) The Counterparty Transaction is one of the types of transactions permitted under the Notice. This means that it is a product type that is permitted by the terms of the Notice, only involves the permitted currencies and does not exceed any tenor limits that are specified.
  - (ii) As discussed above, giving effect to the Counterparty Transaction must not cause either the Net Daily Settlement Amount or Net Open Position to exceed the limit applicable to a Designated Party without the prior written consent of the Prime Broker. The Agreement permits exceptions to be made only in writing (which could include fax or email if specified in the Schedule), in order to avoid the misunderstandings that can arise from oral communications.
  - (iii) The Dealer and Designated Party must have committed to the Material Terms of the Counterparty Transaction. This means that the Dealer and Designated Party must have agreed on these terms in a manner that, if the give up is accepted by the Prime Broker, will be binding on the Dealer and the Prime Broker. As a result, all parties will have the assurance that if the give up is accepted by the Prime Broker, there will be a binding and enforceable transaction between the Prime Broker and Dealer. This condition does not require that the Counterparty Transaction be entered into by any specific means, such as telephone or electronic dealing, so long as the relevant communications represent a commitment to the terms of the trade by the parties.
  - (iv) The Counterparty Transaction must have been entered into by the Dealer acting through a Specified Office. Specified Offices are designated in each Notice. Parties may want to limit Specified Offices, and not engage in give ups of trades from other offices, if they want the trades to be covered by a Master Agreement between them that covers a limited number of offices of each party.
  - (v) In order for the Prime Broker to determine the details of the Counterparty Transaction and determine if it is within the permitted limits, the Prime Broker must receive a Dealer Notice.
  - (vi) If the parties specify it as applicable in the Schedule, it is also a condition to the Prime Broker's obligation to accept a Counterparty Transaction that it receive from the Designated Party a Designated Party Notice setting forth Material Terms that match those in the Dealer Notice. Some Prime Brokers may want to have this condition apply so that they will not have to accept a Counterparty Transaction unless they receive this Designated Party Notice, while others may address the issue in their agreement with the Designated Party.
- (b) Section 4(b) complements Section 4(a) by requiring the Dealer to promptly communicate the Material Terms of each Counterparty Transaction to the Prime Broker. To permit the parties flexibility with respect to communication of these terms and allow for changes in technology, Section 4(b) provides that the communication can be through Reuters or any other system on which the parties mutually agree. It permits notification of the Material Terms through telephone communication in the event that Reuters or any other agreed method is not operating. This approach reflects the market practice to not use the telephone as the primary means of

communicating trade details because it does not give a printed or electronic record of the conversation and is more susceptible to errors than other means of communication.

(c) The Agreement allows the parties to specify in Part 5 of the Schedule the trade acceptance provisions that they want to apply. In addition, parties may, but are not required to, agree that the Prime Broker has other notification obligations by specifying the provisions of Part 6 of the Schedule to be applicable.

## **Section 5.      Exercise of Options.**

As foreign exchange option transactions have increasingly become the subject of prime brokerage, parties have sought more efficient ways of exercising these options and giving notices with respect to them. In that regard, Section 5 reflects several practices that have been developed in the prime brokerage market to address these needs.

(a) Section 5(a) applies to the situation in which the Dealer has sold an option to the Designated Party and the Designated Party has given up the trade to its Prime Broker. At that point, the Dealer has a trade with the Prime Broker and the Prime Broker has a trade with the Designated Party. As the Designated Party is the party that has the economic risk from the transaction, it rather than the Prime Broker will typically be monitoring whether, and when, the option should be exercised. Accordingly, any notice of exercise would usually start with the Designated Party. This clause provides that if the Designated Party gives the notice of exercise directly to the Dealer, that notice will be effective as exercise by the Prime Broker. This approach can be particularly beneficial in situations in which an option is exercised shortly before its expiration time, as often occurs, because it avoids the need for two separate notices to be given to complete the exercise, one by the Designated Party to the Prime Broker and another by the Prime Broker to the Dealer. However, as this Section does not require the Designated Party to give the notice of exercise, a Prime Broker may wish to clarify in its agreements with its client whether the client or the Prime Broker will give the notice of exercise to the Dealer.

(b) The same recognition that the Designated Party is the party with the economic interest in the option applies in Section 5(b). This clause applies when the Dealer has purchased an option from the Designated Party. In that case, the Dealer has a transaction on its books with the Prime Broker although it is the Designated Party that has the economic risk of the transaction. Section 5(b) provides that in this situation, if a Dealer exercises the option, it must do so by giving notice to both the Prime Broker and the Designated Party. This approach does not require any change in the manner in which the Dealer has booked the option as its legal counterparty is still the Prime Broker. To address the notification responsibilities arising from this clause, a Dealer would typically add the Designated Party's notice address to its operations data so that any notice would go to that address as well as to the Prime Broker.

(c) Consistent with subsection (b), Section 5(c) provides that if the Dealer is the calculation agent with respect to an option with knock-in or knock-out features, the Dealer must notify the Designated Party and the Prime Broker of the occurrence of a knock-in or knock-out event by delivery of a Notice of Barrier Event. This would allow the Designated Party, which has the economic risk of the transaction, to manage its position effectively while eliminating the need for the Prime Broker to send a duplicate notice after receiving one from the Dealer. (The Barrier Option Supplement published by the Foreign Exchange Committee provides that the notices of barrier events are sent by the "Barrier Determination Agent". This party would typically be the calculation agent in the transaction. If, however, the Dealer is calculation agent but not the

Barrier Determination Agent, Section 5(c) is not intended to impose a duty to send notices on the Dealer that it would not have under the confirmation or other documents governing the transaction.)

(d) The FX Definitions, which are typically incorporated into Master Agreements, contain provisions for automatic exercise of options. The provisions of Section 5 do not override those provisions, so that if an option is treated as automatically exercised under the FX Definitions, that exercise would be effective without the notice otherwise required in section 5(a) or (b) with respect to an option given up to a Prime Broker.

## **Section 6. Representations/Warranties.**

Section 6 contains representations, warranties and covenants that are made by the Dealer and the Prime Broker as of the date of the Agreement and as of the date of each Counterparty Transaction. These include representations as to their authority to enter into the Agreement and each Counterparty Transaction, the enforceability of the Agreement against them and their reliance on the Agreement in entering into Accepted Transactions.

## **Section 7. Termination/Change.**

(a) As with many other master agreements, the Agreement remains in effect unless and until terminated by either the Prime Broker or the Dealer. Section 7(a) requires that this termination must be communicated in writing to the other party by the party electing to terminate. The Agreement does not require that notification of termination be given to any Designated Party in order for it to be effective. Upon termination becoming effective in accordance with Section 7(c), the Prime Broker would no longer have to accept transactions that are executed after that time. The Prime Broker still would be obligated to accept any Counterparty Transactions that comply with the parameters set forth in the Agreement if those Counterparty Transactions were executed prior to the termination becoming effective, even if the Prime Broker received notice of the Transactions after the termination became effective. However, note that Section 4(b) requires the Dealer to promptly communicate the Material Terms of each Counterparty Transaction to the Prime Broker. Accordingly, the Dealer would need to act in a timely manner in order to fulfill its obligations with respect to a Transaction submitted for give up after termination of the Agreement.

(b) A Notice identifies a Designated Party as authorized to enter into Counterparty Transactions and specifies the types of transactions and trading limits applicable to that Designated Party. The Agreement provides in Section 7(b) that a Prime Broker may amend the Notice in whole or in part at any time by a communication given to the Dealer in writing. (Section 8 provides that a communication required to be in writing may be given by facsimile transmission or e-mail if a facsimile number or e-mail address is specified for the intended recipient in the Schedule.) Section 7(b) gives the Prime Broker the ability to modify the types of transactions and trading limits applicable to a Designated Party. This modification could include reducing the trading limits to zero so as to effectively terminate the ability of a Designated Party to give up transactions with the Dealer to the Prime Broker. The Agreement, however, would continue to be in effect so that other Designated Parties could continue to enter into and give up transactions to the Prime Broker.

(c) Section 7(c) provides that any notification of termination under Section 7(a) or amending a Notice under Section 7(b) will be effective one hour after receipt by the other party.

If the notification is delivered when the recipient is not open for business, it will become effective one hour after the recipient next opens for business. This section is intended to allow a party to quickly either terminate the Agreement or modify a Notice while giving the recipient one hour to react to the notification. In particular, upon receipt of a termination notice or a notification reducing trading limits, a Dealer would typically notify its sales or trading personnel who would be contacted by the Designated Party so that they know of the termination or new limits and, if necessary, could decline to execute new Counterparty Transactions with that Designated Party.

## **Section 8. Notices/Communications.**

(a) Section 8(a) provides that unless otherwise specified in the Agreement, notices, instructions and other communications to be given under the Agreement can be given in writing or by facsimile transmission, electronic messaging system, e-mail or telephone. The ability to use this broad range of communication media gives parties the flexibility to implement new methods of communication, such as electronic platforms, as they are developed. Notices given under the Agreement are effective upon receipt unless the Agreement specifies otherwise. For example, Section 7(c) provides that notifications of termination of the Agreement or amendment of a Notice are effective one hour after receipt.

Importantly, Section 8(a) specifies that a notice required to be in writing may be given by facsimile transmission or e-mail if a facsimile number or e-mail address is specified for the intended recipient in the Schedule. As a result, parties should consider whether they want to receive notices that have to be in writing, such as those given under Section 7, through these means before including a facsimile number or e-mail address in the Schedule. If a party includes a facsimile number or e-mail address, it should be for a facsimile machine or e-mail account that is monitored frequently throughout the business day so that appropriate personnel will be able to take any necessary action in response to the notice.

(b) Parties in the financial services industry frequently record telephonic conversations for use in resolution of any disputes arise in connection with transactions. Accordingly, Section 8(b) permits such recording and contains the agreement that any such recording can be submitted in evidence in any litigation that may arise.

## **Section 9. Miscellaneous.**

Section 9 includes provisions addressing the effect of the invalidity or unenforceability of a provision of the Agreement, waivers, amendments, governing law and a waiver of trial by jury.

Section 9(c) requires that any amendments or modifications to, or waivers of, the Agreement be in writing and signed by both the Prime Broker and Dealer. However, this Section does not require the Prime Broker or Dealer to sign a waiver of a trading limit under Section 4(a)(ii) or override or modify the right of a Prime Broker to amend a Notice by a written communication sent to the Dealer as provided in Section 7(b). Such an amendment would not have to be agreed to by the Dealer or signed by either the Prime Broker or Dealer. Parties may also choose to make modifications to the terms of the Agreement by specifying those modifications in the Schedule.

Section 9(d) provides that the Agreement is governed by New York law and contains a submission by each party to the non-exclusive jurisdiction of the state and federal courts located in Manhattan. The Agreement was not specifically drafted to be used under a governing law

other than that of the State of New York and parties that wish to specify the law of another jurisdiction as governing should have the Agreement reviewed by counsel qualified in that jurisdiction prior to specifying that law. Parties that wish to specify a governing law other than New York may do so in the Schedule to the Agreement.

### **III. SCHEDULE PROVISIONS**

#### **Part 1. Calculation of Dollar Value.**

The determination of Net Open Position involves the conversion of currency amounts owed to or by the Prime Broker to U.S. Dollars at a mid-market rate. This U.S. Dollar amount is defined as the Dollar Value. Part 1 allows parties to choose whether they want to determine the Dollar Value using either the spot or forward rate for the applicable currency pair. As the Agreement does not provide a fallback rate, parties should choose either the spot or forward rate in their Schedule.

#### **Part 2. Calculation with respect to Counterparty Option Transactions.**

The definition of Net Open Position is primarily contained in Section 1. However, participants in the prime brokerage market use several different methods of determining the Net Open Position for Currency Option Transactions and combining the amount determined for spot and forward transactions with the amount determined for options for the purpose of determining the Net Open Position for all transactions. Part 2 specifies two commonly used methods of making this determination and combination. Parties should choose one of the methods specified or may choose another method and add that to their Schedule. However, as the Agreement does not provide a fallback combination method, parties need to specify some method of determining the Net Open Position for Currency Option Transactions and combining cash and option transactions in order for the Net Open Position methodology to produce a final Net Open Position amount.

While parties should review the two choices carefully, in summary, the first choice provides for parties to determine the delta equivalent for each Currency Option Transaction and multiply it by the amount that would be received by the Prime Broker from the Dealer if the Counterparty Option Transaction were exercised. The Dollar Value of these amounts for each Counterparty Option Transaction is then added to the amount determined for cash transactions pursuant to clause (B) of the Net Open Position for each currency with respect to which the Dealer owes a net amount to the Prime Broker. The sum of these amounts is the Net Open Position. The second choice differs from the first choice in that it specifies that the delta equivalent amount will be determined for each leg of the currency pair of a Counterparty Option Transaction. These amounts are then added to the currency amounts payable to or by a Prime Broker for cash transactions for each currency. The Dollar Values of the currency amounts for each currency with respect to which the Dealer owes a net amount to the Prime Broker are then added to obtain the Net Open Position. Documentation personnel who are negotiating an Agreement may wish to consult with operations or other personnel at their institution regarding their preference with respect to this calculation.

#### **Part 3. Master Agreement.**

Section 2 provides that any Counterparty Transactions entered into under the Agreement are subject to the “Master Agreement” between the Prime Broker and the Dealer. In Part 3, the parties identify that Master Agreement by specifying its type and date.

**Part 4. Conditions.**

If the parties specify it as applicable in the Schedule, pursuant to clause 4(a)(vi) of the Agreement, it is an additional condition to the Prime Broker’s obligation to accept a Counterparty Transaction that it receive from the Designated Party a Designated Party Notice setting forth Material Terms that match those in the Dealer Notice. The parties specify in Part 4 of the Schedule whether this condition is applicable. In order to clarify the conditions for acceptance of a Counterparty Transaction, parties should specify that the clause is either applicable or not applicable in this Part. If they do not make any specification the clause will not be applicable.

**Part 5. Trade Acceptance.**

Section 4(c) of the Agreement provides that the trade acceptance provisions selected in Part 5 of the Schedule will be applicable. These provisions determine whether the Prime Broker has any additional notification obligations that affect whether Counterparty Transactions will become Accepted Transactions.

Part 5 contains three alternatives, each of which addresses the Prime Broker’s notification obligations with respect to Accepted Transactions. Importantly, each alternative provides that upon satisfaction of the applicable conditions specified in Section 4(a), a Counterparty Transaction shall be deemed accepted by the Prime Broker. This provision clarifies that if the Section 4(a) conditions are satisfied, the Counterparty Transaction must become an Accepted Transaction regardless of whether any notice is given by the Prime Broker. As a result, the Dealer has the contractual agreement of the Prime Broker that if those conditions are satisfied it will have a binding transaction between it and the Prime Broker. For that reason, the notice provisions set forth in these alternatives only affect those Counterparty Transactions that do not satisfy the Section 4(a) conditions and which would not otherwise be Accepted Transactions. Parties should select one of the three alternative provisions to apply in their Agreement, as the Agreement does not contain any fallback provision that specifies when a Counterparty Transaction is deemed accepted by a Prime Broker in this case.

The first alternative provides that the Prime Broker does not have an obligation to notify the Dealer of its acceptance of a Counterparty Transaction. However, Prime Brokers and Dealers often develop practices outside of the give-up agreements between them regarding how the Prime Broker notifies the dealer of its acceptance of transactions. These practices, which can involve use of the confirmation process, are not restricted by electing this first alternative.

The second alternative also provides that the Prime Broker does not have an obligation to notify the Dealer of its acceptance of a Counterparty Transaction. In addition, it adds that if the Prime Broker does not notify the Dealer of its acceptance or rejection of a Counterparty Transaction within the specified Number of Hours after receipt of the Dealer Notice, the Counterparty Transaction is deemed accepted by the Prime Broker based on the Material Terms included in the Dealer Notice if the applicable conditions set forth in Section 4(a) have been met and any mismatch between the Dealer Notice and Designated Party Notice has been resolved. The parties would specify the Number of Hours applicable to this alternative in this Part of the Schedule. This alternative contemplates a notification procedure by the Prime Broker with

respect to trade acceptance although it would result in acceptance of the same Counterparty Transactions as the first alternative.

The third alternative provides that if the Prime Broker does not notify the Dealer of its acceptance or rejection of a Counterparty Transaction within the specified Number of Hours after receipt of the Dealer Notice, the Counterparty Transaction is deemed accepted by the Prime Broker based on the Material Terms included in the Dealer Notice. It does not add the conditions contained in the second alternative, which are that the applicable conditions set forth in Section 4(a) have been met and any mismatch between the Dealer Notice and Designated Party Notice has been resolved. As a result, if the Prime Broker did not give the required notice within the specified Number of Hours, this third alternative would cause Counterparty Transactions to become Accepted Transactions even if the conditions set forth in Section 4(a) were not met. The effect of this alternative is to add another method for a Counterparty Transaction to become an Accepted Transaction, in addition to the standard method of satisfying the conditions in Section 4(a).

#### **Part 6. Notification by Prime Broker.**

Section 4(c) also provides that the Prime Broker shall comply with the applicable notification requirements, if any, set forth in Part 6 of the Schedule. Parties should specify in Part 6 whether these notifications provisions are applicable or not applicable.

If specified as applicable, the notification provisions require the Prime Broker to notify the Dealer if (i) the Material Terms set forth in a Dealer Notice do not match the Material Terms set forth in the Designated Party Notice within a period equal to the Number of Hours after the Prime Broker's receipt of the later of those two notices, or (ii) the Prime Broker has not received a Designated Party Notice with respect to the Counterparty Transaction that is the subject of a Dealer Notice within a period equal to the Number of Hours after receipt of that Dealer Notice. As in Part 5, the parties specify the Number of Hours applicable to these provisions in the Part. In contrast to the notification provisions in Part 5, which address when a Counterparty Transaction becomes an Accepted Transaction, the provisions in Part 6 do not effect that determination.

Part 6 specifies that the Prime Broker is not responsible or liable for any failure or delay in notifying Dealer as required by Part 6 arising directly or indirectly from circumstances beyond its reasonable control. While Part 6 does not specify the circumstances that would excuse any failure or delay in giving notice, they would reasonably include, among others events, power failures, natural disasters such as hurricanes or other storms and events such as bank holidays, strikes and civil unrest.

#### **Part 7. Notices pursuant to Section 8.**

Parties should specify their addresses and, if applicable, phone numbers for notices in Part 7. As provided in Section 8, a party may change its notice details at any time by giving notice to the other party in accordance with Section 8. As discussed above, Section 8(a) specifies that a notice required to be in writing may be given by facsimile transmission or e-mail if a facsimile number or e-mail address is specified for the intended recipient in the Schedule. As a result, parties should consider whether they want to receive notices that have to be in writing, such as those given under Section 7, through these means before including a facsimile number or e-mail address in the Schedule.

## **Part 8. Notice Periods.**

Part 8 provides for two alternative methods of determining when the Prime Broker's receipt of a Dealer Notice becomes effective. Parties should choose one of these methods as applicable to their Agreement.

The first alternative is designed for Prime Brokers which maintain 24 hour per day operations centers for their prime brokerage business. It provides that a Dealer Notice will be effective if received in the locations specified in the Schedule at any time beginning at 5:00 a.m. Sydney time on Monday in any week until 5:00 p.m. New York time on Friday. A Prime Broker that uses this approach should specify in Part 7 the applicable locations to which notices should be delivered during each time period in the business day. For example, some Prime Brokers may choose to have notices sent to their New York office from 6:00 a.m. to 6:00 p.m. New York time and then sent to an office in Asia from 6:00 p.m. to 6:00 a.m. New York time on each business day.

The second alternative is designed for Prime Brokers that maintain prime brokerage operations only during the business day in one location. This alternative provides that a Dealer Notice is effective if received by the Prime Broker in the locations indicated in the Schedule on any Monday through Friday from 9:00 a.m. to 5:00 p.m. in the location, excluding days that are not business days in the location.

## **Part 9. Electronic Trading Platforms.**

Participants in the prime brokerage market increasingly use electronic platforms for execution and give-up of foreign exchange transactions upon agreement of the Prime Broker, Dealer and the Designated Party. The Agreement may be used for the give-up of those transactions. If parties should decide to do so, they should consider whether any modifications are necessary to accommodate the means by which transactions are executed and given up, including the types of trading limits applicable to the platform.

In addition, these platforms often have detailed rules and procedures for notices. Accordingly, Part 9 specifies that in that situation, notices required under the Agreement may be made in accordance with those rules in lieu of the provisions set forth in the Agreement. As a result, notices that otherwise may have to be in writing or directed to a particular notice address may be accomplished through the electronic functions contained in that platform and described in its rules. As the interaction of the electronic trading platform rules and the provisions of the Agreement may be complex, parties should evaluate whether they want to add any specific provisions to the Schedule addressing the applicability of those rules to specific notification procedures provided under the Agreement.

## **IV. GIVE-UP AGREEMENT NOTICE**

The Give-Up Agreement Notice is the document used by the Prime Broker and Dealer to specify that a client of the Prime Broker is a Designated Party under the Agreement. The Notice

is a bilateral document signed by both the Prime Broker and Dealer and supplements and forms a part of the Agreement. While the Notice has not been designed for use as an amendment to the Agreement, in the event of any inconsistency between the Notice and the other provisions of the Agreement (including the Schedule), the Notice will prevail. In the Notice, the Prime Broker specifies the types of transactions that the Designated Party may execute for give-up under the Agreement and trading limits applicable to the Designated Party. A Notice remains in effect until either the Agreement terminates or the Notice is amended or terminated by the Prime Broker.

The Notice first specifies the name of the Designated Party. Frequently, the Designated Party will be a trading manager acting on behalf of several funds or accounts. In this situation, it is not necessary to identify the funds or accounts, as they generally will not be disclosed to the Dealer by the Designated Party or the Prime Broker. In addition, they may change as the manager's business develops during the time the Notice is in effect.

In the Notice, the Prime Broker would also specify the types of Counterparty Transactions authorized for the identified Designated Party. These can differ from the Counterparty Transactions authorized for other Designated Parties of that Prime Broker. For Currency Option Transactions, the Prime Broker should specify the types of options that are authorized, such as plain vanilla options and single barrier options. The Prime Broker should separately specify whether deliverable and non-deliverable forwards and options are permitted. The Notice also contains entries for Permitted Currencies and Maximum Tenor of the Counterparty Transactions. In the event that a Prime Broker is willing to permit a Designated Party to trade any currencies, it should specify "All" in the entry for Permitted Currencies. In addition, the Notice provides for specification of the Settlement Limit and Net Open Position Limit. These limits typically would be specified in U.S. Dollars. If the Prime Broker should choose to specify a limit in another currency for a particular Designated Party, the parties should amend the definitions of Net Daily Settlement Amount and Net Open Position as applicable to that Designated Party so that they provide for amounts determined in the other currency or provide for conversion of the Net Daily Settlement Amount and Net Open Position to that other currency so that those amounts can be measured against the specified limits.

Lastly, the parties should identify their Specified Offices, as the Agreement is designed for transactions entered into by the parties through those offices. More specifically, Section 4(a) provides that it is a condition of acceptance of a Counterparty Transaction by a Prime Broker that the Counterparty Transaction has been entered into by Dealer acting through a Specified Office.

## **V. COMPENSATION AGREEMENT PROVISIONS**

The Compensation Agreement is an agreement between the Dealer and the Designated Party. It specifies that if a transaction is executed by the Designated Party with the Dealer that is not accepted by the Prime Broker, the Dealer can require that compensation be paid for any cost or expense that is incurred upon close-out of the position that resulted from the executed trade.

Section 1 of the Compensation Agreement contains the agreement of the Designated Party to promptly provide notice to the Prime Broker of the Material Terms of a transaction executed with the Dealer pursuant to a Designation Notice. This notice is the Designated Party Notice referenced in the Give-Up Agreement. If the Prime Broker and Dealer choose to make clause 4(a)(vi) applicable, delivery of this notice to the Prime Broker will be a condition to a

Counterparty Transaction becoming an Accepted Transaction under the Give-Up Agreement. “Material Terms” is defined in the same manner as in the Give-Up Agreement.

Section 2 contains two alternative provisions, each in brackets, that permit the Dealer at its discretion to require that compensation be paid in the event a Counterparty Transaction executed by the Designated Party with the Dealer is not accepted by the Prime Broker under the Give-Up Agreement. Parties should include one of these provisions in their Compensation Agreement. The Dealer must give the Designated Party a notice that it is exercising its rights under this Section.

The first alternative provides that either the Dealer or Designated Party will pay compensation to the other in an amount determined as if the Dealer and Designated Party were parties to a ISDA 2002 Master Agreement and an Early Termination Date were designated under that Agreement as a result of a Termination Event. The Dealer would specify the Early Termination Date, which cannot be later than two Banking Days in the Dealer’s location after the trade date of the Counterparty Transaction. The amount would be determined as if the Counterparty Transaction were the sole Terminated Transaction and the Designated Party were the sole Affected Party. The effect of these provisions is that the amount payable would be determined by the Dealer and would be payable by either the Designated Party or the Dealer, depending on prevailing market rates at the time of determination. The amount would be payable one Banking Day in the Dealer’s location after its calculation, if payable by the Dealer, or on the effective date of a notice by Dealer to Designated Party of the amount payable if it is payable by the Designated Party.

The second alternative provides that the Designated Party will indemnify Dealer for any loss or costs incurred by Dealer in connection with the Counterparty Transaction, including loss of bargain or the cost of terminating or liquidating any hedge or related trading position. In contrast to the first alternative, this alternative only provides for a payment from the Designated Party to the Dealer, although any payment would only be owed if the Dealer incurred a loss or cost as a result of the Prime Broker not accepting the Counterparty Transaction.

Section 3 of the Compensation Agreement includes representations of the Designated Party and Dealer similar to those made by the Dealer and Prime Broker in the Give-Up Agreement.

Section 4 provides that the Compensation Agreement will terminate upon the termination of the authority of the Designated Party to enter into Counterparty Transactions under the Give-Up Agreement. However, Section 4 specifies that the Compensation Agreement remains in effect with respect to all Counterparty Transactions entered into by Designated Party with the Dealer on or before the day on which that termination is effective. This provision is intended to permit the parties to apply the Compensation Agreement to those trades if they should be rejected by the Prime Broker. This Section also specifies that a reduction by the Prime Broker of the Settlement Limit or Net Open Position Limit set forth in the Designation Notice will not constitute termination of the Designated Party’s authority to enter into Counterparty Transactions under the Give-Up Agreement. If a limit is reduced to an amount below the level of the outstanding Net Daily Settlement Amount or Net Open Position, the Designated Party will temporarily be unable to execute additional trades under the Give-Up Agreement. However, if the existing Accepted Transactions mature, such that the Net Daily Settlement Amount or Net Open Position again should be below the new limit, the Designated Party would have authority to execute additional

Counterparty Transactions, unless its authority was in some other way terminated by the Prime Broker.

Sections 5 through 11 contain procedural and interpretive provisions consistent with those in the Give-Up Agreement.