ICOM Close-Out Example

Bank A, a U.S. bank ("Party A"), and Corporation B, a French corporation ("Party B"), have signed a New ICOM Agreement or otherwise have an agreement subject to New ICOM terms (in either case, the "Agreement"). Party A's Base Currency is the U.S. Dollar.

Party B files for bankruptcy on September 1, 1995 (a Friday). Party A learns of the bankruptcy on Tuesday, September 5. (Monday, September 4, was Labor Day, a U.S. bank holiday). In Part IX of the Schedule to the Agreement, the Parties have chosen "Automatic Termination" upon an Event of Default.

At the time of the bankruptcy filing, the parties had six unexercised Options and one partly performed exercised Option as follows (the FMV amounts in parentheses represent the current bid-ask spread for an equivalent Option on September 5, 1995):

1 B sold to A for 100 (premium due 12/1/95)(FMV 90-95 bid-ask)
2 B sold to A for 100 (FMV 90-95)
3 B sold to A for 100 (FMV 110-115)
4 A sold to B for 100 (premium due 8/15/95 and is past due)(FMV 110-115)
5 A sold to B for 100 (premium due 12/1/95)(FMV 105-110)
6 A sold to B for 100 (FMV 95-100)
7 B sold to A for 100. A exercised the option (yen/DEM) on August 25. Resulting trade should have closed on August 29 [the 27th was a Sunday]. A delivered 730,900,000 yen in Tokyo on August 29, but the 10 million DEM were never delivered.

Termination

Because the Parties chose Automatic Termination under Section 8.1, all Options were terminated automatically on September 1 as of the time immediately preceding the institution of the bankruptcy proceeding. Section 8.1(i) requires Party A (the Non-Defaulting Party) to calculate in good faith, as of the Close-out Date or as soon as reasonably practicable thereafter, a settlement amount for each Party. Although the Close-out Date was September 1, it probably will not be practicable for Party A to do its close-out calculations as of September 1, because (a) option prices as of September 1 may not be available on September 5, and (b) the market may have moved between September 1 and September 5 (since September 4 was a Business Day outside the U.S.), and September 5 prices will be a more accurate reflection of the cost to Party A of replacing the terminated Options.

Determining the Settlement Amount for Party A's Options

Party A bought the first three Options. Section 8.1(i)(a) states that the settlement amount for each Option is the current market premium for the Option (in the case of an Option purchase, the offer side).

Option 1. Party A is entitled to the current market premium = 95. [8.1(i)(a)]

Option 2. Party A is entitled to the current market premium = 95. [8.1(i)(a)]

Option 3. Party A is entitled to the current market premium = 115. [8.1(i)(a)]

Party A sold the next three options. Section 8.1(i)(b) states that the settlement amount of each Option is any unpaid Premium.

Option 4. The Premium was due on August 15. Is there an Option? Under Section 3.2(ii), Party A had the right, within 48 hours after the Premium Payment Date, to terminate the Option or declare an Event of Default. It apparently did not terminate the Option, so it must have decided to accept late payment. Accordingly, there is an Option, and Party A is entitled to the overdue Premium ($100) with interest from August 15 to but excluding September 1 at 1% over Party A's Funding Rate. [8.1(i)(b)].

Option 5. There is $100 in unpaid Premium, which is not due until December 1. Party A is entitled to $100 discounted from December 1 to but not including September 1 at 1% over Party A's Funding Rate. [8.1(i)(b)]

Option 6. Premium has been paid. Party A is entitled to 0.

Option 7. Party A is owed the DEM 10 million plus interest from August 29 to September 1 at a rate equal to 1% over Party A's Funding Rate, which will be it's cost to fund that amount of DEM.

Party A is entitled to any additional losses determined under Section 8.1(d).

The Premium payments owed to Party A are apparently already denominated in U.S. Dollars. Thus there is no need to convert the aggregate Premium amounts set forth above into dollars, which is Party's A's Base Currency, in accordance with Section 8.1(ii). However, Party B owes Party A DEM 10 million, which must be converted into Party A's Base Currency of USD. At the exchange rate at which Party A could have bought USD with DEM on September 5, 1995, this amount is approximately $7,028,889.

<u>Determining the Settlement Amount for Party B's Options</u>

Party B sold the first three options. It is entitled to any unpaid Premium, with interest to the payment date if the Premium is overdue, or discounted from the Premium Payment Date, if the Premium is not yet due.

Option 1. The Premium is not due until December 1. Party B is owed $100 Premium, discounted from December 1 to but not including September 1, at LIBOR on September 1. [8.1(i)(b)].

Option 2. Party B has already received the Premium, so the settlement amount = 0.
Option 3. Party B has already received the Premium, so the settlement amount = 0.

Party B purchased the next three Options, and is entitled to the current market premium.

Option 4. Party B is entitled to the current market premium for the Option = 115.

Option 5. Party B is entitled to the current market premium for the Option = 110

Option 6. Party B is entitled to the current market premium for the Option = 100

Option 7. Party B has already been paid with respect to the FX Transaction that resulted from the Option exercise, so settlement amount = 0

No currency amounts need to be converted to Party A's Base Currency.

Netting of Settlement Amounts

After settlement amounts are calculated for each Option, a net amounts must be derived. The net amount in the above example is shown on the following chart:

	Party A	Party B
Option 1	$95	$100 discounted
Option 2	$95	0
Option 3	$115	0
Option 4	$100 plus interest	$115
Option 5	$100 discounted	$110
Option 6	0	$100
Option 7	$7,028,889	0
Total	$505 + $7,028,889	$425
Total	$7,108,889	

Set off against Credit Support

If there were a Credit Support Agreement between the Parties, Party A would be entitled to set off the amount owed it against the amount of any collateral held by it. There is no such collateral in this case.

Notice of Settlement Calculation

Under Section 8.3, Party A should send Party B a notice of its calculation of the settlement amount. If Party B received such notice on September 5, it would be obligated to pay to Party A, on September 6, the net settlement amount with interest at Party A's Funding Rate from September 1 to but excluding September 6. To the extent such amount were not paid on September 6, it would bear interest at 1% over Party A's Funding Rate.