

FIA Legal Opinions Refresher



Wednesday, 13 October 2021

CLIFFORD
CHANCE

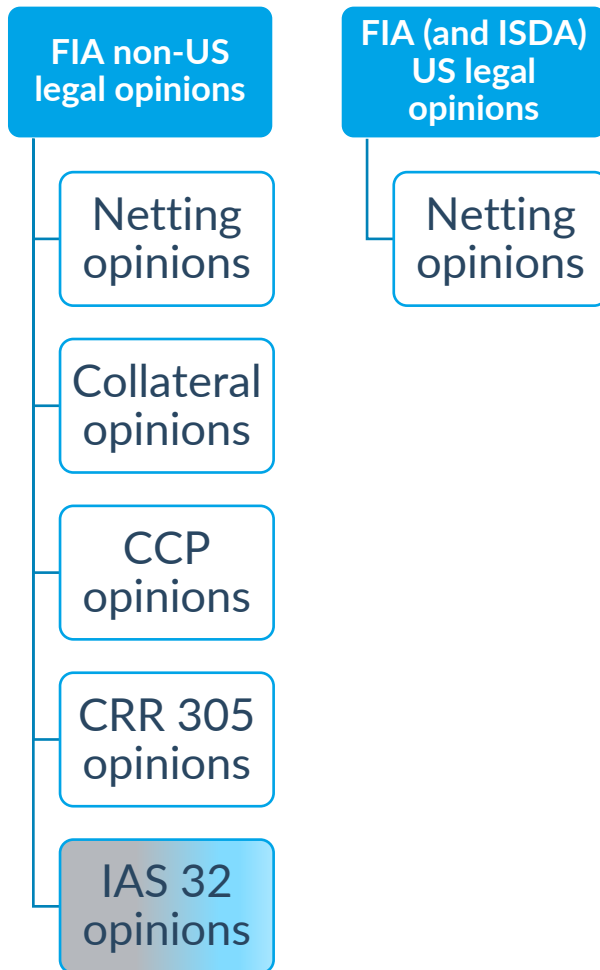




Agenda

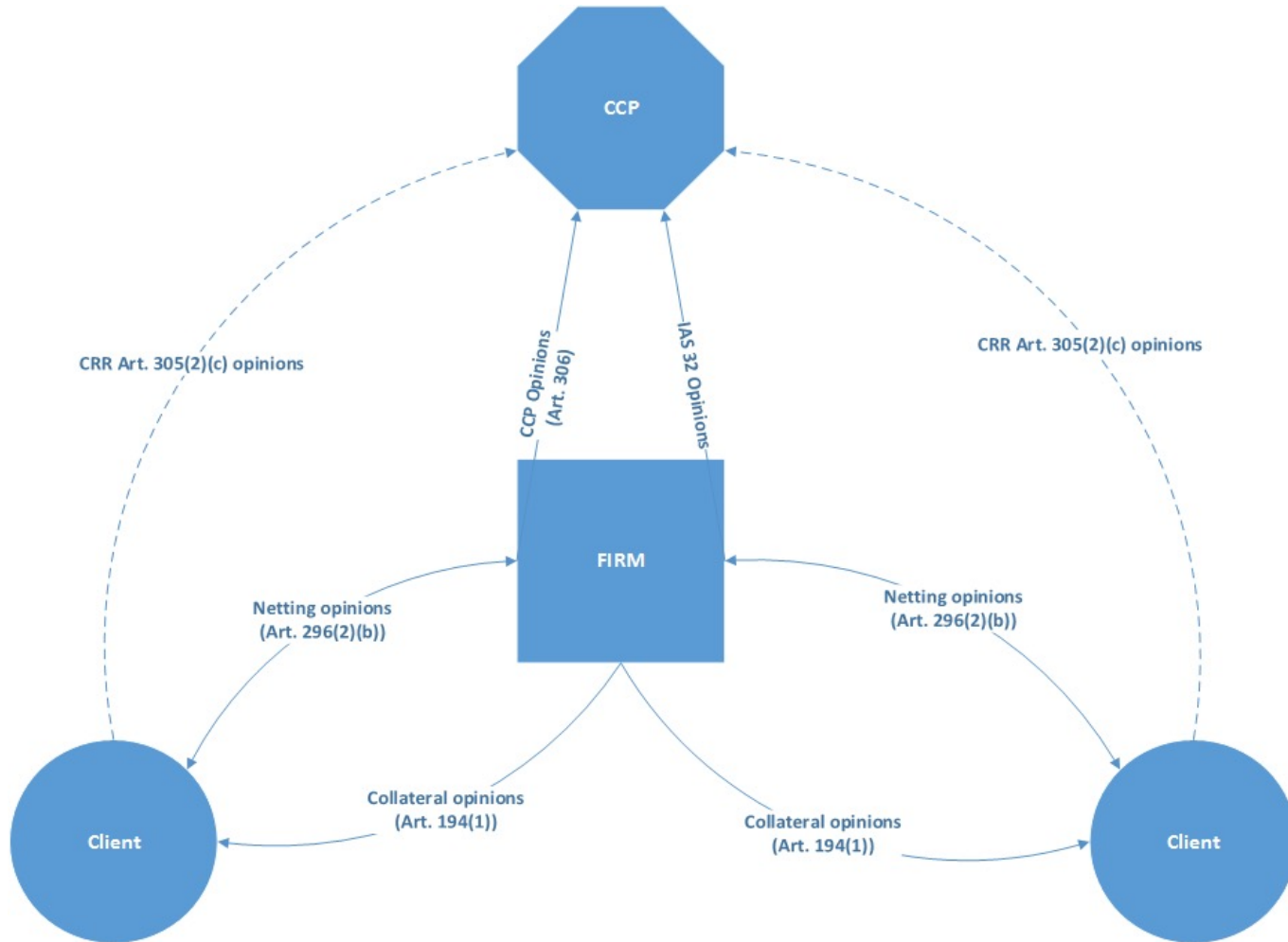
- Introduction
- FIA Legal Opinions Library – Europe + US
- FIA legal opinion types
- High-level structure/scope of FIA legal opinions
- World-wide coverage
- Capital requirements in the context of clearing – overview and types of opinions
- Structure of ‘CRR Article 305’ opinions and changes to CRR Article 305
- Indirect clearing supplemental netting opinions
- Reliance on FIA opinions
- Legal opinion review process – NCCLs and opinion updates
- How to access FIA legal opinions?
- Subscription and ‘add-on’ model
- FAQs

FIA US and Non-US legal opinions



FIA, jointly with ISDA, also maintains netting opinions for U.S. FCMs addressing enforceability of the liquidation and credit support provisions of commonly used futures account agreements and a Cleared Derivatives Addendum upon a customer's default or insolvency. These netting opinions currently cover 22 jurisdictions. FIA members may access these opinions at no charge in the [US FIA Documentation Library](#).

FIA legal opinions library - Europe



High-level structure/scope of FIA opinions

Netting opinions

- 61 opinions [2 new opinions planned for 2021/22]
- Based on 'Category 1' or 'Category 2' opinion templates
- One opinion letter with many legal opinions
- Netting
- Set-off
- TTCA
- Necessary/desirable amendments
- FIA Terms of Business 2018 and pre-2018 versions
- FIA Clearing Module
- ISDA/FIA Addendum

Collateral opinions

- 42 opinions
- Based on 'Situs' or 'Non-situs' opinion templates
- Effectiveness of FIA security interest arrangements
- TTCA covered in the netting opinions

CCP opinions

- 17 CCP opinions [2 new opinions planned for 2021/22]
- Enhanced template
- All CCP services typically covered
- Netting (including TT Margin/cash)
- Set off
- Account Segregation
- Bankruptcy remoteness of collateral

CRR 305 opinions

- 3 CCP 305(2)(c) opinions and 5 CM 305(2)(c) opinions
- "bear no losses" conclusions
- Analysis of the "segregation condition", "bankruptcy remoteness condition" and "porting condition" under 305(2)
- No FIA opinions available for 4% risk weighting under 305(3)

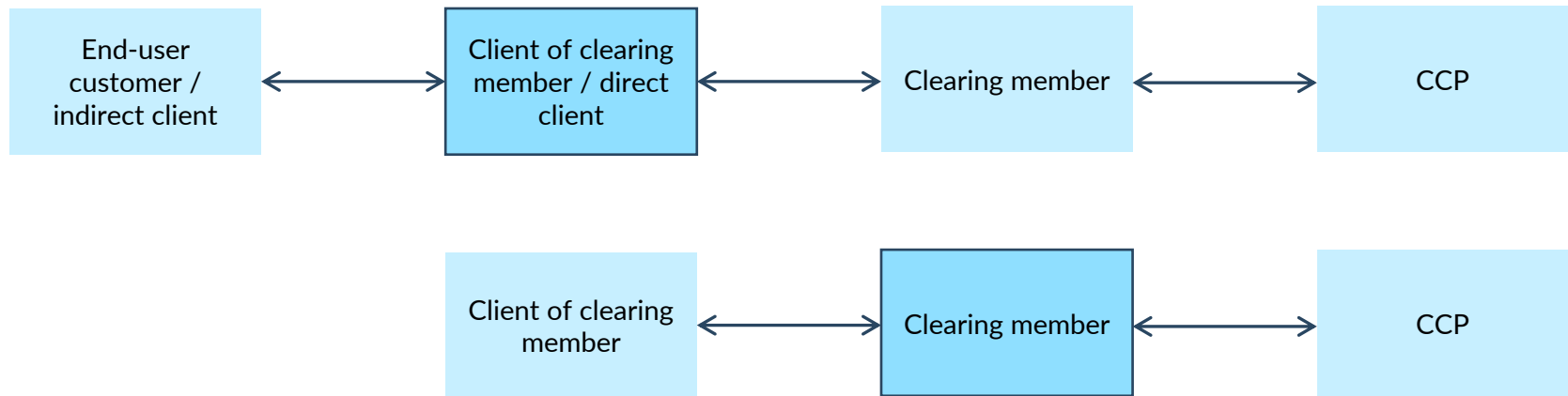
IAS 32 opinions

- 6 CCP opinions and 7 CM opinions
- A set of pre-opinions
- A set of documents on unilateral amendments of CCP Rules
- BAU payment netting
- Close-out netting in the event of CM's and CCP's default

Worldwide coverage

TIERED SUBSCRIPTION MODEL				ADD-ON MODEL		
Netting and collateral opinions		CCP opinions		Netting opinions	CCP opinions	
Australia	Italy	England & Wales	LCH Ltd	Bahrain	Poland	* NEW* KDPW_CCP
Austria	Japan	England & Wales	LME Clear	Bulgaria	Russia	*NEW* National Clearing Centre
Bahamas	Jersey	France	LCH SA	Czech Republic		
Belgium	Luxembourg	England & Wales	ICE Clear Europe	*NEW* Dubai (ADGM)		
Bermuda	Malta	Germany	Eurex Clearing	Dubai (DIFC)		
Brazil (No Collateral)	Malaysia	Sweden	Nasdaq Clearing	Estonia		
British Virgin Islands	Netherlands	Italy	CC&G	Gibraltar		
Canada (Ontario)	Norway	Germany	European Commodity Clearing (ECC)	Hungary		
Canada (Quebec)	Poland	Singapore	Singapore Exchange Derivatives Clearing	Indonesia		
Cayman Islands	Portugal	Australia	ASX Clear (Futures)	Latvia		
Cyprus	Scotland	Hong Kong	HKFE Clearing Corporation Limited (HKCC)	Liechtenstein (Netting + Collateral)		
Denmark	Singapore	Hong Kong	SEHK Options Clearing House Ltd (SEOCH)	Mauritius		
England & Wales	South Africa	Spain	BME Clearing	Mexico		
Finland	South Korea	Brazil	B3	Monaco		
France	Spain	Hong Kong	Securities Clearing (HKSCC)	New Zealand		
Germany	Sweden	Mexico	Asigna Compensacion y Liquidacion	Peru		
Greece	Switzerland	Canada	Canadian Derivatives Clearing Corporation	*NEW* Romania		
Guernsey	Taiwan			Russia		
Hong Kong	Turkey			Slovenia		
India	UAE (No Collateral)			Thailand		
Ireland	United States of America					
Israel						

Opinions in context: management of counterparty risk



- Where does your firm stand in the chain: who is your counterparty (up- and down-stream)?
- How can you be sure that your exposure is *net* if the counterparty fails?
- First step: enter into a close-out netting agreement....
- Capital basics:
 - $\text{Reg cap} = [8]\% * [\text{risk weight}] * [\text{exposure}]$
 - Risk weight differs according to counterparty identity
 - Exposure may be net or gross



Capital requirements – recent developments relevant for legal opinions

CRR, CRR II and IFR

- CRR was amended in 2019 with most new provisions having started to apply on 28 June 2021, including changes to articles relevant for legal opinions (e.g. changes to CRR Article 305)
- IFR has introduced new legal opinion requirements for investment firms (see Articles 25 and 31 of IFR). Most IFR capital requirements started to apply on 26 June 2021.

Brexit

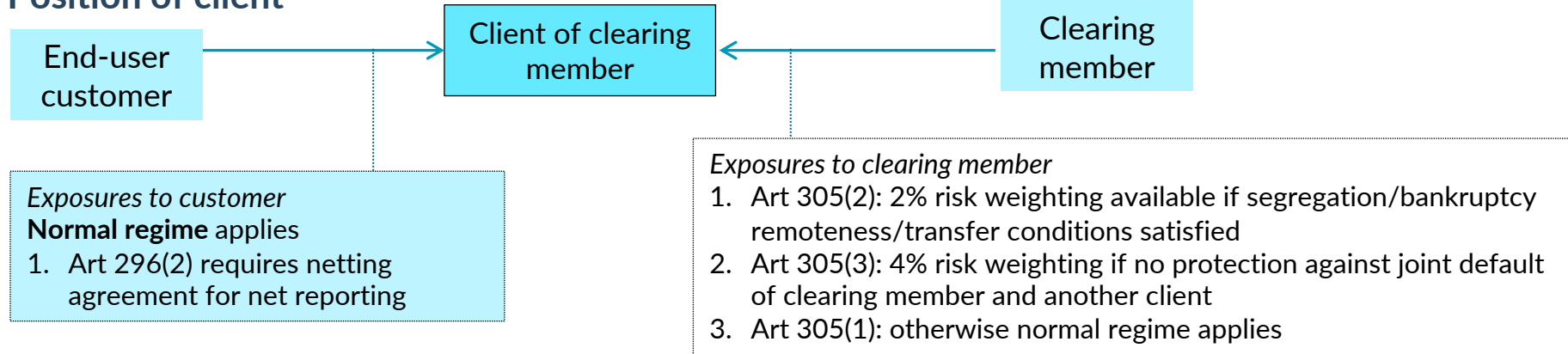
- UK CRR and UK IFR

ECB Banking Supervision

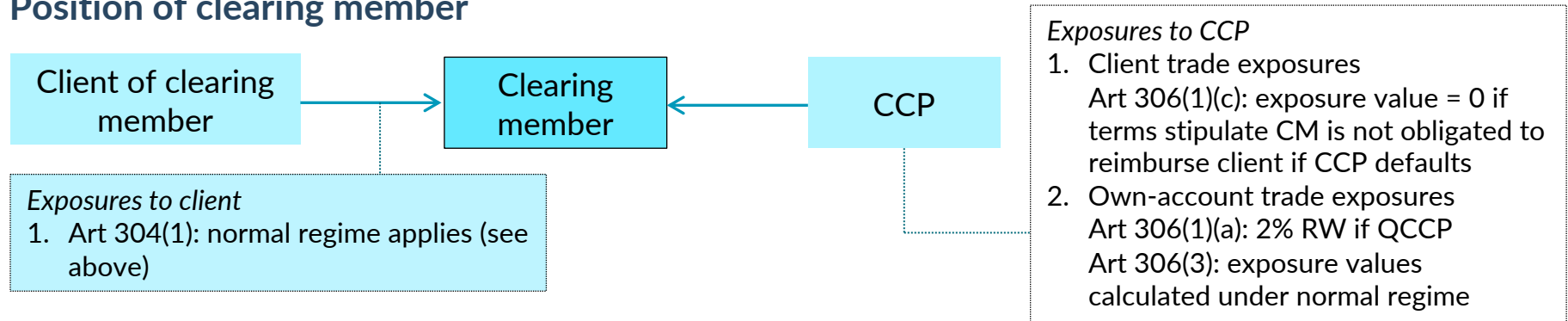
- [Notification requirement](#) of treatment of contractual netting agreements as risk-reducing (applies to significant credit institutions and has applied since 31 January 2020)
- ECB published [FAQs](#) on the notification process for the recognition of netting agreements

Capital requirements – exposures to clients

Position of client

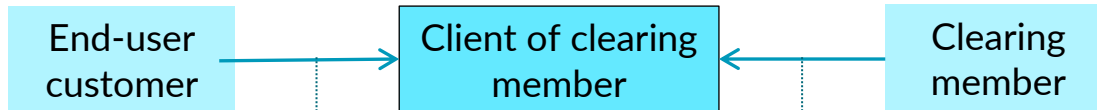


Position of clearing member



Capital requirements – netting opinions

Position of client



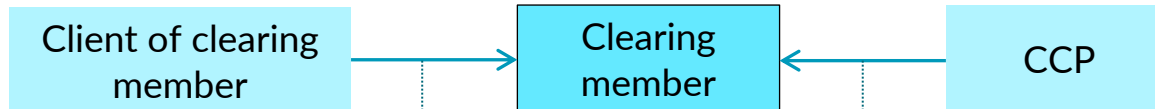
Exposures to customer

1. Art 296(2) requires **netting opinion** for net reporting

Exposures to clearing member

1. Art 305(2): 2% risk weighting requires 'sufficiently thorough legal review' that is kept up to date (previously, legal opinion required)
2. Art 305(3): 4% risk weighting requires **305-4%** 'sufficiently thorough legal review'
3. Art 305(1): if normal regime applies, net reporting requires **netting opinion**

Position of clearing member



Exposures to client

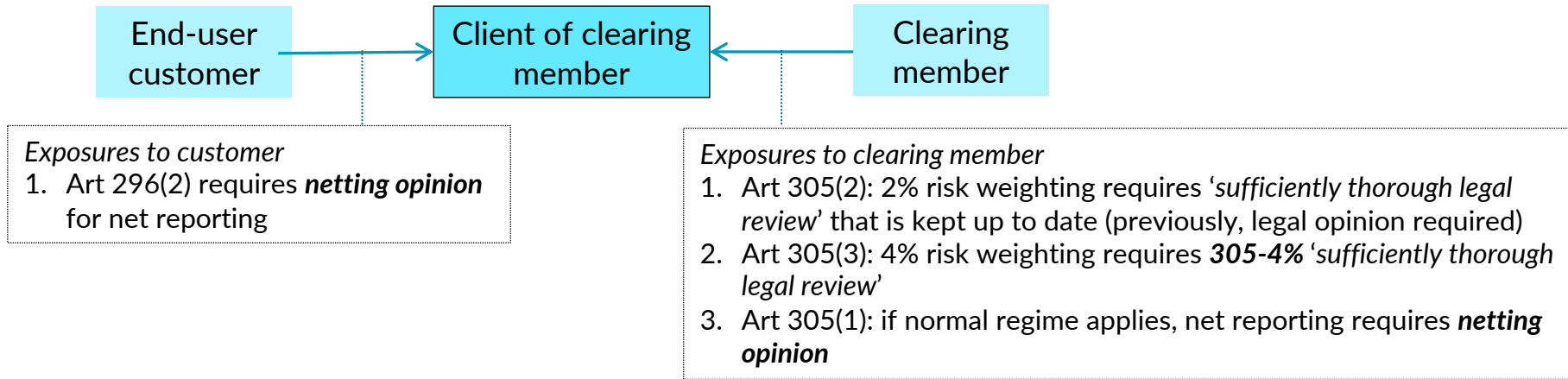
1. Art 304(1): Normal regime applies. Art 296(2) requires **netting opinion** for net reporting

Exposures to CCP

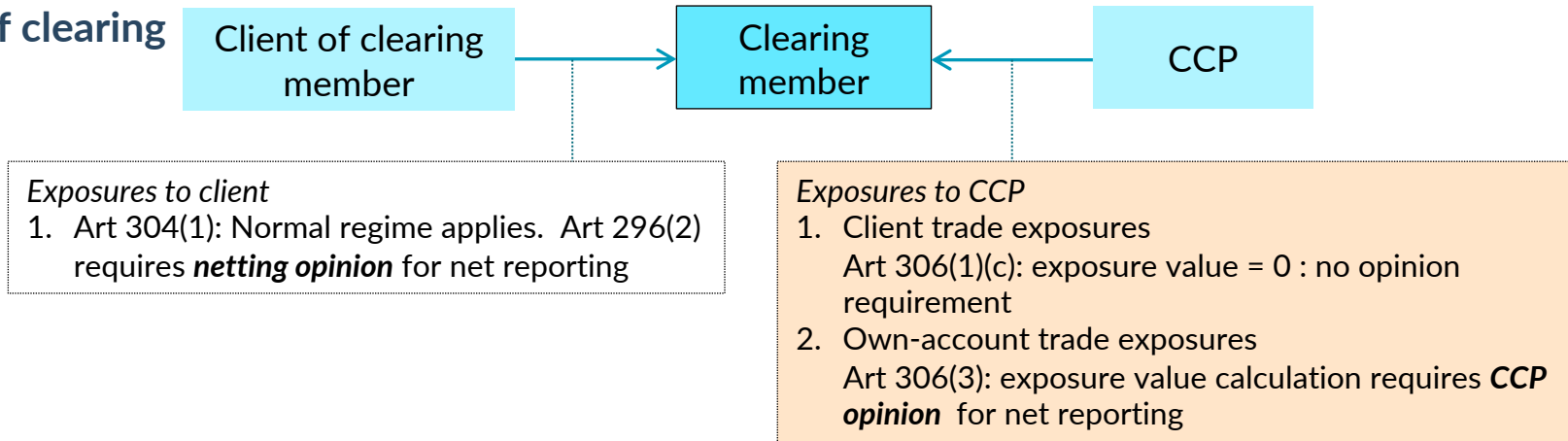
1. Client trade exposures
Art 306(1)(c): exposure value = 0 : no opinion requirement
2. Own-account trade exposures
Art 306(3): exposure value calculation requires **CCP opinion** for net reporting

Capital requirements – CCP opinions

Position of client

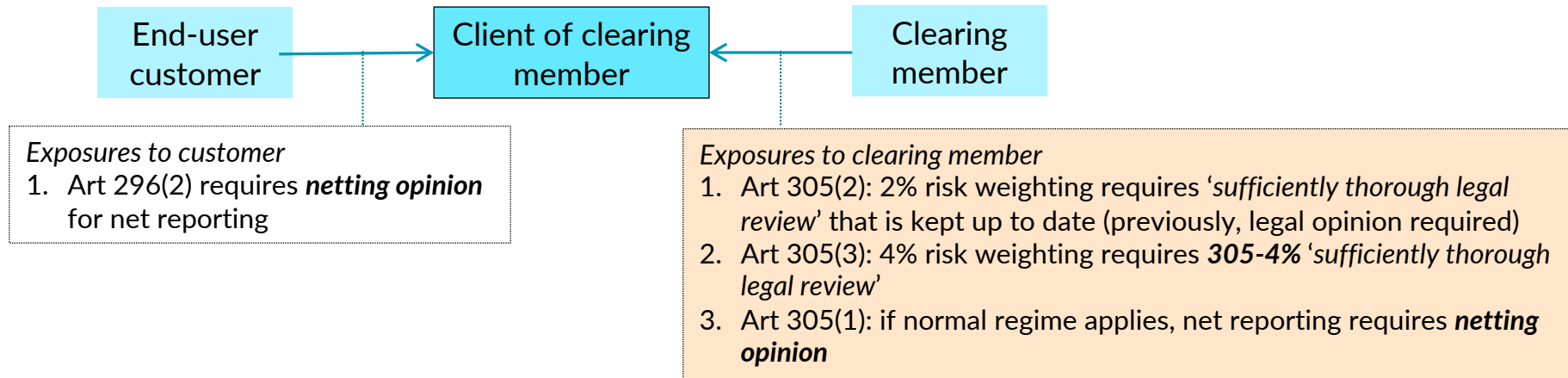


Position of clearing member

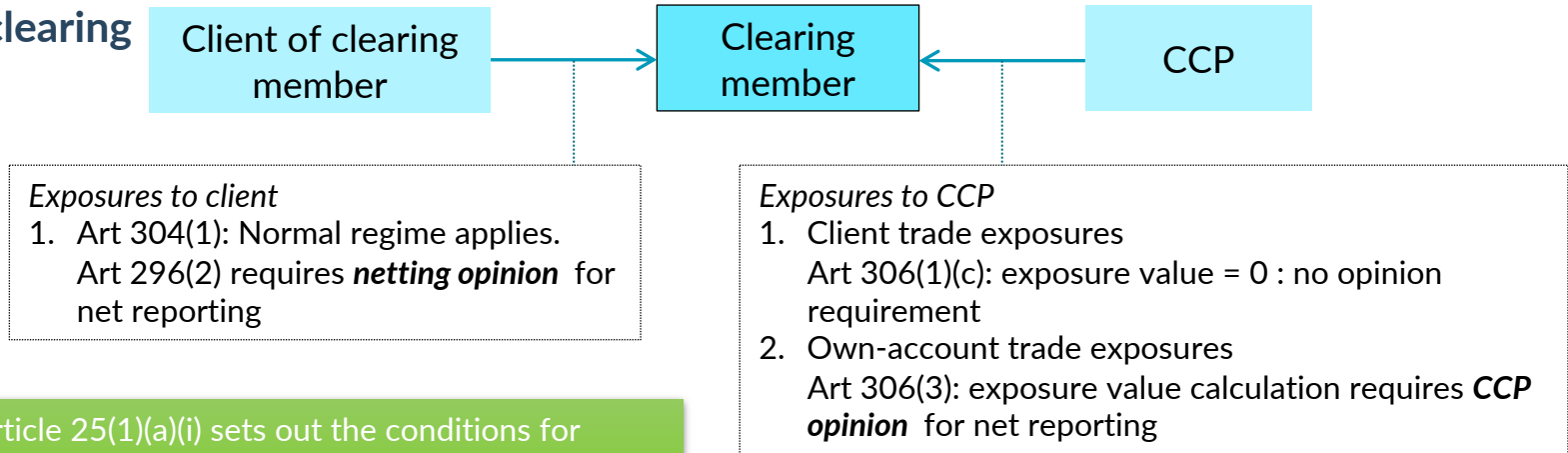


Capital requirements – 305 opinions

Position of client

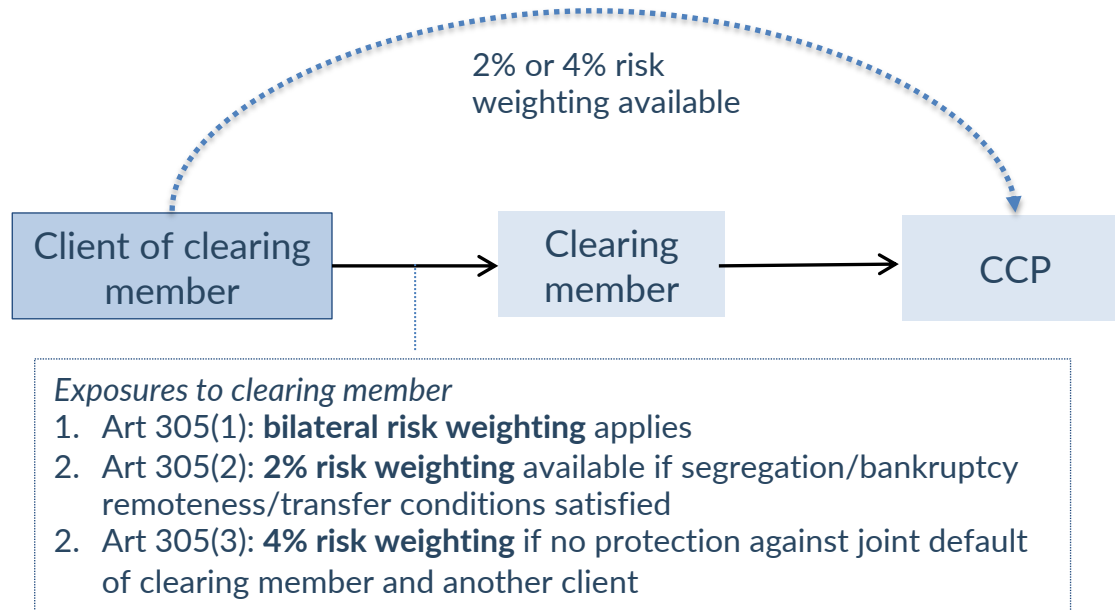


Position of clearing member



NEW: IFR Article 25(1)(a)(i) sets out the conditions for exemption of certain cleared derivative contracts from K-TCD. These conditions are equivalent to 'old' CRR Article 305(2).

Structure of 305 opinions



- If clearing member fails, will client “bear no losses”? See amended CRR Article 305(2)(c).
- The client may risk-weight the part of exposure covered by assets and collateral at the CCP at 2%
- Requires analysis of segregation and effects of porting/leapfrog in clearing member default
- Relevant jurisdictions for analysis are:
 - Jurisdiction of CCP – laws and rules applicable to clearing member default
 - Jurisdiction of CM – insolvency laws and rules applicable to treatment of client assets
- Hence two opinions – CCP and CM opinions, which need to be read together

Changes to CRR Article 305

Amended CRR Article 305(2)

- CRR II introduced changes to Article 305, which came into effect on 28 June 2021.
- We understand that the changes are driven by and follow the latest Basel standards ([here](#)), however the purpose of the requirement remains unchanged.
- No explicit reference to 'bear no losses' and to 'independent, written and reasoned legal opinion', however external counsel have confirmed that FIA CRR Article 305 opinions would also be applicable in relation to the revised Article 305 requirements for 2% risk weighting and to the equivalent IFR provisions.
- While the 305 opinions have been drafted with bank (and investment firm) prudential requirements in mind, we understand that a similar requirement also applies to insurance companies.

2. Without prejudice to the approach specified in paragraph 1, where an institution is a client, it may calculate the own funds requirements for its trade exposures for CCP-related transactions with its clearing member in accordance with Article 306 provided that all the following conditions are met:

(a) the positions and assets of that institution related to those transactions are distinguished and segregated, at the level of both the clearing member and the CCP, from the positions and assets of both the clearing member and the other clients of that clearing member and as a result of that distinction and segregation those positions and assets are bankruptcy remote in the event of the default or insolvency of the clearing member or one or more of its other clients;

(b) laws, regulations, rules and contractual arrangements applicable to or binding that institution or the CCP facilitate the transfer of the client's positions relating to those contracts and transactions and of the corresponding collateral to another clearing member within the applicable margin period of risk in the event of default or insolvency of the original clearing member. In such circumstance, the client's positions and the collateral shall be transferred at market value unless the client requests to close out the position at market value;

(c) the client has conducted a sufficiently thorough legal review, which it has kept up to date, that substantiates that the arrangements that ensure that the condition set out in point (b) is met are legal, valid, binding and enforceable under the relevant laws of the relevant jurisdiction or jurisdictions;

(d) the CCP is a QCCP.

- FIA currently maintains the following CRR Article 305(2) opinions:
 - CCPs: LCH Ltd (2021), ICE Clear Europe (2021) and LME Clear (2021)
 - CM jurisdictions: E&W (2021), France (2020), Germany (2021), Spain (2020) and Ireland (2020)



Indirect Clearing Supplemental Netting Opinions

What are the IC Supplemental Netting Opinions?

- These opinions are 'top-up' opinions that supplement FIA jurisdictional netting opinions to cover the enforceability and validity of the FIA Indirect Clearing Netting Provisions.

What is their scope?

- They cover the forms of the FIA Indirect Clearing Terms that include amendments to the netting provisions in the FIA Terms of Business. They are given in respect of the same types of parties and transactions as the FIA jurisdictional netting opinions.

Why does FIA maintain them?

- FIA maintains a number of Indirect Clearing Terms and some of them include amended netting provisions that are not covered in the 'base' FIA jurisdictional netting opinions. Therefore, we maintain the IC Supplemental Netting Opinions to help firms benefit from netting for regulatory capital purposes when they use the FIA Indirect Clearing Terms.

Why may firms require them?

- **CM-DC netting amendments:** creation of multiple netting sets (multiple Liquidation Amounts or Cleared Set Termination Amounts) instead of a single amount
- **DC-IC netting amendments:** new termination event (the DC Trigger Event), upon the occurrence of which, netting provisions apply that are not provided for in the FIA Terms of Business.



Indirect Clearing Supplemental Netting Opinions - continued

Are there any FIA IC Terms that are not covered by the IC Supplemental Netting Opinions?

- Yes, the 'BOSA DC-IC Indirect Clearing Terms' are not covered by the IC Supplemental Netting Opinions as these terms do not amend the netting provisions.

Which jurisdictions are covered?

- Currently we have 4 IC Supplemental Netting Opinions with respect to the jurisdictions of England & Wales, France, Germany and Switzerland.

What is the update process for these legal opinions?

- These opinions are currently not subject to an annual review. As we are about to publish the updated and new FIA Indirect Clearing Terms, it is essential that we also update the existing IC Supplemental Netting Opinions.

How much do they cost?

- Pricing of the IC Supplemental Netting Opinions depends on the number of firms that wish to purchase them. They are all subject to a one-off fee. Subject to changes in the number of purchasing firms, we propose to introduce the following pricing structure for the updated IC top-up opinions: (i) GBP3,500 for E&W, (ii) GBP6,000 for France, (iii) GBP7,000 for Germany and (iv) GBP11,000 for Switzerland.



Reliance on FIA legal opinions

- FIA legal opinions can be relied on for regulatory capital purposes by subscribing firms and their affiliates, provided that the names of affiliates that wish to rely on the opinions have been communicated to FIA.
- Firms that have not subscribed to FIA opinions and have instead obtained them from any other source cannot rely on them.
- FIA legal opinions are prepared on the basis of instructions from FIA in the context of the netting and collateral requirements of the Basel III capital rules in Europe (EU and UK) and the US.
- FIA legal opinions can be shared by the subscribing firms with
 - the officers, employees, auditors and professional advisers of any addressee or any subscribing member;
 - any person to whom disclosure is required to be made by applicable law or court order or pursuant to the rules or regulations of any supervisory or regulatory body or in connection with any judicial proceedings; and
 - any competent authority supervising a subscribing member,on the basis that (i) such disclosure is made solely to enable any such person to be informed that an opinion letter has been issued and to be made aware of its terms but not for the purposes of reliance, and (ii) we do not assume any duty or liability to any person to whom such disclosure is made and in preparing this opinion letter we have not had regard to the interests of any such person.

Legal opinion review process – NCCLs, Brief Descriptions and opinion updates

- What are ‘no change confirmation letters’ (NCCLs) and Brief Descriptions?
- Reviewing v. updating the opinions
- Some institutions are subject to capital regimes that require them to review legal opinions on an annual basis
- Update process:

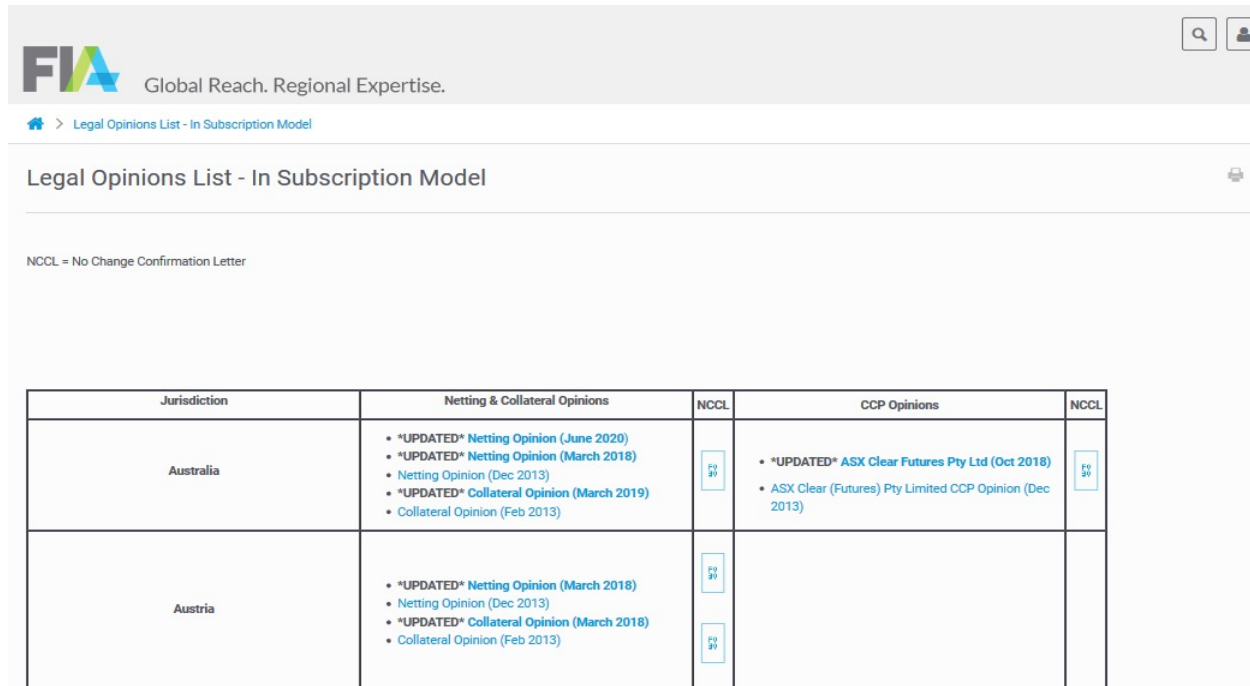
It is important that firms provide comments in the timeline requested to ensure efficient update process.







- Legal opinions WG – all subscribing firms are eligible to participate in the WG

How to access FIA legal opinions?

- FIA hosts its legal opinions on FIA [Documentation Platform](#) (not on FIA website).
- Access to FIA legal opinions is restricted to the FIA subscribing firms (member and non-member firms).



The screenshot shows the FIA Documentation Platform interface. At the top, the FIA logo is followed by the tagline "Global Reach. Regional Expertise." and search and user icons. Below the header, the breadcrumb "Legal Opinions List - In Subscription Model" is visible. The main content area is titled "Legal Opinions List - In Subscription Model" and includes a legend: "NCCL = No Change Confirmation Letter".

Jurisdiction	Netting & Collateral Opinions	NCCL	CCP Opinions	NCCL
Australia	<ul style="list-style-type: none"> • *UPDATED* Netting Opinion (June 2020) • *UPDATED* Netting Opinion (March 2018) • Netting Opinion (Dec 2013) • *UPDATED* Collateral Opinion (March 2019) • Collateral Opinion (Feb 2013) 		<ul style="list-style-type: none"> • *UPDATED* ASX Clear Futures Pty Ltd (Oct 2018) • ASX Clear (Futures) Pty Limited CCP Opinion (Dec 2013) 	
Austria	<ul style="list-style-type: none"> • *UPDATED* Netting Opinion (March 2018) • Netting Opinion (Dec 2013) • *UPDATED* Collateral Opinion (March 2018) • Collateral Opinion (Feb 2013) 	 		



Subscription model and 'Add-on' model

- FIA legal opinions are available to member and non-member firms. Non-members pay a premium subscription fee.
- In 2018, FIA introduced an annual 'tiered' subscription model for certain legal opinions. Subscribers required to sign a subscription agreement.
- In 2019, a variation of the annual subscription model ('Add-on Model') was introduced for less in-demand netting opinions.
- Subscription year for both models runs from 1 October to 30 September. Both subscription models are reviewed on an annual basis and opinions can be moved between the models (once a year) depending on the number of subscribers. Subscription renewals are automatic, unless cancelled by subscribing firms.
- FIA reaches out to subscribing firms over summer in advance of subscription model anniversary to confirm subscription selection and pricing.
- Subscribers are free to amend their selection of opinions during subscription year.
- Key difference between the 'tiered' subscription model and the 'add-on' model:
 - **Tiered subscription model**: pricing depends on the number of opinions that each firm wishes to subscribe to (i.e. annual fee does not depend on demand for each opinion, but rather on the 'tier' that each subscribing firm is in);
 - **Add-on model**: pricing depends on the number of subscribing firms for each opinion (i.e. the more firms subscribe to the opinion in the 'Add-on' model, the cheaper the annual fee).

Subscription Model Pricing 2021/22

Tier	Netting
Platinum 30+	£ 36,000
Gold 20+	£ 27,000
Silver 10+	£ 16,000
Bronze 1+	£ 5,000

Tier	Collateral
Platinum 30+	£ 44,000
Gold 20+	£ 35,000
Silver 10+	£ 20,000
Bronze 1+	£ 6,000

Tier	CCP
Platinum 8+	£ 16,000
Gold 4+	£ 10,000
Silver 1+	£ 5,000

Tier	Incremental Unit GBP
Platinum 30+	£ 750
Gold 20+	£ 1,000
Silver 10+	£ 1,500
Bronze 1+	£ 2,000
Off the shelf - 3 yr	£ 10,000

Tier	Incremental Unit GBP
Platinum 30+	£ 1,000
Gold 20+	£ 1,250
Silver 10+	£ 1,500
Bronze 1+	£ 2,000
Off the shelf - 3yr	£ 10,000

Tier	Incremental Unit GBP
Platinum 8+	£ 1,000
Gold 4+	£ 1,500
Silver 1+	£ 2,000
Off the shelf - 3yr	£ 10,000

Library Opinion count **43**

41

17

Sample Calculation / Example: A firm would like to subscribe to 23 Netting Opinions, 4 Collateral Opinions and 8 CCP Opinions. For the first 20 Netting Opinions the Tier is “Gold 20 +” 27,000GBP. The incremental 3 Netting Opinions are under Tier “Incremental Gold 20+” (1,000 GBP x 3) = 3,000GBP. Total Netting 30k GBP. The 1st Collateral Opinion would fall under Tier “Bronze 1+” 6,000 GBP . The Incremental 3 Collateral Opinions are under Tier “Incremental Bronze 1+” (2,000 GBP x 3) = 6,000 GBP. Total Collateral 12k GBP. Lastly, the 8 CCP Opinions would fall under Tier “Platinum 8+” and cost would be 16,000 GBP.

Grand Total: 30k Netting + 12k Collateral + 16k CCP = 58K GBP.

Please note that these are member rates. Non-members need to pay a 25% premium fee.



Frequently Asked Questions

Q1 -Why do the opinions not opine on the availability of any judicial remedy in respect of the enforceability of any net obligation?

Answer: This is a standard carve-out included in FIA opinions, which is aimed at limiting the opinion to the process of getting to the net sum by virtue of the operation of the netting provision – the opinions do not extend to what happens once such single net sum is produced. Therefore, each opinion addresses the issue of whether netting works, but does not cover whether the single net sum resulting from the netting process is enforceable (i.e., whether the party in question can claim/get its money corresponding to the net sum).

Q2 - Why do opinions not always confirm that a safe harbour applies and instead merely outline the requirements for the safe harbour to apply?

Answer: This can apply to either a collateral opinion or a netting opinion. The answer is distinct to each jurisdiction but in many cases it is because either the law is unclear or it would require a factual review of the agreement (for example, if only certain categories of transaction are protected then any opinion would need to include additional assumptions regarding the transactions that have been entered into).

Frequently Asked Questions

Q3 - Why are the opinions limited to Transactions which are capable, under their governing laws, of being terminated and liquidated in accordance with the FIA Netting Provision?

Answer: This provision is based on the fact that counsel have not reviewed each individual Transaction and its terms and are therefore unable to give a view on them. In any case, what this means in practice is that counsel only carve out those Transactions which for whatever reason are not capable of being terminated, liquidated or netted in accordance with the Netting Provision; netting still works for the remaining Transactions, with the "problematic" ones omitted from the netting set / calculation. Please also note that this language features in a number of other industry opinions.

Q4 - Why do the opinions sometimes refer to set-off in the context of netting provisions?

Answer: Many jurisdictions do not draw a distinction between netting arrangements and set-off arrangements and correspondingly their analysis and qualifications can refer to set-off in the context of netting arrangements. In other cases, it is not clear whether a court what characterise a netting arrangement as a set-off arrangement and in these cases it is possible for some common qualifications to be relevant to both a netting provision and a set-off provision.

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C L I F F O R D
C H A N C E

