STIKEMAN ELLIOTT

Stikeman Elliott LLP Barristers & Solicitors
1155 René-Lévesque Blvd. West, 40th Floor, Montréal, Québec, Canada H3B 3V2
Tel: (514) 397-3000 Fax: (514) 397-3222 www.stikeman.com

Sterling Dietze
Direct: 514-397-3076
E-mail: sdietze@stikeman.com

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The Futures & Options Association
36-38 Botolph Lane, 2nd Floor
London EC3R 8DE
United Kingdom

Dear Sirs/Mesdames,

FOA netting opinion issued in relation to FOA Netting Agreement, FOA Clearing Module and ISDA/FOA Clearing Addendum – Quebec and Canadian Federal Law –Situs version

You have asked us to give an opinion in respect of the laws of Quebec and the federal laws of Canada applicable in Quebec ("**this jurisdiction**") in respect of the enforceability of the FOA Netting Provision, the Clearing Module Netting Provision and the Addendum Netting Provision contained in an FOA Netting Agreement or a Clearing Agreement. Where the term "this jurisdiction" refers to a physical place it means the province of Quebec.

We understand that your fundamental requirement is for the enforceability of the FOA Netting Provision, the Clearing Module Netting Provision and the Addendum Netting Provision to be substantiated by a written and reasoned opinion. Our opinions on the enforceability of the FOA Netting Provision, the Clearing Module Netting Provision and the Addendum Netting Provision are given in paragraph 3 of this opinion letter.

Further, this opinion letter covers the enforceability of the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision and the Title Transfer Provisions.

1. TERMS OF REFERENCE AND DEFINITIONS

1.1 Subject as provided at paragraph 1.2, this opinion is given

1.1.2 generally, in respect of Parties (which act as "Client", "Firm" or "Clearing Member") which are corporations incorporated under the business corporations legislation of Canada, namely the *Canada Business Corporations Act* (Canada) ("**CBCA**"), the *Business Corporations Act* (Quebec), or similar legislation in any other province of Canada, including Investment Firms/Broker Dealers (meaning a corporation that does not conduct commercial banking activities but deals in and/or manages securities and/or other financial instruments as agent for third parties or as principal for its own account)[1]; and

1.1.3 generally, in respect of Parties incorporated or formed under the laws of another jurisdiction which are companies which have a branch or branches located in this jurisdiction.

1.2 This opinion is also given in respect to Parties (which act as "Firm" or "Clearing Member") which are Financial Institutions that are Banks, Trust and Loan Companies or Cooperative Credit Associations (Schedule 1) or Insurance Companies (Schedule 3), subject to the terms of reference, definitions, modifications and additional assumptions and qualifications set out in the applicable Schedule.

1.3 This opinion is also given in respect of Parties (which act as "Client") that are any of the following, subject to the terms of reference, definitions, modifications and additional assumptions and qualifications set out in the applicable Schedule:

1.3.2 Financial Institutions that are Banks, Trust and Loan Companies or Cooperative Credit Associations (Schedule 1);

1.3.3 Partnerships (Schedule 2);

1.3.4 Insurance Companies (Schedule 3);

1.3.5 Individuals domiciled and resident in Quebec (Schedule 4);

1.3.6 Investment Funds, but not including Pension Entities described in 1.3.10 (Schedule 5);

1.3.7 Sovereign, State of a Federal Sovereign and Sovereign Owned Entity (Schedule 6);

1.3.8 Private Trusts that are not funds described in 1.3.6 or Pension Entities described in 1.3.10 (Schedule 7);

1.3.9 Charitable Corporations (Schedule 8);

[1] In Canada, such entities are referred to as broker-dealers or dealers.

1.3.10 Pension Entities (Schedule 9); and

1.3.11 Quebec Municipal Corporations (Schedule 10).

Although the coverage described above includes entities that are not formed under the laws of this jurisdiction, our opinion is restricted to this jurisdiction's laws and does not consider any provisions of the laws of those other jurisdictions even if those laws may be relevant and applicable to the issues addressed in this opinion.

1.4 This opinion is given in respect of the FOA Netting Agreement and the Clearing Agreement when the FOA Netting Agreement and the Clearing Agreement are expressed to be governed by English law.

1.5 This opinion covers all Transactions (whether entered into on an exchange, any other form of organized market place or multilateral trading facility, or over-the-counter), subject to the following:

1.5.1 The Annex 2 List of Transactions includes in (A)(v) "any other Transaction which the parties agree to be a Transaction". As discussed in this opinion, the insolvency law safe-harbours for termination, netting and collateral enforcement rights ("**EFC safe-harbours**") apply only to a specific list of transaction types, defined as "eligible financial contracts" (**EFCs**) in Canadian Insolvency Statutes. We cannot opine on Transactions that Parties may agree to include under the FOA Netting Agreement or the Clearing Agreement without understanding the nature of those Transactions. Consequently, our opinion with respect to Transactions covered by (A)(v) is restricted to those that meet the definition of an EFC.

1.5.2 The Annex 2 List of Transactions in (B), (C) and (D) includes Transactions "relating to" fixed income securities, equities and commodities. The words "relating to" are wide and, consequently, it is unclear as to what other types of transactions "relating to" fixed income, equity securities or commodities might be subject to the FOA Netting Agreement and the Clearing Agreement. Unless the Transactions are agreement types covered by the statutory definition of an EFC, they will not benefit from the EFC safe-harbours and, consequently, may be subject to automatic or court ordered stays on termination and netting. Consequently, much of this opinion applies only to the types of Transactions covered by (B), (C) or (D) which are caught by the definition of an EFC. This definition is discussed in the body of the opinion and at Annex 8.

1.5.3 The Annex 2 List of Transactions in (E) includes "(OTC derivatives) Transactions which fall within paragraphs (4) to (10) of Section C of Annex 1 to Directive 2004/39/EC, including (but not limited to)" certain types of derivatives specifically listed in (E). As noted above, unless the Transactions which are covered by (E) but are not specifically listed therein are agreement types covered by the statutory definition of an EFC, they will not benefit from the EFC safe-harbours and, consequently, may be subject to automatic or court ordered stays on termination and netting. Consequently much of this opinion applies only to the types of Transactions which are covered by (E) but are not specifically listed therein to the extent they are caught by the definition of an EFC.

1.5.4 This opinion is given in respect of only such of those Transactions which, under their governing laws, are legal, valid, binding and enforceable and capable of being terminated and liquidated in accordance with the FOA Netting Provision, the Clearing Module Netting Provision or, as the case may be, the Addendum Netting Provision.

1.6 In this opinion, references to the word "enforceable" and cognate terms are used to refer to the ability of a Party to exercise its contractual rights in accordance with their terms and without risk of successful challenge. We do not opine on the availability of any judicial remedy.

1.7 The opinions at paragraphs 3.7, 3.8 and 3.9 in respect of the FOA Set-Off Provisions, the Clearing Module Set-Off Provision and the Addendum Set-Off Provision, respectively, are given only in respect of cash balances credited to an account which is inside or located outside Quebec.

1.8 The opinion is given in respect of margin consisting only of (i) cash or (ii) securities located inside or outside this jurisdiction.

1.9 We do not opine on (i) the enforceability or collectability of any net obligation resulting from any netting or set-off, whether pursuant to the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provisions, the Addendum Set-Off Provisions, the Title Transfer Provisions or otherwise, or (ii) subject to our discussion in relation to the General Set-Off Clause in paragraph 3.7, the set-off of any amounts other than the amounts owing under the FOA Netting Agreement or the Clearing Agreement.

1.10 This opinion letter relates solely to matters under the laws of this jurisdiction

and does not consider the impact of any laws (including insolvency laws) other than the law of this jurisdiction, even where, under the law of this jurisdiction, any foreign law is to be applied. This opinion letter and the opinions given in it are governed by the law of this jurisdiction and relate only to the law of this jurisdiction as of the date of this opinion. We express no opinion on the laws of any other jurisdiction.

1.11 Subject to paragraph 2.1, we do not express any opinion as to any provision of any Rule Set or as to the effect of any such provision on the opinions in this opinion letter.

1.12 We do not express any opinion as to any matters of fact.

1.13 Definitions

Terms used in this opinion letter and not otherwise defined herein shall have the meanings ascribed to them in the FOA Netting Agreement or the Clearing Agreement, unless the context specifies otherwise. Where, in an FOA Netting Agreement or, as the case may be, a Clearing Agreement, a defined term has been changed but the changed term corresponds to a term defined in a FOA Published Form Agreement or, as the case may be, the FOA Clearing Module and/or the ISDA/FOA Clearing Addendum, or this opinion letter, this opinion letter may be read as if terms used in it were the terms as so changed.

1.13.1 "**Insolvency Proceedings**" means the procedures listed in paragraph 3.1;

1.13.2 "**Insolvency Representative**" means a liquidator, administrator, trustee in bankruptcy, administrative receiver or analogous or equivalent official in this jurisdiction;

1.13.3 "**FOA Member**" means a member (excluding associate members) of the Futures and Options Association which subscribes to the Futures and Options Association's Netting Analyser service (and whose terms of subscription give access to this opinion);

1.13.4 References to "**termination and liquidation**" of Transactions or, as the case may be, Client Transactions are to the termination of obligations to make any further payment or deliveries under (i) such Transactions which would have fallen due for performance on or after the Termination Date under an FOA Netting Agreement or (ii) such Client Transactions which would have fallen due for performance on or after the occurrence of a Firm Trigger Event (or CM Trigger Event, as applicable) or of a CCP Default under a Clearing Agreement, except for the obligation to settle the Termination Amount or Cleared

Set Termination Amount in respect of such Transactions or, as the case may be, Client Transactions, and references to "terminated Transactions" or, as the case may be, "terminated Client Transactions" or like expressions shall be construed accordingly;

1.13.5 A reference to a "**designated clearing and settlement system**" is a reference to a system which has been designated under section 4 of the *Payment Clearing and Settlement Act* (Canada) (the "**PCSA**"). To date, the Large Value Transfer System (LVTS), CDSX, CLS Bank, the Canadian Derivatives Clearing Service and LCH's SwapClear service have been designated under section 4 of the PCSA;

1.13.6 The term "**EFC**" or "**eligible financial contract**" has the meaning attributed to such term in Annex 8;

1.13.7 "**Relevant Title Transfer Provisions**" means, in relation to the Title Transfer Provisions, Clause 5 of the Title Transfer and Physical Collateral Annex to the Netting Module (2007 and 2011 version) or any provision forming part of the Title Transfer Provisions which corresponds thereto; and

1.13.8 A reference to a "**paragraph**" is to a paragraph of this opinion letter.

Annex 3 contains further definitions of terms relating to the FOA Netting Agreement and the Clearing Agreement.

1.14 Headings are for ease of reference only and shall not affect the interpretation of this opinion letter.

2. ASSUMPTIONS

We assume:

2.1 That no provision of the FOA Netting Agreement or Clearing Agreement that is necessary for the giving of our opinions and advice in this opinion letter has been altered in any material respect, including by reason of a Mandatory CCP Provision. In our view, an alteration contemplated in Part 2 (*Non-material Amendments*) of Annex 4 hereto would not constitute a material alteration for this purpose. We express no view whether an alteration not contemplated in Part 2 (*Non-material Amendments*) of Annex 4 hereto would or would not constitute a material alteration of the FOA Netting Agreement or, as the case may be, the Clearing Agreement.

2.2 That the FOA Netting Agreement or, as the case may be, the Clearing Agreement, and the Transactions (or, as the case may be, the Client

Transactions) are legally binding and enforceable against both Parties under their governing laws.

2.3 That each Party has the capacity, power and authority under all applicable laws to enter into the FOA Netting Agreement or, as the case may be, the Clearing Agreement, and the Transactions or, as the case may be, the Client Transactions, and to perform its obligations under the FOA Netting Agreement or, as the case may be, the Clearing Agreement, and the Transactions or, as the case may be, Client Transactions; and that each Party has taken all necessary steps to execute, deliver and perform the FOA Netting Agreement or, as the case may be, the Clearing Agreement.

2.4 That each Party has obtained, complied with the terms of and maintained all authorizations, approvals, licences and consents, and has complied with all applicable regulatory restrictions or requirements, required to enable it lawfully to enter into and perform its obligations under the FOA Netting Agreement or, as the case may be, the Clearing Agreement, and the Transactions or, as the case may be, the Client Transactions, and to ensure the legality, validity, enforceability or admissibility in evidence of the FOA Netting Agreement or, as the case may be, the Clearing Agreement in this jurisdiction.

2.5 That the FOA Netting Agreement or, as the case may be, the Clearing Agreement has been properly executed by both Parties.

2.6 That the FOA Netting Agreement or, as the case may be, the Clearing Agreement is entered into prior to the formal commencement of any Insolvency Proceedings against either Party.

2.7 That no provision of the FOA Netting Agreement or, as the case may be, the Clearing Agreement, or a document of which the FOA Netting Agreement or, as the case may be, the Clearing Agreement forms part, or any other agreement or arrangement between the Parties, or any Mandatory CCP Provisions, constitutes an Adverse Amendment or modifies or supersedes the FOA Netting Agreement or, as the case may be, the Clearing Agreement.

2.8 The FOA Netting Agreement or, as the case may be, the Clearing Agreement has been entered into, and each of the Transactions (or, as the case may be, the Client Transactions) referred to therein is carried out, by each of the parties thereto in good faith, for the benefit of each of them respectively, on arms' length commercial terms and for the purpose of carrying on, and by way of, their respective businesses.

2.9 That the FOA Netting Agreement, or, as the case may be, the Clearing

Agreement accurately reflects the true intentions of each Party.

2.10 That the obligations assumed under the FOA Netting Agreement or, as the case may be, the Clearing Agreement, and the Transactions (or, as the case may be, the Client Transactions) are "mutual" between the Parties, in the sense that the Parties are each personally and solely liable as regards obligations owing by it to the other Party and solely entitled to the benefit of obligations owed to it by the other Party.

2.11 In relation to the opinions set out at paragraphs 3.4 and 3.5 only, that each form of Insolvency Proceeding respectively constitutes a Firm Trigger Event or a CM Trigger Event under the relevant Rule Set.

2.12 That each Party when transferring margin pursuant to the Title Transfer Provisions, has full legal title to such margin at the time of transfer, free and clear of any lien, claim, charge or encumbrance or any other interest of the transferring party or of any third person (other than a lien routinely imposed on all securities in a relevant clearance or settlement system).

2.13 That all margin transferred pursuant to the Title Transfer Provision is freely transferable and all acts or things required by the laws of this or any other jurisdiction to be done to ensure the validity of each transfer of margin pursuant to the Title Transfer Provisions will have been effectively carried out.

2.14 That each Party which receives transferred margin pursuant to the Title Transfer Provisions does not treat that transferred margin in any manner which could indicate that the other Party retains any proprietary interest in that transferred margin.

2.15 That any cash provided as margin is in a currency that is freely transferable internationally under the laws of all relevant jurisdictions.

2.16 An account located outside of this jurisdiction for purposes of paragraph 1.7 means:

2.16.1 An account maintained by a financial institution located outside of Quebec, which account is not governed by Quebec law or maintained in an office located in Quebec; or

2.16.2 An account maintained by the Party that is a financial institution and that receives the amounts to be credited to the account, where the Party is located outside of Quebec, which account is not governed by Quebec law or maintained in an office located in Quebec.

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2.17 An asset located outside of this jurisdiction for purposes of paragraph 1.8 means:

2.17.1 If the asset is a certificated security or instrument in physical form, the physical certificate or instrument is located outside of Quebec at all relevant times;

2.17.2 If the asset is an uncertificated security[2], the issuer's jurisdiction (as we have defined this in accordance with the conflict of laws rules of this jurisdiction)[3] is outside of Quebec and the issuer or transfer agent maintains the transfer or ownership records outside of Quebec; and

2.17.3 If the asset or account is a securities account[4] or securities entitlement[5] maintained in a securities account with a securities intermediary (including a clearing organization), the jurisdiction of the securities intermediary (as determined under the conflict of laws rules of this jurisdiction)[6] is outside of Quebec.

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2 A security not evidenced by a physical certificate that is held directly by the holder, not by a securities intermediary.

3 The "issuer's jurisdiction" is not defined in *An Act respecting the transfer of securities and the establishment of security entitlements* (Quebec) ("**QSTA**") or the *Civil Code of Québec* ("**Civil Code**" or "**CCQ**"), as it is in the *Securities Transfer Act* (Ontario) ("**OSTA**"). The Quebec rules do, however, specify a jurisdiction in substantively the same manner as the OSTA. Therefore, the issuer's jurisdiction for Canadian federally incorporated issuers is the province or territory in which it has its head office (which likely corresponds to "registered office" which is used in the CBCA and "head office" as used in Article 307, CCQ), or, if Canadian federal law permits (which it does not yet do), another jurisdiction specified by the issuer. For Canadian, provincial, or territorial Crowns, the laws of Canada, the province and territory respectively or, if the laws of Canada, the province and territory respectively, permit, the laws of another jurisdiction specified by the issuer (Article 3108.3, CCQ). For other issuers, the jurisdiction under which the issuer is constituted, or, if the law of that jurisdiction permits, another jurisdiction specified by the issuer. So, for example, the jurisdiction of a Quebec incorporated or organized entity or the Quebec Crown is normally Quebec, but the Civil Code expressly allows the issuer to choose another jurisdiction at Article 3108.4, CCQ.

4 Not every account holding financial assets is a securities account. The person (e.g. a broker, bank or trust company) maintaining the account must be either a clearing agency (as defined in the QSTA, s.1(1)) or it must be in the ordinary course of its business to maintain securities accounts for others, and it must be acting in that capacity with respect to the account. So, while a bank could be a securities intermediary, a typical deposit account would likely not be characterized as a securities account.

5 See Annex 10 for how a party obtains a security entitlement.

6 The term "securities intermediary's jurisdiction" is not defined in the QSTA or the Civil Code but the Quebec conflict rules specify a jurisdiction in substantively the same manner as the OSTA at Article 31087.7 of the Civil Code. Those rules specify a number of alternatives for determining the

2.18 That each Party (which acts as "Firm" or "Clearing Member") under a Clearing Agreement is (i) a clearing member in respect of any Agreed CCP Service to which the Clearing Agreement relates, and (ii) an entity of a type described in paragraph 1.1 and 1.2 above. We refer you to Schedules 1 and 3 with respect to the analysis of insolvency and other issues which are specific to Financial Institutions and Insurance Companies, respectively, which analysis supplements the opinions expressed in paragraph 3 of this opinion letter.

2.19 That neither Party is a "*bridge institution*" as defined in section 2 of the *Canada Deposit Insurance Corporation Act* (Canada) ("**CIDC Act**"). The implications of dealing with a bridge institution are discussed in Schedule 1.

3. OPINION

On the basis of the foregoing terms of reference and assumptions and subject to the qualifications set out in paragraph 4 below, we are of the following opinion:

3.1 Insolvency Proceedings

The only bankruptcy, composition, rehabilitation (e.g. liquidation, administration, receivership or voluntary arrangement) or other insolvency laws and procedures to which a Party would be subject in this jurisdiction are the following:

3.1.1 Proceedings under the *Bankruptcy and Insolvency Act* (Canada) ("**BIA**") for either (i) liquidation (including with respect to a Party which is an Investment Firm/Broker Dealer the special securities firm provisions of Part XII) ("**BIA Bankruptcy**") or (ii) reorganization/ arrangement with creditors under Part III, Division I ("**BIA Proposals**");

3.1.2 Proceedings under the *Winding-up and Restructuring Act* (Canada)

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securities intermediary's jurisdiction applied in the following order:

(i) the law of the jurisdiction specified as governing the matters set out in the first paragraph of Article 3108.7 of the Civil Code, including the acquisition of a security entitlement from the securities intermediary, in a juridical act (agreement) governing the securities account between the intermediary and its entitlement holder;

(ii) the expressly stated governing law of a juridical act (agreement) governing the securities account;

(iii) if a juridical act (agreement) governing the securities account expressly provides that the securities account is maintained at an establishment in a particular jurisdiction, then the law of that jurisdiction;

(iv) the law of the jurisdiction in which the establishment identified in an account statement as the establishment serving the entitlement holder's account is located; or

(v) the law of the jurisdiction where the decision-making centre of the securities intermediary is located.

("**WURA**") for either (i) liquidation or (ii) reorganization/arrangement with creditors ("**WURA Proceedings**") (but not for a Party which is a corporation governed by the CBCA);

3.1.3 Proceedings under the *Companies' Creditors Arrangement Act* (Canada) ("**CCAA**") for reorganization/arrangement of claims of creditors of corporations ("**CCAA Plan of Arrangement**");

3.1.4 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**"); and

3.1.5 Corporate plans of arrangement involving insolvent entities and providing for the reorganization/arrangement of claims of creditors ("**Corporate Plans of Arrangement**").

For an insolvent Investment Firm/Broker Dealer, the most likely Insolvency Proceeding is a BIA Bankruptcy given that there are special procedures for bankrupt securities firms in Part XII of the BIA.

We have included a chart as Annex 6 that indicates which Party types are subject to each of the Insolvency Proceedings.

"**Insolvency Statutes**" for purposes of this opinion means the BIA, the WURA, and the CCAA. Please note that "**Insolvency Statutes**" may be defined in a different manner in the Schedules to this opinion as there are other insolvency statutes which apply to the types of Parties addressed in such Schedules.

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, without the need for any additions.

3.2 Recognition of Choice of Law

3.2.1 The choice of English law to govern the FOA Netting Agreement or, as the case may be, the Clearing Agreement will be recognised in this jurisdiction even if neither Party is incorporated or established in England, subject to the provisos and qualifications set out in paragraph 4.4.1. However, there are some matters which are not determined by reference to the chosen governing law (which will only cover substantive issues determined by the proper law of the contract), but which are mandatory in the forum irrespective of the choice of governing law. In particular, where all the elements relevant to a situation being adjudicated upon were, at the time the choice of law

was made, connected with a particular country, the courts of this jurisdiction may apply rules of law of that country which cannot be derogated from by contract. We express no opinion on the binding effect of the choice of law provisions in the FOA Netting Agreement or, as the case may be, Clearing Agreement insofar as they relate to non-contractual obligations arising from or connected with the FOA Netting Agreement or, as the case may be, Clearing Agreement.

3.2.2 An Insolvency Representative or court in this jurisdiction would have regard to English law as the governing law of the FOA Netting Agreement or, as the case may be, the Clearing Agreement, in determining the enforceability or effectiveness of the (i) FOA Netting Provision and the FOA Set-Off Provision or, as the case may be, of the Clearing Module Netting Provision and/or the Addendum Netting Provision and the Clearing Module Set-Off Provision and/or the Addendum Set-Off Provision and (ii) the Relevant Title Transfer Provisions, subject to the provisos and qualifications set out in paragraph 4.4.2.

3.3 Enforceability of FOA Netting Provision

Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.3 and the qualifications in paragraph 4, in relation to an FOA Netting Agreement, or in relation to a Clearing Agreement where the Defaulting Party acts as the Client, the FOA Netting Provision will be immediately (and without fulfilment of any further conditions) enforceable in accordance with their terms so that, following an Event of Default, including as a result of the opening of any Insolvency Proceedings:

3.3.1 the Non-Defaulting Party would be entitled immediately to exercise its rights under the FOA Netting Provision; and

3.3.2 the Non-Defaulting Party would be entitled to receive or obliged to pay only the net sum of the positive and negative mark-to-market values of individual Transactions.

We are of this opinion because generally contractually binding termination rights and rights to set-off mutual obligations arising under such contractual arrangements are not contrary to bankruptcy principles, such as the anti-forfeiture principle, or rendered ineffective by the Insolvency Statutes. This conclusion is subject to the discussion which follows dealing with stay orders and laws.

There are rules of law in this jurisdiction which could impose a moratorium

or stay which would prevent, delay or otherwise affect the exercise of such rights by the Non-Defaulting Party, but in many cases an exemption from the moratorium or stay will apply. In summary,

- In certain Canadian Insolvency Proceedings (e.g. BIA Bankruptcy and, less clearly, Corporate Plan of Arrangement) there are no applicable laws or provisions that prevent or delay the exercise of termination and netting rights, and with respect to such Insolvency Proceedings we believe that in a properly presented and argued case a court would not prevent the exercise of the FOA Netting Provision.
    - **BIA Bankruptcy.** There is no express recognition of the right to terminate and net under EFCs or similar agreements in the BIA bankruptcy provisions, but it is our view that the FOA Netting Provision would be enforceable based on general principles of bankruptcy law which apply to executory contracts, such as a FOA Netting Agreement or a Clearing Agreement, as applicable. There is no court ordered stay in this proceeding. The statutory stays do not apply to contractual rights of termination. Further, the BIA allows for the application of the general law of set-off as it applies outside of a proceeding in a BIA Bankruptcy, which we believe includes contractual netting of mutual obligations, such as are provided for under the FOA Netting Provision. Consequently, in a BIA Bankruptcy, the FOA Netting Provision would be effective with respect to Transactions.
    - **BIA Bankruptcy of Investment Firms/Broker Dealers.** Securities firms (which includes Investment Firms/Broker Dealers that deal as agent for customers) are also subject to a special liquidation regime under the BIA involving the pooling of assets to meet customer claims. Section 254(4) of Part XII of the BIA provides that nothing in Part XII affects the rights of a party to a contract, including an EFC, with respect to termination, netting or setting off or compensation. Consequently, it should not generally affect the operation of the termination and netting rights under the FOA Netting or Clearing Agreement.
    - **Receivership.** A court order appointing a receiver and manager will often prevent the termination of contracts. This type of order is generally intended to prevent utilities and other suppliers from terminating their arrangements with the debtor in a way which would prejudice the receiver and manager's opportunities to sell

the business as a going concern. In theory, the order preventing termination may be drafted widely enough to capture an FOA Netting Agreement or a Clearing Agreement. We believe that, even if an original order was drafted so widely as to capture an FOA Netting Agreement or a Clearing Agreement, a court would amend this order to exclude it upon a motion by the Non-Defaulting Party. A court administered receivership is, in essence, a liquidation proceeding, not a creditor reorganization proceeding, and consequently, a court would be reluctant to allow a situation that differs so markedly from that under either the BIA, CCAA or WURA.

- **Corporate Plans of Arrangement.** With respect to Corporate Plans, we believe that a court before which the issue was fully argued would not grant a stay delaying or preventing enforceability of the FOA Netting Provisions in the face of the generally applicable bankruptcy principles relating to executory contracts and the statutory recognition of termination and netting rights for EFCs in other insolvency regimes.

- In the remaining Canadian Insolvency Proceedings (e.g. CCAA, WURA, BIA Proposal) there are automatic or court ordered stays that prevent the exercise of termination or acceleration rights and that delay or otherwise interfere with liquidation rights. Rights of set-off, including likely contractual set-off, as long as the obligations are mutual, are recognized in these Insolvency Proceedings, but may be subject to temporary stays.[7] However, in each of these Insolvency Proceedings there is an exemption for termination and netting rights under EFCs. There is express recognition of the right to terminate and to calculate a net termination amount with respect to "eligible financial contracts" if the contract between the parties expressly provides for such termination and netting. If the Transactions are not EFCs, then the right to terminate and accelerate obligations under those Transactions may be stayed (unless the PCSA applies) and this will affect the ability to calculate a Liquidation Amount or Cleared Set Termination Amount, as applicable, with respect to such Transactions.

- Where no other exemption is available or to provide certainty in those proceedings without an express exemption, the PCSA may provide an exemption for EFCs and other Transactions if the termination and

[7] See more detailed analysis in paragraph 3.7.

liquidation occurs pursuant to a "netting agreement" (which in our view would include an FOA Netting Agreement or a Clearing Agreement) between (i) "financial institutions" or (ii) a participant in a clearing system and its customer. To the extent a party relies on (ii) above, the relevant agreement will be a "netting agreement" with respect to the cleared transactions only. Certain business corporations, including Investment Firms/Broker Dealers, are "financial institutions" as defined in the PCSA. With respect to Transactions that are not cleared, as long as the Client is also a "financial institution" the PCSA should apply. The PCSA is described in more detail in Schedule 1.

- Any Transaction listed on Annex 2, part A (i) to (iv) and any Transaction specifically listed in Annex 2, part (E) is in our view an EFC subject to meeting the general criteria relevant to all Transaction types. Transactions listed on Annex 2, parts (B), (C) and (D), part A(v) and Part E (unless specifically listed therein) may be EFCs if they are of a type listed in the definition of EFC and they meet general criteria relevant to all Transaction types. Each of the FOA Agreement and the Clearing Agreement would, to the extent of the FOA Netting Provision and its application to Transactions, also be characterized as an EFC. The definition of EFC and criteria for being an EFC are set out at Annex 8.
- More detail is provided in the qualifications in paragraph 4 as they relate to each Insolvency Proceeding. A chart is available at Annex 7 to summarize this analysis.

No amendments to the FOA Netting Provision are necessary in order for the opinions expressed in this paragraph 3.3 to apply.

3.4 Enforceability of the Clearing Module Netting Provision

Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.4 and the qualifications in paragraph 4, in relation to a Clearing Agreement which includes the Clearing Module Netting Provision, the Clearing Module Netting Provision will be immediately (and without fulfilment of any further conditions) enforceable in accordance with its terms so that, following (i) a Firm Trigger Event or (ii) a CCP Default, the Parties would be entitled to receive or obliged to pay, in respect of each Cleared Transaction Set, only a net sum incorporating:

3.4.1 the positive and negative mark-to-market values of the relevant individual Client Transactions that are terminated in accordance with the Clearing Agreement;

3.4.2 any unpaid amount in respect of such terminated Client Transactions;

3.4.3 any Relevant Collateral Value associated with such terminated Client Transactions; and

3.4.4 any other amount attributed to such Client Transactions.

We are of this opinion because generally, contractually binding termination rights and rights to set-off mutual obligations arising under such contractual arrangements are not contrary to bankruptcy principles, such as the anti-forfeiture principle, or rendered ineffective by the Insolvency Statutes. This conclusion is subject to the discussion which follows dealing with stay orders and laws.

There are rules of law in this jurisdiction which could impose a moratorium or stay which would prevent, delay or otherwise affect the exercise of such rights by the applicable Party, but in many cases an exemption from the moratorium or stay will apply. Please see paragraph 3.3 for a summary of such rules of law which apply equally in connection with the Clearing Module Netting Provision.

Application of PCSA

We note in particular in this context that the definition of a "netting agreement", for the purposes of the application of the overriding termination and liquidation protections in the PCSA, includes an agreement between a participant in a clearing system and a customer to whom it provides clearing services, regardless of whether the customer is a financial institution. The PCSA would therefore apply to a Transaction between two Parties as a result of the fact that such Transaction was entered into on, or is back to back with a Transaction entered into on an exchange (in this or another jurisdiction), or is cleared at, or is back-to-back with a transaction to be cleared by a central counterparty.

Previously, the PCSA's overriding safe-harbour for termination, netting and dealings with financial collateral generally only applied to agreements between financial institutions. However, as of December 14, 2012, it applies also to an agreement between "a participant and a customer to which the participant provides clearing services". "Participant" means a member of a clearing house or a party to an arrangement that establishes a clearing and settlement system. "Clearing house" means a corporation, association, partnership, agency or other entity that provides clearing or settlement services for a clearing and settlement system. It includes a securities and

derivatives clearing house, as defined in subsection 13.1(3) of the PCSA[8]. A "clearing and settlement system" means a system or arrangement for the clearing or settlement of payment obligations or payment messages in which:

(a) there are at least three participants, at least one of which is a Canadian participant and at least one of which has its head office in a jurisdiction other than the jurisdiction where the head office of the clearing house is located;

(b) clearing or settlement is all or partly in Canadian dollars; and

(c) except in the case of a system or arrangement for the clearing or settlement of derivatives contracts, the payment obligations that arise from clearing within the system or arrangement are ultimately settled through adjustments to the account or accounts of one or more of the participants at the Bank.

It includes a system or arrangement for the clearing or settlement of securities transactions, derivatives contracts, foreign exchange transactions or other transactions if the system or arrangement also clears or settles payment obligations arising from those transactions.

The significance of this provision is that the overriding netting protections of the PCSA will applied to cleared sets of Transactions between a Client and Firm or Clearing Member, as the case may be. This may be important in the context of Insolvency Proceedings without an express safe-harbour for termination, netting and collateral dealing rights under an EFC.

No amendments to the Clearing Module Netting Provision are necessary in order for the opinions expressed in this paragraph 3.4 to apply.

3.5 Enforceability of the Addendum Netting Provision

Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.5 and the qualifications in paragraph 4, in relation to a Clearing Agreement which includes the Addendum Netting Provision, the Addendum Netting Provision will be immediately (and without fulfilment of any further conditions) enforceable in accordance with its terms so that, following (i) a

[8] These are Canadian Derivatives Clearing Corporation, CDS Clearing and Depository Services, the WCE Clearing Corporation and any other securities and derivatives clearing house designated by the Minister of Finance.

CM Trigger Event or (ii) a CCP Default, the Parties would be entitled to receive or obliged to pay only, in respect of each Cleared Transaction Set, a net sum incorporating:

3.5.1 the positive and negative mark-to-market values of the relevant individual Client Transactions that are terminated in accordance with the Clearing Agreement;

3.5.2 any unpaid amount in respect of such terminated Client Transactions;

3.5.3 any Relevant Collateral Value associated with such terminated Client Transactions; and

3.5.4 any other amount attributed to such Client Transactions.

We are of this opinion because generally contractually binding termination rights and rights to set-off mutual obligations arising under such contractual arrangements are not contrary to bankruptcy principles, such as the anti-forfeiture principle, or rendered ineffective by the Insolvency Statutes. This conclusion is subject to the discussion which follows dealing with stay orders and laws.

There are rules of law in this jurisdiction which could impose a moratorium or stay which would prevent, delay or otherwise affect the exercise of such rights by the applicable Party, but in many cases an exemption from the moratorium or stay will apply. Please see paragraph 3.3 for a summary of such rules of law which apply equally in connection with the Addendum Netting Provision.

Please see the discussion under "*Application of PCSA*" in paragraph 3.4 which applies equally to Client Transactions which are subject to ISDA/FOA Clearing Addendum.

No amendments to the ISDA/FOA Clearing Addendum Netting Provision are necessary in order for the opinions expressed in this paragraph 3.5 to apply.

3.6 Use of FOA Clearing Module or ISDA/FOA Clearing Addendum not detrimental to FOA Netting Provision

In relation to a Clearing Agreement, the opinions expressed at paragraph 3.3 above in relation to the FOA Netting Provision are not affected by the use of the FOA Clearing Module or the ISDA/FOA Clearing Addendum in conjunction with the FOA Netting Agreement. In a case where a Party, who

would (but for the use of the FOA Clearing Module or the ISDA/FOA Clearing Addendum) be the Defaulting Party for the purposes of the FOA Netting Agreement, acts as Firm (as defined in the FOA Clearing Module) or Clearing Member (as defined in the ISDA/FOA Clearing Addendum), the question as to whether FOA Netting Provision will, to the extent inconsistent with the Clearing Module Netting Provision or, as the case may be, the Addendum Netting Provision, be superseded by the Clearing Module Netting Provision or, as the case may be, the Addendum Netting Provision. would be determined under the governing law of the Clearing Agreement.

3.7 Enforceability of the FOA Set-Off Provisions

3.7.1 Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.7 and the qualifications in paragraph 4, in relation to an FOA Netting Agreement which includes the FOA Set-Off Provisions, the FOA Set-Off Provisions will be immediately (and without fulfilment of any further conditions) enforceable in accordance with their terms, so that, following an Event of Default, the Non-Defaulting Party would be immediately entitled to exercise its rights under either or both of the FOA Set-Off Provisions, and in particular so that, upon the exercise of such rights:

(a) where the FOA Set-Off Provisions include the General Set-Off Clause:

(i) the value of any cash balance owed by the Non-Defaulting Party to the Defaulting Party would be set off against the Liquidation Amount (where owed by the Defaulting Party); or

(ii) the value of any cash balance owed by the Defaulting Party to the Non-Defaulting Party would be set off against the Liquidation Amount (where owed by the Non-Defaulting Party); or

(b) where the FOA Set-Off Provisions comprise the Margin Cash Set-Off Clause only, the value of any cash margin owed by the Firm to the Client would be set-off against the Liquidation Amount (where such Liquidation Amount is owed by the Client).

We are of this opinion because there is no generally applicable law of this jurisdiction which would apply to prohibit the Parties from entering into a contract upon the terms of the FOA Set-Off Provisions or which would render such terms ineffective. However, we note that (1) enforceability of the FOA Set-Off Provisions assumes an ability to terminate and, as set out in paragraph 3.3, termination may be stayed if the Transactions are not EFCs, (2) even if not delayed by this stay, the right to set-off requires that the obligations be accrued due at the date of commencement of the Insolvency Proceeding, and (3) to the extent the set off calculation includes the cash margin exercise of the right may be subject to priority under the relevant priority law.

Cash Margin/ Cash Balance Owed by Non-Defaulting Party

Several years ago, the Quebec legislator amended the *Derivatives Act* (Quebec) to add two sections in respect of set-off rights over cash and cash collateral. The sections provide as follows:

> MARGIN OR SETTLEMENT DEPOSIT
>
> 11.1. An instrument under which a person is required to pay an amount of money to a party to a derivative, including as a margin or settlement deposit, and which allows that party, in all circumstances described in the instrument, to extinguish or reduce, by means of a set off, its obligation to repay that amount to the person is enforceable against third persons without further formality.
>
> Such an instrument is governed by the law expressly designated in it or the designation of which may be inferred with certainty from the terms of the instrument.
>
> 11.2. For the purpose of section 11.1, the following are considered to be derivatives:
>
> (1) an exchange, securities lending or securities redemption contract, including any contract governing such a contract; and
>
> (2) a contract between a clearing house and one of its members, and the rules governing their relationship.

In our view, under Quebec law, section 11.1 of the *Derivatives Act* would apply to the FOA Netting Agreement. Therefore, pursuant to this section, the characterization and enforceability of the Set-Off

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

Provisions would be governed by the law governing the Agreement, that is English law, and not Quebec law and, in addition, as provided in 11.1, no "further formality" is required to be accomplished under Quebec law. Therefore, in our view, even if English law were to recharacterize the Set-Off Provisions as creating a security interest in the cash margin, Quebec law would not require the accomplishment of any further actions in order to render such security interest enforceable against third parties.

There are, however, super-priority statutorily created deemed trusts, security interests and liens that apply with respect to certain types of obligations. There may be court ordered liens in certain Insolvency Proceedings. These are further described in Annex 9. The *Derivatives Act* provisions set out above would not be applicable to such trusts, security interests and liens.

There are also automatic or court ordered stays that could apply to any realization on that cash margin to the extent it is credit support for obligations under Transactions that are not EFCs, as summarized below.

Set-off of Cash Margin Cash Balance Owed by Defaulting Party or Non-Defaulting Party

Generally rights to set-off liquidated mutual claims accrued at the date of the commencement of the proceeding under contract set-off provisions are enforceable in Insolvency Proceedings. The right to set-off the cash margin balance whether owing to or by the Non-Defaulting Party to the Liquidated Amount would not be adversely affected by the opening of Insolvency Proceedings as long as it secures Transactions that are EFCs.

The BIA[9], WURA[10] and CCAA[11] expressly provide that the law of set-

[9] 97 (3) The law of set-off or compensation applies to all claims made against the estate of the bankrupt and also to all actions instituted by the trustee for the recovery of debts due to the bankrupt in the same manner and to the same extent as if the bankrupt were plaintiff or defendant, as the case may be, except in so far as any claim for set-off or compensation is affected by the provisions of this Act respecting frauds or fraudulent preferences.

[10] 73. (1) The law of set-off, as administered by the courts, whether of law or equity, applies to all claims on the estate of a company, and to all proceedings for the recovery of debts due or accruing due to a company at the commencement of the winding-up of the company, in the same

off applies in the Insolvency Proceeding to the same extent as it applies outside of it. This includes, under Quebec law,[12] legal set-off (the set-off of mutual certain liquidated claims that are due and payable), judicial set-off (set off stated by the court of claims that are potentially unliquidated at that time) and contractual set-off respecting, most likely, mutual claims.[13]

There are no express provisions with respect to set-off for Receivership or Corporate Plans of Arrangement, but generally rights of set-off are recognized in such proceedings.[14]

Notwithstanding these provisions, rights of set-off may be temporarily delayed in restructuring proceedings such as BIA Proposal, CCAA and Receivership, to give the Insolvency Representative time to assess the claims and the validity of the set-off right.

There is a body of case law to support the extension of rights of set-off to contractual set-off rights as long as the claims are mutual and are due or accruing due at the date of the proceeding.[15] We believe that the calculation of a Liquidation Amount triggered by a post proceeding termination would not preclude set off on the basis that it is a post proceeding debt, but this is not a matter that has received judicial attention in the context of agreements similar to the Agreement. Transactions entered into after the commencement of bankruptcy proceedings under the BIA or the commencement of WURA

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manner and to the same extent as if the business of the company was not being wound up under this Act.

11 21. The law of set-off or compensation applies to all claims made against a debtor company and to all actions instituted by it for the recovery of debts due to the company in the same manner and to the same extent as if the company were plaintiff or defendant, as the case may be.

12 A Quebec court sitting in insolvency proceedings will apply Quebec law for a determination of what is set-off (in Quebec, "compensation") under that law.

13 *Caisse populaire Desjardins de l'Est de Drummond v. Canada*, 2009 SCC 29.

14 Ching v. Jeffrey (1885), 12 O.A.R. 432 (C.A.); Toronto-Dominion Bank v. Block Bros. Contractors Ltd. (1980), 118 D.L.R. (3d) 311 (Alta. Q.B.); Bank of Montreal v. Tudhope (1911), 17 W.L.R. 83 (Man. Q.B.).

15 *Caisse populaire Desjardins de l'Est de Drummond v. Canada*, 2009 SCC 29; Re McMurtry & Co. Ltd., [1924] 1 D.L.R. 737; Re Berman (1979), 105 D.L.R. (3d) 380 (Ont. C.A.); Adatia v. A. Faber Ltd. (2004) 7 C.B.R. (5th) 165 (Ont. S.C.); Re Blue Range Resource Corp., (1999) 245 A.R. 154; Canada (Attorney General) v. Reliance Insurance Company (2009), 58 C.C.L.I. (4th) 220, 40 C.B.R. (5th) 292, 40 B.L.R. (4th) 204.

proceedings cannot be included in the netting calculations.

However, to the extent the cash margin arrangements relate to EFCs, the Non-Defaulting Party can also rely on express safe-harbours that allow a party to deal with any financial collateral under a title transfer credit support arrangement (or a security agreement).

A cash margin arrangement for an EFC is itself also an EFC within the meaning of those Insolvency Statutes that include an EFC safe-harbour. Consequently the right to set-off the cash margin amount to the extent it is margin for an EFC (which can itself include a financial collateral arrangement for another EFC), is exempt from stays (temporary or otherwise) that might otherwise apply.

The PCSA also includes a safe-harbour for any dealings with financial collateral for an EFC under a netting agreement.

The following chart summarizes the recognition of set-off rights in Insolvency Proceedings and the availability of the EFCs safe-harbour with respect to dealing with any margin.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

Set-off Rights and Insolvency Proceeding Stays re Cash Margin

	Likelihood of Stay on Mutual Set-off of Accrued Claims[16]	Statutory Exemption Allowing Dealings with Financial Collateral for Eligible Financial Contracts
BIA Bankruptcy	No stay likely as BIA recognizes rights of set-off for claims accrued due at date of bankruptcy– s.93(3).	Yes
BIA Proposal	While BIA proposal expressly protects set-off rights, it has been interpreted as allowing a temporary delay in order to give the Insolvency Representative time to assess the claims. The period of delay will depend on the timing of the claims process which will vary from proceeding to proceeding.	Yes
WURA	No stay likely as WURA recognizes rights of set-off for claims accrued due at date of liquidation order - (s.73).	Yes
CCAA	While CCAA expressly protects set-off rights for claims accrued due at date of the claims bar date in the proceeding (s.21), it has been interpreted as allowing a temporary delay in order to give the Insolvency Representative time to assess the claims. The period of delay will depend on the timing of the claims process which will vary from proceeding to proceeding.	Yes
Receivership	Unlikely for claims accrued due at the date of the receivership.	No, but it would be acceptable practice in Quebec to follow the CCAA and BIA bankruptcy or proposal exemptions; would be express exemption where PCSA applies
Corporate Plan	Unlikely	No; but would be express exemption where PCSA applies

Set-off Under General Set-off Clause

Set-off pursuant to the General Set-Off Clause is subject to the analysis above. Future and contingent claims might not be available for set-off

[16] Non-mutual set-off may not be enforceable in Insolvency Proceedings.

under the protection for contractual rights of set-off. Also our view is that the claims to be set-off must be mutual and be due or accruing due at the date of commencement of the proceeding. The case law recognizing contractual rights of set-off in Insolvency Proceedings deals largely with claims under specific agreements or of specific types so there is uncertainty as to whether a provision as generally framed as the General Set-Off Clause could support the set-off of any and all claims between the parties.

No amendments to the General Set-Off Clause or the Margin Cash Set-Off Clause are necessary in order for the opinions expressed in this paragraph 3.7.1 to apply. If the General Set-Off Clause is intended to be relied upon to permit set-off of obligations arising under other specific types of agreements, we recommend that those specific agreement types be specifically referred to.

3.7.2 Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.7 and the qualifications in paragraph 4, in relation to a Clearing Agreement which includes the FOA Set-Off Provisions and the Clearing Module Set-Off Provision (insofar as the FOA Set-Off Provisions are not Disapplied Set-Off Provisions) and/or the Addendum Set-Off Provision, the FOA Set-Off Provisions will, to the extent that set-off has not already occurred pursuant to the Clearing Module Set-Off Provision or the Addendum Set-Off Provision, be immediately (and without fulfilment of any further conditions) enforceable in accordance with their terms, so that following an Event of Default in respect of the Client, the Firm or, as the case may be, the Clearing Member would be immediately entitled to exercise its rights under either or both of the FOA Set-Off Provisions, and in particular so that, upon the exercise of such rights:

(a) where the FOA Set-Off Provisions includes the General Set-Off Clause:

(i) the value of any cash balance owed by the Firm or, as the case may be, the Clearing Member to the Client would be set off against the Liquidation Amount (where such liquidation amount is owed by the Client); or

(ii) the value of any cash balance owed by the Client to the Firm or, as the case may be, the Clearing Member would

be set off against the Liquidation Amount (where such liquidation amount is owed by the Firm or, as the case may be, the Clearing Member); or

(b) where the FOA Set-Off Provisions comprise the Margin Cash Set-Off Clause only, the value of any cash margin owed by the Firm or, as the case may be, the Clearing Member to the Client would be set-off against the Liquidation Amount (where such Liquidation Amount is owed by the Client).

We are of this opinion because there are no laws of this jurisdiction which would apply to prohibit the Parties from entering into a contract upon the terms of the FOA Set-Off Provisions or which would render such terms ineffective. However, we note that (1) enforceability of the FOA Set-Off Provisions assumes an ability to terminate and, as set out in paragraph 3.3, termination may be stayed unless the Transactions are EFCs, (2) even if not delayed by this stay, the right to set-off requires that the obligations be accrued due at the date of commencement of the Insolvency Proceeding, and (3) to the extent the set off calculation includes the cash margin exercise of the right is conditional on priority under the relevant priority law. Please also see the discussion in paragraph 3.7.1 under "*Cash Margin Cash Balance Owed by Non-Defaulting Party*", "*Set-Off of Cash Margin Cash Balance Owed by Defaulting Party or Non-Defaulting Party*" and "*Set-off under General Set-off Clause*" which is equally applicable to the opinion expressed in this paragraph 3.7.2.

No amendments to the General Set-Off Clause or the Margin Cash Set-Off Clause are necessary in order for the opinions expressed in this paragraph 3.7.2 to apply. If the General Set-Off Clause is intended to be relied upon to permit set-off of obligations arising under other specific types of agreements, we recommend that those specific agreement types be specifically referred to.

3.8 Set-Off under a Clearing Agreement with a Clearing Module Set-Off Provision

3.8.1 Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.8 and in paragraph 4, in relation to a Clearing Agreement which includes the Clearing Module Set-Off Provision (whether or not the FOA Set-Off Provisions is a Disapplied Set-Off

Provisions, insofar as constituting part of the Clearing Agreement). The Clearing Module Set-Off Provision will be immediately (and without fulfilment of any further conditions) enforceable in accordance with its terms so that the Firm would be immediately entitled to exercise its rights under the Clearing Module Set-Off Provision, and in particular, upon the exercise of such rights:

(a) if the Client is a Defaulting Party, so that the value of any cash balance owed by the Firm to the Client would be set-off against any Liquidation Amount owed by the Client to the Firm; and

(b) if there has been a Firm Trigger Event or a CCP Default, so that the value of any cash balance owed by one Party to the other would, insofar as not already brought into account as part of the Relevant Collateral Value, be set off against any Available Termination Amount owed by the Party entitled to receive the cash balance.

We are of this opinion because there are no laws of this jurisdiction which would apply to prohibit the Parties from entering into a contract upon the terms of the Clearing Module Set-Off Provision or which would render such terms ineffective. However, we note that because (1) enforceability of the Clearing Module Set-Off Provision assumes an ability to terminate and, as set out in paragraph 3.3, termination may be stayed unless the Transactions are EFCs, (2) even if not delayed by this stay, the right to set-off requires that the obligations be accrued due at the date of commencement of the Insolvency Proceeding, (3) to the extent the set off calculation includes the cash margin exercise of the right is conditional on priority under the relevant priority law. Please also see the discussion in paragraph 3.7.1 under "*Cash Margin Cash Balance Owed by Non-Defaulting Party*", "*Set-Off of Cash Margin Cash Balance Owed by Defaulting Party or Non-Defaulting Party*" and "*Set-off under General Set-off Clause*" which is equally applicable to the opinion expressed in this paragraph 3.8.1. The case law recognizing contractual rights of set-off in Insolvency Proceedings deals largely with claims under specific agreements or of specific types so there is uncertainty as to whether a provision as generally framed as the Clearing Module Set-Off Provision could support the set-off of any and all claims between the parties.

No amendments to the Clearing Module Set-Off Provision are necessary in order for the opinions expressed in this paragraph 3.8.1 to apply. If the Firm intends to rely on the Clearing Module Set-Off Provision to support the set off

of claims under specific types of agreements, we recommend referring to the specific agreement types in this provision.

3.8.2 In relation to a Clearing Agreement which includes the Clearing Module Set-Off Provision for which the FOA Set-Off Provision (insofar as constituting part of the FOA Netting Agreement) is not a Disapplied Set-Off Provision, the Clearing Module Set-Off Provision will be immediately (and without fulfilment of any further conditions) enforceable in accordance with its terms, as set-out in and subject to the same qualifications, conditions and exceptions expressed in paragraph 3.8.1 above; and the FOA Set-Off Provision will, to the extent that set-off is not already covered by the Clearing Module Set-Off Provision, be immediately (and without fulfilment of any further conditions) enforceable in accordance with its terms, as set out in and subject to qualifications, conditions and exceptions expressed in paragraph 3.7.1 above.

3.9 Set-Off under a Clearing Agreement with an Addendum Set-Off Provision

Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.9 and the qualifications in paragraph 4, in relation to a Clearing Agreement which includes the Addendum Set-Off Provision, the Addendum Set-Off Provision will be immediately (and without fulfilment of any further conditions) enforceable in accordance with its terms so that following (i) a CM Trigger Event (as defined in the ISDA/FOA Clearing Addendum) or (ii) a CCP Default (as defined in the ISDA/FOA Clearing Addendum):

(a) in the case of a CM Trigger Event, the Client (as defined in the ISDA/FOA Clearing Addendum); or

(b) in the case of a CCP Default, either Party (the "**Electing Party**"),

would be immediately entitled to exercise its rights under the Addendum Set-Off Provision, and in particular so that, upon the exercise of such rights, in the case of a CM Trigger Event, any Available Termination Amount would be reduced by its set-off against any cash balance which constitutes a termination amount payable by (or to) a Party which is owed (or owes) the Available Termination Amount, insofar as not already brought into account as part of the Relevant Collateral Value.

We are of this opinion because there are no laws of this jurisdiction which would apply to prohibit the Parties from entering into a contract upon the

terms of the Addendum Set-Off Provision or which would render such terms ineffective. However, we note that (1) enforceability of the Addendum Set-Off Provisions assumes an ability to terminate and, as set out in paragraph 3.3, termination may be stayed unless the Transactions are EFCs, (2) even if not delayed by this stay, the right to set-off requires that the obligations be accrued due at the date of commencement of the Insolvency Proceeding, and (3) to the extent the set off calculation includes the cash margin exercise of the right is conditional on priority under the relevant priority law. Please also see the discussion in paragraph 3.7.1 under "*Cash Margin Cash Balance Owed by Non-Defaulting Party*", "*Set-Off of Cash Margin Cash Balance Owed by Defaulting Party or Non-Defaulting Party*" and "*Set-off under General Set-off Clause*" which is equally applicable to the opinion expressed in this paragraph 3.9. The case law recognizing contractual rights of set-off in Insolvency Proceedings deals largely with claims under specific agreements or of specific types so there is uncertainty as to whether a provision as generally framed as the Addendum Set-Off Provision could support the set-off of any and all claims between the Parties.

No amendments to the Addendum Set-Off Provision are necessary in order for the opinions expressed in this paragraph 3.9 to apply. If the Clearing Member intends to rely on the Addendum Set-Off Provision to support the set off of claims under specific types of agreements, we recommend referring to the specific agreement types in this provision.

3.10 Enforceability of the Title Transfer Provisions

3.10.1 Subject to the conditions, qualifications and exceptions expressed in this paragraph 3.10, in relation to an FOA Netting Agreement (with Title Transfer Provisions) or in relation to a Clearing Agreement which includes the Title Transfer Provisions where the Client is the Defaulting Party, following the specification or deemed occurrence of a Liquidation Date, the Non-Defaulting Party would be immediately (and without fulfilment of any further condition) entitled to exercise its rights under the Title Transfer Provisions, so that the Default Margin Amount (as calculated pursuant to the terms of the Title Transfer Provisions) shall be taken into account for the purposes of calculating the Liquidation Amount pursuant to the FOA Netting Provision.

We are of this opinion because there are no laws of this jurisdiction which would apply to prohibit the Parties from entering into a contract

upon the terms of the Title Transfer Provisions or which would render such terms ineffective. Generally, the courts of this jurisdiction will give effect to the intention of the parties such that, where the terms of the arrangement are that title to the collateral be transferred from the transferor to the transferee, and that the transferor was to retain no proprietary interest in such collateral but would merely have a contractual right to receive equivalent cash or securities transferred to it by the transferee at some future point in time. In this context, Clause 7.2 of the Title Transfer Provision provides that all right, title and interest in any collateral shall vest in the transferee, and that the parties do not intend to create a security interest over such collateral, and the consequences of such vesting of title in the transferee are reflected in the inclusion of the Default Margin Amount in the calculation of a Liquidation Amount pursuant to Clause 5 of the Title Transfer Provisions as described above in this paragraph 3.10.1. In this regard we also refer you to paragraphs 2.9 and 2.14 above. However, such arrangements might also be characterized as creating a security interest and the implications and possibility of characterization as a security interest are discussed immediately below and in paragraph 3.7.1.

Civil Code Implications

Notwithstanding that the FOA Netting Agreement (with Title Transfer Provisions) or, as the case may be, a Clearing Agreement which includes the Title Transfer Provisions does not purport to create a security interest in any Margin Transferred, there is a possibility that it would nevertheless be characterized as a security agreement for purposes of Quebec security interest law although, given the formalistic nature of Quebec law, this is likely less of a risk than in Ontario. The fact that the property may be located outside of Quebec is not relevant. The location of the Defaulting Party is relevant to the Civil Code with respect to cash margin. There are no further recommended steps to protect against characterization as it is a risk inherent in the fact that the margin is intended to provide credit support for obligations and not in the form of the agreement.

Validity, Perfection and Priority. If characterized as a security agreement,[17] for any cash margin not credited to a securities account,

[17] See discussion at para. 3.7.1 of *Derivatives Act* (Quebec).

the laws of Quebec would govern the validity or perfection of a security interest over such cash where the Defaulting Party is domiciled in Quebec at the time of creation or perfection. Therefore, recognition that the Non-Defaulting Party had an enforceable security interest that could be asserted against other consensual secured creditors or an Insolvency Representative would require compliance with the requirements of the Civil Code with respect to the validity and perfection (in Quebec, publication) of the security interest which would include amendment of the Netting or Clearing Agreement to create a valid conventional movable hypothec without delivery in such cash margin. In addition, to perfect the security interest, the secured party would be required to register a Form RH with a central Quebec government registry, the Register of personal and movable real rights. An initial registration period of 10 years is possible and registration can be renewed. If there are any prior perfected secured creditors (including statutory lien and other claimants), the Non-Defaulting Party's ability to realize on the security interest might be impeded.

If characterized as a security agreement, the validity, perfection and priority of any security interest in financial assets[18], which would include securities or cash margin credited to a securities account, credited to a securities account with an intermediary located inside or outside of Quebec would be governed by the law of the securities intermediary's jurisdiction.[19] As long as the Non-Defaulting Party had control[20] of the security entitlement relating to the financial assets, no further action would be required in order to create a valid perfected security interest under Quebec law. (See the opinion in paragraph 3.7.1 for the analysis of the characterization risk.)

Realization Procedures. Quebec law does not clearly provide for what law governs realization procedures. In our view, substantive issues with respect to a secured party's right to enforce a security interest will likely be determined by the law governing perfection of the security agreement or the domicile of the grantor and procedural issues with respect to a secured party's right to enforce a security interest will be determined by the law of the place where the enforcement rights are

18 See Annex 10 for definition of financial asset.

19 See footnote 6.

20 See Annex 10 for definition of control.

exercised. Therefore, (i) if the Title Transfer Provisions were characterized as creating a security interest in the Transferred Margin under Quebec law; and (ii) if Quebec were the law governing perfection of the security interest or enforcement rights were exercised in Quebec, then the "secured party" would have to comply with the procedural requirements of the Civil Code and/or *Code of Civil Procedure* (Quebec), including providing notice and exercising only the security party rights provided in the Civil Code.

Unless the security interest provides that the grantor of the security interest is authorized to collect any claims (roughly equivalent to receivables and would include debt obligations, proceeds and distributions forming part of the collateral), from the moment of execution of a hypothec on a claim, the creditor has the right to collect the same (Art. 2743 CCQ). This right is in addition to any hypothecary rights respecting enforcement. If the grantor is authorized in the security interest agreement to collect the claims, this authorization may be withdrawn at any time by the creditor, subject to the terms of the security agreement (Art. 2745 CCQ). However a notice of withdrawal must be registered and the grantor and the account debtors appropriately notified. We would not characterize these as matters of a procedural nature with respect to enforcement.

For cash which is not held in a securities account, if the Title Transfer Provisions were characterized as creating a security interest in the Transferred Margin under Quebec law and the "secured party" effected the appropriate steps to create and perfect a valid Quebec security interest (modification of agreement and registration), then the secured party may have to comply with the procedural requirements of the Civil Code. This includes (i) sending a prior notice of the intention to exercise a specific hypothecary right (which notice must be registered at the Register), and (ii) in general, waiting the required period, normally 20 days, before exercising the specific right. There are four hypothecary rights available if the security interest charges assets used in a business: taking of possession for the purposes of administration, taking in payment, sale by the creditor and sale by judicial authority. Only one of these rights may be exercised at a time. The rights of taking in payment (roughly equivalent to foreclosure) and sale by judicial authority are available even if the security interest does not charge assets used in an enterprise. There are other requirements in

the Civil Code if a secured party wishes to take the collateral in payment of the debtor's obligations, including giving notice to the grantor and all subsequent hypothecary creditors of the collateral. Court approval must be obtained before "taking in payment" is exercised if the debtor has already discharged one-half or more of the obligations secured by the hypothec.

If the Title Transfer Provisions were characterized as creating a security interest in Transferred Margin which consisted of securities and security entitlements within the meaning of the QSTA, by virtue of Article 2759 of the Civil Code, a secured party which has control and which has a security interest on such securities or security entitlements may, where permitted by its agreement with the grantor of the security interest, sell the securities or security entitlements or otherwise dispose of them without giving prior notice, obtaining surrender or observing any time limits prescribed under the Civil Code. The same article provides that a secured party without control may, if the agreement so permits, dispose of the securities and security entitlements without following the Civil Code formalities if the securities or security entitlements are of the type, dealt in or traded on securities exchanges or financial markets. The secured party must impute the proceeds to payment of the costs incurred to dispose of the securities or the security entitlements, to payment of the obligations secured by prior ranking security and finally to payment of the secured obligations and remit any surplus to the grantor.

If the Margin Transferred is "financial collateral" for an "eligible financial contract", there will be no material stay risk in Insolvency Proceedings with respect to any dealing with that property, including treating its value as part of the calculation of the Liquidation Amount. Securities and cash would constitute financial collateral. As long as the obligations for which the Margin Transferred was provided as credit support are EFCs, the right to net the value of the Margin Transferred or its proceeds as part of the calculation of the Liquidating Amount will be subject to the EFC safe-harbours.

In addition, securities firms (which includes Investment Firms/Broker Dealers that deal as agent for customers) are subject to a special liquidation regime under the BIA involving the pooling of assets to meet customer claims. However, Section 254(4) of Part XII of the BIA

provides that nothing in Part XII affects the rights of party to a contract, including an eligible financial contract, with respect to termination, netting or setting off or compensation. Further, Section 254(5) states that the operation of Part XII is subject to the rights of secured creditors and therefore the Non-Defaulting Party can rely on the express safe-harbours discussed above that allow a party to deal with any "financial collateral" under a title transfer credit support arrangement (or a security agreement). Consequently, Part XII should not generally affect the exercise of a Party's rights in respect of financial collateral under the FOA Netting or Clearing Agreement except as set out below (please see, however, the caveat below pertaining to Commodity Securities).

Please also see the discussion in paragraph 3.4 under "*Application of PCSA*" which applies equally in connection with the Title Transfer Provisions.

Commodity Securities would not constitute financial collateral. Hence there is Insolvency Proceeding stay risk with respect to this type of Transferred Margin.

This risk applies even with respect to Transferred Margin located outside of Canada as far as Canadian law is concerned for domestic Canadian parties. A Canadian Insolvency Representative may have to seek the assistance of foreign courts to enforce its jurisdiction over assets outside of Canada. If Canada is not the jurisdiction of the main insolvency proceeding, but only for ancillary proceedings with regard to Canadian located assets, then the stay would likely not reach to such assets.

The following chart summarizes the stay risk:

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

Margin Enforcement and Insolvency Proceeding Stays and Exemptions

	Stay on Realization of Security Interests	Length of Stay on Realization of Credit Support (without statutory exemption)	Statutory Exemption Allowing Dealing with Financial Collateral for EFCs
BIA Bankruptcy	Unlikely (but possible) for securities, cash or other margin with easily determined value	Up to 6 months	Yes
BIA Proposal	Automatic stay on dealings with credit support	Up to 6 months plus possibility that plan may stay permanently (subject to new default) or otherwise compromise rights	Yes
WURA	Unlikely (but possible) for securities, cash or other margin with easily determined value	Up to 6 months (may be longer in restructuring proceedings)	Yes
CCAA	Automatic stay on dealings with credit support	No limit; plus possibility that plan or court order may stay permanently (subject to new default) or otherwise compromise rights	Yes
Receivership	Unlikely (but possible) for securities, cash or other margin with easily determined value	No limit	No, but it would be acceptable practice in Quebec to follow the practice in CCAA and other BIA proceedings so order will likely include an exemption; express exemption if PCSA applies
Corporate Plan	Unlikely (but possible) for securities, cash or other margin with easily determined value	No limit	No

3.10.2 In relation to a Clearing Agreement which includes the Title Transfer Provisions, and in the case of a Firm Trigger Event, a CM Trigger Event, or a CCP Default, the value of the Transferred Margin would be taken into account as part of the Relevant Collateral Value.

3.10.3 As discussed in paragraph 3.10.1 under the healing "*Civil Code Implications*", there is a risk that courts of this jurisdiction may

characterize transfers of margin in the form of cash under the Title Transfer Provisions of an FOA Netting Agreement (with Title Transfer Provisions) or, as the case may be, a Clearing Agreement which includes the Title Transfer Provisions, as creating a security interest.

3.10.4 A Party shall be entitled to use or invest for its own benefit, as outright owner and without restriction, any Margin Transferred to it pursuant to the Title Transfer Provisions of an FOA Netting Agreement (with Title Transfer Provisions), or as the case may be, a Clearing Agreement which includes the Title Transfer Provisions.

To the extent it applies, the Civil Code allows (i) a secured creditor with a pledge (that is a Quebec security interest with possession) to use the property with the permission of the debtor and (ii) a secured creditor with "control" of securities or "security entitlements" to alienate or grant a hypothec on the collateral unless the agreement provides otherwise. Therefore, even if the Title Transfer Provisions of an FOA Netting Agreement (with Title Transfer Provisions), or, as the case may be, a Clearing Agreement which includes the Title Transfer Provisions are characterized as a security agreement, this provision would permit a Party to use or invest the Transferred Margin without being in breach of the usual statutory duties of a secured party to maintain the collateral.

Article 2714.6 of the Civil Code provides that a secured party having a movable hypothec with delivery on securities or security entitlements may alienate or grant a hypothec on the collateral unless agreed otherwise with the debtor. A person acquires a security entitlement when a securities intermediary (i) credits a financial asset to such person's securities account by book entry, (ii) receives a financial asset from or acquires a financial asset for such person and accepts it for credit to such person's securities account, or (iii) is obligated to credit a financial asset to such person's securities account. A person has a security entitlement upon satisfaction of one of these three methods of acquisition, regardless of whether the securities intermediary actually holds the financial asset.

We would note that neither the QSTA nor the Civil Code contains a provision dealing with continuance of control and, under Quebec law, a secured party must continue to have control in order to continue to have a valid and published security interest (for security interests

whose perfection depends upon control). From a practical standpoint, if a secured party has obtained control of a security entitlement by becoming the entitlement holder itself, then it may deal with the security entitlement as it pleases without any intervention from the debtor. The same is also true in respect of control by way of a control agreement for all security entitlements in a securities account over which the secured party has control. The secured party would have control of all present and future financial assets in such securities account irrespective of the moment that a financial asset is credited to the securities account.

We are assuming that the law of the place where the Transferred Margin is located would permit such use.

No amendments to the Title Transfer Provisions are necessary in order for the opinions expressed in this paragraph 3.10 to apply.

3.11 Use of Security Interest Provisions not detrimental to Title Transfer Provisions

In relation to an FOA Netting Agreement (with Title Transfer Provisions) and in relation to a Clearing Agreement which includes the Title Transfer Provisions, the opinions expressed above in paragraph 3.10 (*Enforceability of the Title Transfer Provisions*) in relation to the Title Transfer Provisions are not affected by the use of the Security Interest Provisions (whether in respect of non-cash margin and/or cash margin) as part of an FOA Netting Agreement (with Title Transfer Provisions), or as part of a Clearing Agreement which includes the Title Transfer Provisions, provided always that:

(i) a provision in the form of, or with equivalent effect to, Clauses 4.3 and/or 4.4 of the FOA Clearing Module is used or the agreement otherwise unambiguously specifies the circumstances in which the Security Interest Provisions or the Title Transfer Provisions apply in respect of any given item of margin so that it is not possible for both the security interest provisions and the Title Transfer Provisions to apply simultaneously to the same item of margin; and

(ii) the pool of margin subject to a security interest and the pool of margin subject to the Title Transfer Provisions are operationally segregated.

3.12 Single Agreement

Where there is express statutory recognition of termination and netting rights (i.e. BIA Proposal, CCAA, WURA or if PCSA applies), it is not necessary that the Transactions and the FOA Netting Agreement or, as the case may be, the Clearing Agreement are part of a single agreement in order for the termination and liquidation under the FOA Netting Provision, the Clearing Module Netting Provision or the Addendum Netting Provision to be enforceable. However, where general principles of insolvency might have to be relied upon (i.e. BIA Bankruptcy, Receivership, Corporate Plans of Arrangement and the PCSA does not apply) it would be helpful if all Transactions were to be treated as a single agreement. In our view, the FOA Netting Agreement or, as the case may be, the Clearing Agreement, and Transactions are part of a single agreement because of the fact that they expressly so provide.

3.13 Automatic Termination

It is not necessary for the Parties to agree to an automatic, rather than an optional, termination and liquidation under the FOA Netting Provision, the Clearing Module Netting Provision and/or the Addendum Netting Provision to ensure the effectiveness of netting under the FOA Netting Agreement or, as the case may be, the Clearing Agreement in the event of bankruptcy, liquidation, or other similar circumstances where the EFC safe-harbours apply. It is not the practice to include automatic termination provisions in netting agreements with respect to Quebec counterparties as it would be subject to the same analysis as optional provisions.

3.14 Multibranch Parties

We do not consider that the use of the FOA Netting Agreement or, as the case may be, the Clearing Agreement by a party with branches in a number of different jurisdictions, including some where netting may not be enforceable would jeopardise the enforceability of the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provision, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision or the Title Transfer Provisions in so far as the laws of this jurisdiction are concerned.

3.15 Insolvency of Foreign Parties

Where a Party is incorporated or formed under the laws of another jurisdiction and an Event of Default or a Firm Trigger Event or, as the case

may be, a CM Trigger Event occurs in respect of such Party (a "**Foreign Defaulting Party**") the Foreign Defaulting Party can be subject to Insolvency Proceedings with respect to its assets located in this jurisdiction. In Canadian Insolvency Proceedings, the Insolvency Representative is given jurisdiction over the world wide assets of the entity and has the power to seek to enforce interests outside of Canada. It can seek recognition orders in foreign courts to assist in taking control of such assets. Whether any court outside of Canada would provide such assistance to a Canadian insolvency representative is not within the scope of this opinion.

While a Canadian court may entertain concurrent main proceedings or ancillary proceedings that defer to various degrees with main or concurrent proceedings in a foreign jurisdiction, the BIA and CCAA both have explicit provisions dealing with international insolvencies that allow the court to recognize a foreign insolvency representative and to enter into protocols to deal with creditor claims in various ways. There can be concurrent main proceedings under the BIA or CCAA and the foreign regime or there can be a main proceeding in a foreign state and ancillary proceedings in Canada under section 18.6 of the CCAA or section 271 of the BIA. There can be various other types of proceedings, such as a receivership in Canada and a proceeding of various types under foreign proceedings (e.g. Chapter 15 or Chapter 11 proceedings under the U.S. Bankruptcy Code). The current procedures adopt a balance between principles of comity and protecting domestic creditors and debtors. In policy terms, the BIA and CCAA provisions are close to the objectives of the UNCITRAL Model Law on Cross-Border Insolvency. The scope for judicial discretion is broad in either regime, including a discretion to enforce or decline to enforce any order made by a foreign court. The court will consider public policy and generally would not make orders contrary to domestic law.

The BIA and CCAA[21] adopt a modified version of the Model Law. These provisions are different in each of the BIA and CCAA reflecting the fact that the BIA is both a liquidation and restructuring regime and the CCAA a restructuring regime.[22] The provisions allow for cross-border cooperation and coordination. If a recognition order is granted under the provisions, the

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21 S.C. 2005, c.47 as amended by S.C. 2007, c.36. Proclaimed into force on September 19, 2009.

22 The many ways in which this law differs from the Model Law is beyond the scope of this opinion. We refer you to an article on this topic: Janis Sarra, 16 Int. Insolv. Rev. 19-61 (2007) entitled *Northern Lights, Canada's Version of the UNCITRAL Model Law on Cross-Border Insolvency*. Please note that S.C. 2007, c.36 made further amendments to the law that are not reflected in the article.

court may make any order that it considers appropriate on the foreign representative's application, if it is satisfied that it is necessary for the protection of the debtor company's property or the interests of creditors. Certain stay orders (stay of domestic proceedings for example) are mandatory once a recognition order is made. The Acts specifically state that the Canadian court is not obligated to make any order contrary to public policy. The Model Law is not incorporated into the WURA, which will continue to allow for cross-border cooperation consistent with the court's territorial jurisdiction over institutions doing business in Canada.

3.16 Special legal provisions for market contracts

Please see the discussion in paragraph 3.4 under "*Application of PCSA*" which is pertinent to the FOA Clearing Module, the ISDA/FOA Clearing Addendum and the Title Transfer Provisions.

4. QUALIFICATIONS

The opinions in this opinion letter are subject to the following qualifications, provisos and further elaboration:

4.1 General

4.1.1 When reference is made to a Party being "entitled to receive or obliged to pay" a net sum in respect of the FOA Netting Provisions or the Clearing Module Netting Provisions, including in respect of the Cleared Transaction Sets, we note that such net sum may be subject to the exercise of rights of set-off of the other Party (or its Insolvency Representative) that arise by operation of law. As explained in paragraph 3.7.1 under the heading *Set-off of Cash Margin Cash Balance Owed by Defaulting Party or Non-Defaulting Party*, rights of set-off (legal and judicial compensation in Quebec) may arise by operation of law in certain circumstances, such as under the BIA by a Party's trustee-in-bankruptcy. Therefore, for example, once amounts owing under the Cleared Transaction Set are determined, an Insolvency Representative of the Defaulting Party, such as a trustee-in-bankruptcy under the BIA, might have the right to set-off against each other, all mutual obligations between the Defaulting Party and the Non-Defaulting Party (including in respect of another Cleared Transaction Set) that fulfilled the criteria for legal or judicial set-off. Legal set-off applies where the amounts owing are certain, mutual and liquidated, and judicial set-off may be stated by the court in respect of mutual claims

that are potentially unliquidated at that time. Such set-off in insolvency only applies where the amounts being set-off are "mutual" between the parties. In this context, "mutual" means that the Parties are each personally and solely liable as regards obligations owing by it to the other Party and solely entitled to the benefit of obligations owed to it by the other Party. Circumstances in which the requisite mutuality will not be established include, without limitation, where a Party is acting as agent for another person, where a Party is acting as a trustee, where a Party has a joint interest (other than where a Party is a partnership organised under the laws of this jurisdiction and then only in relation to the position between the partnership and the other Party to the FOA Netting Agreement or, as the case may be, the Clearing Agreement), or where a Party's rights or obligations or any interest therein have been assigned, charged or transferred (whether in whole or in part) whether unilaterally, by agreement or by operation of law or by order. An advance waiver of such rights of set-off by a Party may not bind the Party's Insolvency Representative.

4.1.2 If the effect of proceedings in a forum outside this jurisdiction is to extinguish claims or liabilities under the governing law of those claims or liabilities, Canadian courts may recognise the extinction of those claims or liabilities. In particular, in relation to any Transaction or Client Transaction which is governed by a law other than the law of this jurisdiction, such proceedings may affect whether or not that Transaction or Client Transaction is available for inclusion in any netting or set-off pursuant to a FOA Netting Agreement or a Clearing Agreement.

4.2 General Insolvency issues

4.2.1 Canadian courts having jurisdiction in relation to insolvency law in this jurisdiction may give assistance to courts in which concurrent insolvency proceedings have commenced under the laws of another jurisdiction. Such assistance may take the form of, for example, dealing with only those assets located in this jurisdiction or selectively applying provisions of foreign law in Insolvency Proceedings which are otherwise generally governed by English law. The courts of this jurisdiction may accordingly apply foreign systems of law rather than English law where the insolvent Party is subject to insolvency proceedings in another jurisdiction. Under section 284 of the BIA, the court may, on the application of a foreign representative or any other interested person, apply any legal or equitable rules governing the

recognition of foreign insolvency orders and assistance to foreign representatives that are not inconsistent with the provisions of the Insolvency Statutes (see paragraph 3.15 for more detail).

4.2.2 Under applicable law, the Rule Set or the commercial arrangements between the parties, an amount may be paid directly to a person who is a "Client" by a central counterparty, notwithstanding that that amount, or a sum calculated so as to take account of that amount, is owed to the Client by the Defaulting Party ("**leap-frogging arrangements**"). We express no view as to the impact which such a payment may have on the effectiveness of the Clearing Module Set-Off Provision or Addendum Set-Off Provision or the Title Transfer Provisions to the extent that the amount so paid directly by the central counterparty to the Client corresponds to an amount owing by the Firm to the Client under the Clearing Agreement. The effectiveness of such provisions will depend on the recognition and enforceability of such leap-frogging arrangements, which in turn may depend on whether the CCP is a designated clearing and settlement system under the PCSA to the extent the laws of this jurisdiction apply.

4.2.3 Under applicable law, the Rule Set or the commercial arrangements between the parties, transactions between a Firm or Clearing Member and a central counterparty may be transferred, assigned or otherwise ported to an alternative Firm or Clearing Member (together with related margin) in the event of a Firm Trigger Event ("**porting arrangements**") and in such a case such ported Transactions and margin are deemed to zero value for the insolvent Firm or Clearing Member. The enforceability of the provisions of the FOA Netting and Clearing Agreements may be affected by porting arrangements (thus deeming the Transactions which are being ported have zero value for the insolvent Firm or Clearing Member) and any resulting unenforceability of such provisions could affect the net sums due under the FOA Netting Provisions, the Clearing Module Set-Off Provision or Addendum Set-Off Provision. The effectiveness of such arrangements will depend on the recognition and enforceability of such porting arrangements as against the Firm or Clearing Member and its Insolvency Representative, which in turn may depend on whether the CCP is a designated clearing and settlement system under the PCSA to the extent that the laws of this jurisdiction apply.

4.2.4 An arrangement proceeding, such as a CCAA Plan of Arrangement, BIA Proposal or Corporate Plan of Arrangement, could affect both set-

off rights of creditors and the value of claims which the creditors may have against the insolvent Party. If the Termination Date or Cleared Set Termination Date has occurred before the approval of such an arrangement, any provision of such an arrangement which purports to unwind the application of the FOA Netting Provisions, the FOA Set-off Provisions, the Clearing Module Netting Provision, the Clearing Module Set-Off Provision, the Addendum Netting Provision, the Addendum Set-Off Provision or the Title Transfer Provisions would not bind the affected creditor if timely objection to the arrangement is made to the applicable court. An arrangement could, however, affect the value of any resulting net claim.

4.2.5 Where an Investment Firm/Broker Dealer is acting as a Firm or Clearing Member with respect to Client Transactions, certain provisions of the BIA may affect the rights of set-off of a Client with respect to the return of excess margin. Cash margin posted by Clients would be part of the customer pool of assets against which all customers of the bankrupt Firm or Clearing Member can make their net claims. Section 262(1.1) of the BIA provides that, with respect to that cash margin, a person, such as the Client, "shall share" in the "distribution of the customer pool fund as if it were a customer of the firm with a claim for net equity equal to the net value of the property that would have been returnable to the person after deducting any amount owing by the person under the contract." Our interpretation of this section is that the Client can net and apply the value of the cash margin to what it owes under the netting mechanics of the agreement, but if anything is owed to the Client with respect to excess margin value, it has a claim against the customer pool fund for that amount. What is limiting is that it may not allow set off by the Client of indebtedness it has to the Firm or Clearing Member unless that indebtedness arises under the particular agreement under which the margin was provided.

4.2.6 If costs, losses and gains included in the calculation of a Liquidation Amount or a Cleared Set Termination Amount are not provable or reasonable, they may be challenged by an Insolvency Representative.

4.3 Fraudulent Transfers, Preferences and Transfers at an Undervalue

4.3.1 Transactions or obligations entered into after Insolvency Proceedings have been commenced in relation to a Party might not be capable of inclusion in the net calculation carried out under the FOA Netting

Provisions, the FOA Set-Off Provisions, the Clearing Module Netting Provision, the Clearing Module Set-Off Provision, the Addendum Netting Provision, the Addendum Set-Off Provision or the Title Transfer Provisions, but this would not impair the effectiveness of the FOA Netting Provisions, the FOA Set-Off Provisions, the Clearing Module Netting Provision, the Clearing Module Set-Off Provision, the Addendum Netting Provision, the Addendum Set-Off Provision or the Title Transfer Provisions in respect of Transactions or, as the case may be, Client Transactions entered into before the commencement of such Insolvency Proceedings.

4.3.2 We are not opining on whether transfers of margin after, or Transactions or obligations entered into after, Insolvency Proceedings have been commenced in relation to a Party, when a Party is insolvent or near insolvent or which would render a Party insolvent or near insolvent would be capable of inclusion in the net calculation carried out under the FOA Netting Provisions, the FOA Set-Off Provisions, the Clearing Module Netting Provision, the Clearing Module Set-Off Provision, the Addendum Netting Provision, the Addendum Set-Off Provision or the Title Transfer Provisions. Such Transactions or transfers of margin might be subject to being voided under legislation in respect of credit preferences, fraudulent transfers or transactions at an undervalue. These laws are summarized in the following paragraphs.

4.3.3 The federal laws applicable in Quebec are the preference provisions in the BIA (which are incorporated by reference into the CCAA and which apply in either a BIA bankruptcy or BIA proposal proceeding) and those in the WURA. The BIA, CCAA and the WURA apply to the Parties as set out in Annex 6. Under these federal statutes, there are suspect periods during which transactions or transfers of property (which would include transfers of margin) by an insolvent party can be overturned if it has the effect of preferring a creditor of the insolvent party. The preference periods relate to transfers after commencement of a proceeding and in a specified period prior to commencement of the proceeding. The relevant provisions under the BIA and WURA are described more fully below. There are also applicable provincial laws, but they are less frequently invoked. The Quebec provincial laws are the Paulian action provisions of the Civil Code discussed below.

4.3.4 That a transfer of margin during a suspect period is made pursuant to a binding agreement entered into prior to the suspect period may be

evidence that there was no preferential intent but it is not determinative. In most cases, if the transfer is made by the defaulting Party with the genuine intent to try to avoid bankruptcy and to remain in business, then any presumption that the transfer prefers the other Party can be rebutted.

BIA

Section 95 of the BIA allows a trustee to move to set aside a transfer of Margin or Transactions to an arm's length person if it showed that:

- the transfer to the non-defaulting Party was a transfer of property, a charge on property, or a payment made,
- the non-defaulting Party was a "creditor" at the time of the conveyance or transfer,
- the transferring Party was insolvent at the time of the transfer,
- the transfer was made with the intent of preferring the non-defaulting Party over the transferring Party's other creditors, and
- the transfer, charge or payment took place within three months of the commencement of the transferring Party's bankruptcy.

Until recently, the trustee would not have had to prove that the debtor intended to prefer a secured party, but only that the transfer, charge or payment had the effect of preferring a secured party. The onus would then shift to the secured party to prove that the debtor did not intend to prefer it. This shift in onus or "presumption" was repealed with respect to a transfer made in connection with "financial collateral" and in accordance with the provisions of eligible financial contracts. Consequently, the trustee must now prove intent to prefer.

If the Parties are not at arm's length, then section 95 operates slightly differently. Usually it is not necessary to prove intent in such a case, only that the transfer, charge or payment has the effect of preferring the creditor. The suspect period is 12 months before the date of the initial bankruptcy event. However, the Parties are deemed to be dealing with each other at arm's length in respect of a transfer, charge or payment made in connection with financial collateral and in

accordance with the provisions of an eligible financial contract. In other words, the law with respect to non-arm's length transfers of financial collateral for an eligible financial contract is the same as for arm's length transfers except that the suspect period is 12 months.

If the trustee did prove each of the elements set out above, any such transfer would be void. If there is no presumption operating, the trustee may have difficulty proving intent to prefer, however. Canadian cases generally have taken the position that an agreement to grant security in future upon request is not in and of itself preferential. The fact that the margin is provided pursuant to an agreement that pre-dates the transferring Party's insolvency and particularly the three-month suspect period, will be considered evidence, possibly determinative evidence, that the transferring Party did not have the requisite intent to prefer the other Party. There is case law, however, where a pre-existing contractual obligation to post the security has not, in and of itself, rebutted the presumption. Also, if the transferring Party is insolvent at the time it enters into the agreement, then the other Party might not be able to rely on the fact of this pre-existing contract to disprove intent. In any event, other evidence may be relevant to intent. For example, the transferring Party may have valid reasons to transfer the margin to the other Party in preference to its other creditors. Delay in the transfer of margin to the other Party might have devastating financial effects, in that it would constitute an event of default under the agreement and, consequently, an acceleration of its obligations. Non-payment of other creditors may not be as disadvantageous. The transferring Party might honestly and reasonably believe that by transferring the margin it buys time necessary to allow it to carry on in business. In such a case, the trustee would not likely be able to prove the requisite intent as long as the transferring Party's hope that the business would recover was both bona fide and reasonable.

WURA

The WURA contains fraudulent conveyance and preference provisions that differ from those under the BIA and the provincial statutes. Because the WURA applies to limited types of entities and, consequently, liquidations are far less common than bankruptcies, the jurisprudence is not very well developed. Although the form of the

provisions are different from those in the BIA, in substance most of them operate in much the same way and are intended to effect the same result. Therefore, the following analysis relies on the case law considering the analogous provisions in these other statutes.

The WURA contains two sets of provisions with potential application to the FOA Netting and Clearing Agreements. These are:

- the unjust preference provisions, and
- the payments within 30 days of winding-up provision.

Unjust Preferences

Section 100 of the WURA voids any deposit, transfer or payment to a creditor "in contemplation of insolvency" that has the effect of giving the creditor an "unjust preference". Normally, any deposit, transfer or payment made within 30 days of the appointment of the liquidator is deemed to have been made in contemplation of insolvency. A recent amendment, however, provides that this presumption does not apply to a sale, deposit, pledge or transfer of "financial collateral" made in accordance with the provisions of an "eligible financial contract." This means that the liquidator would have to prove the transfer of collateral was made with the intention to provide the secured party an unjust preference, the same proof it would have to adduce if the transfers were more than 30 days prior to the proceeding. Although the wording is quite different, the intent of this provision is similar to the unjust preference provisions in Section 95 of the BIA. However, unlike the BIA, it is not just transfers and transactions that take place within the suspect period (i.e. three months) that are subject to being set aside; any transaction made with the requisite intent and effect can be set aside.

Transfers of margin pursuant to a typical agreement such as the FOA Netting Agreement and the Clearing Agreement are transfers of property and so are subject to the preference analysis. The meaning of the term "unjust" in this context is unclear. However, there is some early case law suggesting that it means only that the transfer or payment interferes with the rateable distribution of the insolvent company's assets. Therefore, there is a risk that a court would view the transfers of Margin or Transactions under an agreement such as the

FOA Netting Agreement and the Clearing Agreement as having the effect of unjustly preferring the non-defaulting Party.

The meaning of the phrase "in contemplation of insolvency" is also unclear. However, by analogy to the BIA preference provision, it likely means that the transfer or payment is made at a time when the transferring Party is either insolvent or very nearly insolvent with the intention of giving the creditor a preferred position over other creditors. Any transfers or payments made within 30 days of the commencement of liquidation would be deemed to be made with this intent (unless they were transfers or payments with respect to financial collateral for an eligible financial contract).

A non-defaulting Party would have to bring forth evidence to generally meet the liquidator's case with respect to the transferring Party's intent. It will always be essential to demonstrate that in making any transfer at a time when it is insolvent, the transferring Party had a reasonable and bona fide belief that by doing so it would be able to carry on in business and the fact that a failure to deliver Margin is an Event of Default entitling the non-defaulting Party to terminate all Transactions will be of assistance in this regard. As with the BIA, the preferential intent might be disproved by evidence that the transfer was made pursuant to an agreement that pre-dated insolvency and the suspect period.

Payments within 30 Days of Winding-up

With respect to entities subject to the WURA, there is an additional provision, not found in the BIA or provincial legislation, which must be considered in relation to any transfers of money. Transfers of money made within 30 days of the commencement of liquidation can be set aside. Subsection 101(1) voids every "payment" made within 30 days of commencement of the liquidation by an insolvent company to a person who knows of the insolvency or who has reason to know of it. Intent in making the payment is not relevant under this provision. If, during this 30-day period, the non-defaulting Party had actual knowledge of the transferring Party's insolvent state or reason to question its solvency, then the payments made during this period might be set aside.

This provision does not apply, however, to a payment made in

connection with financial collateral in accordance with the provisions of an eligible financial contract.

Therefore, notwithstanding these limitations, because the FOA Netting Agreement or, as the case may be, the Clearing Agreement constitutes an eligible financial contract, a transfer of margin made in accordance with the provisions of the agreement will not be voidable unless the Insolvency Representative proves that the transferring Party transferred the margin with a view to giving the transferee Party a preference (the presumption of such a preference not operating in such cases).

Paulian action

The provincial Paulian action can apply to any Party type and can be enforced by creditors, a trustee in bankruptcy, a receiver or a liquidator. Articles 1631 to 1636 of the Civil Code set out when a creditor can challenge a "juridical act" (which term would include, inter alia, both (i) a contract and (ii) a payment made for the performance of a contract) made by a party who is insolvent or on the brink of insolvency.

The trustee or creditor challenging the transaction must prove that the act was done "in fraud of his rights" and that the effect of the transaction was (i) to grant a preference to another creditor when the debtor was insolvent or (ii) to render the debtor insolvent. For preferential transactions, the Paulian action does not require proof of actual fraudulent intent but generally it must be proved that the preferential transfer was made when the transferee was insolvent. For juridical acts such as transfers of property, there is a presumption that a transfer made by an insolvent party or which renders a party insolvent is "in fraud of" another creditor's rights if the transferee knows of the transferring party's insolvency or pending insolvency. It is likely, however, possible to rebut the presumption of fraud upon proof of the good faith of the transferee and that the transfer was made in the interests of the debtor in that it permitted it to carry on business. However, there is a risk that, under the Paulian action provisions, a transfer of margin made by an insolvent Party or one on the verge of insolvency, particularly to the extent it relates to a pre-existing transaction, could be set aside as a creditor preference or fraudulent transfer even if it is made pursuant to a binding security agreement

entered into prior to the insolvency. While the sanction in a Paulian action is not the nullity of the juridical act but that the act is declared "inopposable", that is, of no effect, vis-à-vis the attacking creditor, the effect is the same. The act is also inopposable to any creditor who could have taken a Paulian action and the property involved or payment may be seized and sold, or paid to the creditors.

Under the Paulian action provisions, there is no true preference period. Article 1635 of the Civil Code provides that a Paulian action must be brought within one year of the appointment of the trustee in bankruptcy where the action is brought by a trustee. If a creditor challenges the transaction, it must be brought within one year of his learning of the prejudice resulting from the act which is being attacked or the fraudulent nature of the act. It is not clear whether the action will also be subject to the general prescription period of three years for all personal actions which is set out at Article 2925 of the Civil Code. There is some jurisprudence in Quebec suggesting an action may be brought more than three years after the date of the transaction being attacked and that the three year period would not start to run until the creditor had knowledge of the fraudulent or prejudicial nature of the transaction.

Transfer at undervalue

The BIA and CCAA also contain a provision respecting transfers at an undervalue. Under the BIA provision, a "transfer at undervalue" is void as against or may not be set up against the trustee. In addition, any person that is a party to the transaction or is a privy of a party to the transaction may be ordered to make compensatory payments to the estate if the transaction is found to be a transaction at an undervalue. A "transfer at undervalue" is defined in the BIA as:

> a disposition of property or provision of services for which no consideration is received by the debtor or for which the consideration received by the debtor is conspicuously less than the fair market value of the consideration given by the debtor;

Where the debtor and the party to the transaction are dealing at arm's length, the trustee must prove that (i) the transfer occurred during the

period that begins on the day that is one year before the date of the initial bankruptcy event (e.g. the date of the assignment, the filing of a notice to make a proposal etc.) and that ends on the date of the bankruptcy, (ii) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, and (iii) the debtor intended to defraud, defeat or delay a creditor. Where proved the transfer is void and the transferee may be ordered to pay the difference between the value of the consideration the given or received by the debtor and the fair market value of the property or services given or received by the debtor.

Transactions or, as the case may be, Client Transactions entered into on arm's length terms and at the then prevailing market rates are unlikely to constitute transactions at an undervalue. In relation to a Transfer of margin under the Title Transfer Provisions, it is theoretically possible that a collateral arrangement such as that constituted under the Title Transfer Provisions could constitute a transaction at an undervalue; however, the provision of margin on an arms-length basis would not normally result in the over-provision of consideration by the Margin provider as compared to consideration received by it. However, whether the requisite intent is present in any particular case is a matter of fact.

4.4 Choice of Law

4.4.1 The opinion in paragraph 3.2.2 (*Choice of Law*) is subject to the proviso that:

(a) this choice of law is *bona fide* (in the sense that it was not made solely with a view to avoiding the consequences of the law of any other jurisdiction); and

(b) this choice of law is not contrary to public order, as that term is understood under the laws of the Province of Quebec.

If there is a valid business reason for choosing a particular jurisdiction (such as one of the parties is present in the jurisdiction or, as in this case, the agreement is a standard industry form of contract drafted with the laws of the chosen jurisdiction in mind) it will likely be considered a *bona fide* and valid choice and not contrary to public order.

4.4.2 The opinion in paragraph 3.2.2 (*Choice of Law*) is subject to the

qualification that in any proceedings undertaken in courts of competent jurisdiction in the Province of Quebec to enforce and interpret the FOA Netting Agreement or the Clearing Agreement, only with respect to issues that would be characterized by courts in Quebec as contract law issues, the courts would, upon appropriate evidence of the laws of England being adduced, enforce the Agreement in accordance with those laws. Exceptions to the application of those laws are that courts in the Province of Quebec:

(a) will apply Quebec procedural laws and will not apply procedural laws of England,

(b) may not enforce an obligation enforceable under the laws of England if performance of the obligation would be illegal under the law of the place where the obligation is to be performed or which constitutes the direct or indirect enforcement of a foreign revenue (tax), penal or expropriation law,

(c) will not apply provisions of the foreign law if the application would be manifestly inconsistent with public order as understood in international relations, and

(d) will apply the rules of evidence of the jurisdiction whose laws are applicable to the merits of the dispute but will apply the rules of evidence of Quebec where those rules are more favourable to the establishment of evidence.

(e) Canadian insolvency laws will determine the ability of a Party to enforce the FOA Netting Provision and the FOA Set-Off Provision or, as the case may be, the Clearing Module Netting Provision and/or the Addendum Netting Provision and the Clearing Module Set-Off Provision and/or the Addendum Set-Off Provision in an Insolvency Proceeding and may affect the enforceability of certain provisions (as described above in response to specific questions).

4.5 Enforceability of the FOA Netting Provision, the Clearing Module Netting Provision and the Addendum Netting Provision

4.5.1 Our opinions in paragraphs 3.3 (*Enforceability of FOA Netting Provision*), 3.4 (*Enforceability of the Clearing Module Netting Provision*) and 3.5 (*Enforceability of the Addendum Netting Provision*) rely on

characterization of the Transactions as EFCs and requires that it meet the criteria set out in Annex 8. In particular, a physical commodity transaction that does not allocate price risk may not be an EFC, unless it is a future or option on a future that trades on an exchange or other regulated trading systems.

4.5.2 Our opinions in paragraphs 3.3 (*Enforceability of FOA Netting Provision*), 3.4 (*Enforceability of the Clearing Module Netting Provision*) and 3.5 (*Enforceability of the Addendum Netting Provision*) with respect to Receivership is subject to the qualification that there is a risk of a court order in an Quebec receivership preventing the enforcement of the FOA Netting Provision, the Clearing Module Netting Provision or the Addendum Netting Provision, as applicable, because there is no statutory safe-harbour. We believe, however, that the risk is minimal with respect to Transactions that are EFCs as current practice in Quebec is to exclude EFCs from such orders. We would expect that, at most, there might be a period of delay until the court can hear and determine the Non-Defaulting Party's motion to exclude it from the general stay that might be granted by the order in the event such an exception was not included.

4.5.3 Our opinions in paragraphs 3.3 (*Enforceability of FOA Netting Provision*), 3.4 (*Enforceability of the Clearing Module Netting Provision*) and 3.5 (*Enforceability of the Addendum Netting Provision*) with respect to Corporate Plans of Arrangement is subject to the qualification that there is a risk of a court order preventing enforcement of the FOA Netting Provisions, the Clearing Module Netting Provision or the Addendum Netting Provision, as applicable, because there is no statutory safe-harbour. There is some case support for the position that a stay should not be granted (*RE Enron Canada*[23]). While we know of one proceeding where the court did take the unprecedented step of staying the termination of contracts with the applicant companies with no exception for EFCs (*In re Abitibi*). The *Enron Canada* case, in which such an order was refused, was not before the court. The proceeding was made in the context of a proposal to restructure, through a series of relatively complicated corporate steps, the outstanding bonds and term loans of the company. The Quebec Superior Court in its reasons associated with the order does not deal with EFCs except to note that the orders requested "exclude from their application swap or

[23] *Re Enron Canada* (2001), 31 C.B.R. (4th) 15 (Alta. Q.B.).

derivative transactions or eligible financial contracts". However, the order itself did not exclude all EFCs from the stay. It only excluded EFCs with persons "other than the Abitibi parties". The intention here was seemingly to not interfere with the operation of credit default transactions having Abitibi as a reference entity or other EFCs between third parties where termination may have been triggered by an Abitibi default. The very fact that the Abitibi order was made raises an issue for the exercise of termination rights under EFCs. It is important to note, however, that the court did not hear arguments from any affected parties regarding the application of the order to EFCs and it was not the focus of the company's submissions to the court. The Enron Canada decision also was not before the court. Nor was the order subsequently challenged by any party to an EFC. The order became moot when Abitibi filed under the CCAA, it having become apparent that the corporate plan would not succeed. Given the circumstances, the precedential value of the order on this issue is not as great as that of the Enron Canada case.

If, as this case suggests, the courts will allow the Corporate Plan proceeding to be used by an insolvent corporation as an alternative to a CCAA proceeding to deal not only with bondholder claims but also claims of ordinary creditors such as term lenders, then it makes sense to treat the commencement of such a proceeding, at least where creditors' claims are involved, in the same way as other bankruptcy events of default. The standard form wording of the "Event of Default" in certain of the agreements based on the terms specified in Annex 1 appears to cover a Corporate Plan of Arrangement in terms of clarifying that a similar law includes a corporate law (e.g., 10.1(b) of the Professional Agreement). An FOA Netting Agreement or a Clearing Agreement without this additional wording may not include a trigger that would apply to a Corporate Plan of Arrangement (e.g. Eligible Counterparty Agreements, Short One-Way Clauses and Short Two-Way Clauses).

4.5.4 We believe that upon the commencement of an Insolvency Proceeding, the Non-Defaulting Party should exercise its rights as soon as reasonably possible to avoid any argument on the part of the Insolvency Representative that the Non-Defaulting Party is awaiting favourable market conditions at the expense of the Defaulting Party.

4.5.5 The ability to make a claim for interest accruing due after the

commencement of an Insolvency Proceeding may be precluded or limited.

4.5.6 Each of the FOA Netting Agreement and the Clearing Agreement provides for the Liquidation Amount or the Cleared Set Termination Amount to be converted to and paid in a Base Currency or in the same currency as the termination amount payable by the Firm (or Clearing Member) or the relevant Agreed CCP, as applicable. Some Canadian insolvency statutes expressly deal with the treatment of foreign currency claims upon an insolvency, whilst others do not. Even where the relevant insolvency statutes do not expressly say so, it is accepted that a foreign currency claimant would have to submit its claim to the Insolvency Representative valued in Canadian dollars. In more detail:

(a) Under the bankruptcy provisions of the BIA, the general principle is that a creditor is to value its claim as of the date of the bankruptcy, which is the date of the petition into bankruptcy.[24] Accordingly, the Liquidation Amount or the Cleared Set Termination Agreement must be converted to Canadian funds using a conversion rate applicable on that date. The BIA does not specify a method of conversion. The trustee in bankruptcy might accept the Non-Defaulting Party's choice of the source for the conversion rate, so long as it is a generally accepted rate (for example, the rate quoted by the Bank of Canada or a Canadian incorporated bank (i.e. listed in Schedule 1 of the *Bank Act* (Canada)), although it is more likely that the trustee will establish a rate for all creditors with claims in a particular currency based on a particular published source.

(b) With respect to BIA Proposals, claims are to be converted as of

(A) the date of filing the notice of intention to file a proposal (or the proposal itself if no notice is filed), or

(B) the date of bankruptcy where the proposal is filed by an entity that is already bankrupt, or

(C) the date specified in the proposal.

(c) The CCAA includes similar provisions to BIA Proposals.

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[24] BIA, s.275.

(d) With respect to the WURA and Receivership there is no method of conversion specified in the legislation, but the Insolvency Representative could establish an acceptable rate for all creditors with claims in a particular foreign currency for converting the Liquidation Amount or the Cleared Set Termination Amount to Canadian currency.

(e) None of the statutory provisions or established practices apply to converting individual Transactions to a Base Currency (or other applicable currency) as part of the netting process and we do not expect that an Insolvency Representative would interfere with the contract provisions in this regard.

4.5.7 Provisions requiring "topping-up" of any amount to account for subsequent foreign currency losses attributable to fluctuations after the opening of an Insolvency Proceeding may not be enforceable, on the basis that they infringe the *pari passu* distribution principle.

4.5.8 Where no specific Insolvency Proceeding has been commenced and the Non-Defaulting Party is seeking payment of the Liquidation Amount or the Cleared Set Termination Amount in court proceedings, there are other specific rules that come into play. The *Currency Act* (Canada)[25] provides that any reference to money or monetary value in any legal proceeding shall be stated in Canadian currency. This does not mean, however, that a party to an agreement providing for the payment of money in a foreign currency must convert the foreign currency to Canadian currency in its claim. In Quebec, a court will not give a judgment denominated in a currency other than Canadian dollars. When a claim in respect of an obligation is in foreign currency, the courts will generally convert the foreign currency into Canadian currency for the purposes of the judgment on the date chosen by the plaintiff between the date of the breach and the date of the judgment as long as there has been no negligence or inaction by the plaintiff which has prejudiced the defendant. In addition, a court would probably give effect to any express contractual provision which stipulates a date of conversion into Canadian currency at a specific date, provided the plaintiff's negligence or inaction does not make the application of such a clause "abusive". Subject to these provisions, we conclude that, as a practical matter, the payment of the Liquidation

[25] R.S.C. 1985, c.C-52, s.12.

Amount or the Cleared Set Termination Amount in the applicable currency contemplated by the FOA Netting Agreement or the Clearing Agreement, as the case may be, is enforceable in proceedings brought in Quebec.

4.5.9 For purposes of calculating the value of any Transferred Margin or Commodity Securities which are not Acceptable Margin, assigning a value of zero would likely in the context of an Insolvency Proceeding, offend the anti-forfeiture principle. Any value attributed to Transferred Margin on realization must be a fair market value.

4.5.10 As has been described above, transfers of margin, whether by way of title transfer or otherwise, and payments under agreements are subject to fraudulent and credit preferences laws and provisions relating to transfers at an undervalue that may in certain circumstances allow the conveyor or its Insolvency Representative to claw-back the transfer or payment.

There are no other material issues relevant to the issues addressed in this opinion which we wish to draw to your attention.

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This opinion is given for the sole benefit of the Futures and Options Association and such of its members (excluding associate members) as subscribe to the Futures and Options Association's opinions library (and whose terms of subscription gives them access to this opinion). This opinion may not be relied upon by any other person unless we otherwise specifically agree with that person in writing, although we consent to its being shown to such Futures and Options Association members' affiliates (being members of such persons' groups, as defined by the UK Financial Services and Markets Act 2000) and to any competent authority supervising such member firms and their affiliates in connection with their compliance with their obligations under prudential regulation.

Yours faithfully,

ST. Kinman Ellis LLP

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 1
Financial Institutions

Subject to the modifications and additions set out in this Schedule 1 (*Financial Institutions*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties (acting as Client, Firm or Clearing Member) which are Financial Institutions. "***Financial Institution***" means a bank incorporated under the *Bank Act* (Canada), a corporation incorporated as a trust company under the *Trust and Loan Companies Act* (Canada) or a cooperative credit association under the *Cooperative Credit Associations Act* (Canada). This Schedule also covers non-Canadian banks authorized to do business in Canada with respect to a branch or branches in Canada.

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 1 (Financial Institutions);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Financial Institutions (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Financial Institution could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Proceedings under the *Winding-up and Restructuring Act* (Canada) ("**WURA**") for either (i) liquidation or (ii) reorganization/ arrangement with creditors ("**WURA Proceedings**");

3.1.2 Proceedings under the CDIC Act for reorganization or liquidation of federal deposit taking institutions, such as banks ("**CDIC Proceedings**") if the entity is insured by CDIC; and

We confirm that these Insolvency Proceedings are adequately covered by the

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Event of Default.

- **Recognition of Choice of Law (paragraph 3.2)**

The analysis is the same as in the main body of the opinion.

- **Enforceability of the FOA Netting Provision (paragraph 3.3), the Clearing Module Netting Provision (paragraph 3.4) and the Addendum Netting Provision (paragraph 3.5)**

The analysis in the main body of the opinion applies, except as modified below.

There are rules of law in this jurisdiction which could impose a moratorium or stay which would prevent, delay or otherwise affect the exercise of such rights by the Non-Defaulting Party, but in many cases an exemption from the moratorium or stay will apply. In summary,

- In WURA and CDIC Act proceedings there are automatic or court ordered stays that prevent the exercise of termination rights and delay or otherwise interfere with rights of set-off, but statutory exemptions for Transactions that are EFCs are available under these Insolvency Statutes (e.g. WURA, CDIC Act).
- Where no other exemption is available or to provide certainty in those proceedings without an express exemption, the PCSA may apply to provide an exemption for EFCs and other netted transactions if the parties are both "financial institutions" or if the agreement is between a participant in a clearing system and its customer (please see "*Application of PCSA*" in paragraph 3.4).
- If the Transactions are not EFCs and the PCSA does not apply, then the right to terminate and accelerate obligations under those Transactions may be stayed and this will affect the ability to calculate a Liquidation Amount in a Cleared Set Termination Amount with respect to such Transactions.
- There are certain situations in which the exercise of the FOA Netting Provision, the Clearing Module Netting Provision and the Addendum Netting Provision may be stayed, even with respect to EFCs and where the PCSA applies, with respect to Financial Institutions that are Canadian deposit taking institutions (e.g. CDIC bridge institution provisions apply).
- There is an automatic stay of proceedings that would prevent the commencement of any court or other proceedings to enforce payment of the Liquidation Amount in a Cleared Set Termination Amount.

The WURA analysis in the main opinion will apply equally to Financial Institutions. Financial Institutions are "financial institutions" for purposes of the PCSA. The analysis which is different relates to Financial Institutions which are CDIC insured deposit taking institutions. In more detail, the analysis with respect to such Financial Institutions with respect to the CDIC Act Proceedings is as follows:

CDIC Act. Prior to the involvement of the Canada Deposit Insurance Corporation ("**CDIC**") in the restructuring or liquidation of a federal deposit taking institution such as a bank, the Superintendent of Financial Institutions may take control of the institution's assets.[26] After taking control, the Superintendent might also, as a further step, take over the management of the business and affairs of the institution.[27] The Superintendent is not given any extraordinary powers that could, in our view, allow him to alter the contractual arrangements of the Financial Institution.

In certain circumstances, CDIC can obtain an order vesting the shares and subordinated debt of such institutions in it in order to attempt a sale of the institution, an amalgamation or any other transaction to restructure a substantial part of the institution's business.[28] Where CDIC obtains the vesting order, the CDIC Act[29] imposes a number of different limitations on the rights that can be exercised against the institution, including that no person may terminate or amend any agreement with the institution or claim an accelerated payment only because of (i) the institution's insolvency, (ii) the making of the order, or (iii) a default before the order was made in any performance of obligations under the agreement.[30] It also prevents the exercise of any right of set-off.

However, subject to exceptions with respect to the bridge institution regime,

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26 The statutory authority for the Superintendent's intervention depends upon the type of entity involved. The *Bank Act* (Canada) ("**Bank Act**"), S.C. 1991, c.46, s.538 confers the authority with respect to banks. The *Trust and Loan Companies Act* (Canada), S.C. 1991, c.45, s.510 confers the authority with respect to federal trust or loan companies.

27 Bank Act, s.538; Trust and Loan Companies Act, s.514.

28 CDIC Act, s.39.19.

29 CDIC Act, s.39.15.

30 CDIC Act, s.39.15(1)(d). Note that the CDIC Act differs from section 65.1(1) of the BIA in that under the CDIC Act a prior default, such as a payment default, cannot provide grounds for termination once an order is made, whereas under the BIA the pre-proceeding defaults can be relied on. The Governor in Council (essentially the federal cabinet), in making the order, has the power to provide that these provisions do not apply to the institution, but no such order has been made (s.39.15(1)).

the CDIC Act provides that these provisions do not prevent termination in accordance with their terms of or exercise of netting rights under EFCs. Any Transaction listed on Annex 2, part A (i) to (iv) and specifically listed on Annex 2, part E is in our view an EFC subject to meeting the general criteria relevant to all Transaction types (discussed in following paragraphs). Transactions listed on Annex 2, parts (B), (C) and (D) and part A(v) may be EFCs if they are of a type listed in the definition above and they meet general criteria relevant to all Transaction types. The Agreement would, to the extent of the FOA Netting Provision, the Clearing Module Netting Provision or the Addendum Netting Provision and this application to Transactions, also be characterized as an EFC. The definition of EFC and criteria for being an EFC are set out at Annex 8.

There is an automatic temporary (one business day) stay on termination and consequently on set-off under EFCs in a CDIC Act receivership proceeding where an order is made to incorporate a bridge institution. There is also the possibility of a permanent stay if the Transactions are transferred to the new bridge institution or CDIC guarantees payment of this obligations under the Transactions. This is discussed in greater detail in the qualifications below.

Overriding Effect of the Payment Clearing and Settlement Act. The PCSA expressly recognizes (in section 13) a right to terminate and liquidate pursuant to a "netting agreement". The netting agreement must be "between financial institutions" or between a participant in a clearing system and its customer. This right applies notwithstanding anything in any law relating to bankruptcy or insolvency or any order of a court made pursuant to an administration of a reorganization, arrangement or receivership involving insolvency (e.g. Receivership or Corporate Plan if it involves insolvency). To the extent that it applies, section 13 is intended to override any court order made in the context of any Insolvency Proceeding. Given that the major Canadian insolvency statutes noted above all include express statutory protections for termination and netting rights, it will usually be necessary to rely on section 13 of the PCSA only with respect to transactions that are not EFCs and perhaps in those situations where there are no express protections (i.e. BIA bankruptcy[31], Receivership and Corporate Plans). The effectiveness of section 13 has not been tested before Canadian courts.

The keys to section 13 of the PCSA are the definitions of "financial institution", "netting agreement" and "participant".

[31] Although, as noted above, we do not believe there is a stay risk in a BIA bankruptcy notwithstanding the lack of express statutory protections.

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A "netting agreement" includes an agreement between two or more financial institutions (or a participant in a clearing system and its customer to the extent it relates to the cleared transactions or clearing obligations) that is either an EFC (as defined above) or an agreement that provides for netting or set-off of present or future obligations to make payments against present or future rights to receive payments. Even with respect to Transactions that are not EFCs, the FOA Netting Provision, the Clearing Module Netting Provision or the Addendum Netting Provision would each constitute a netting agreement as long as both parties were financial institutions. The Clearing Module Netting Provision and the Addendum Netting Provision would constitute a netting agreement by virtue of being a netting agreement between a participant (which means "a member of a clearing house[32] or a party to an arrangement that establishes a clearing and settlement system[33]") and its customer for clearing services.

"Financial institution" is broadly defined and includes Canadian (federal or provincial) or foreign:

(a) banks;

(b) trust or loan companies;

(c) insurance companies and fraternal benefit companies;

(d) co-operative credit associations; and

(e) securities dealers (including portfolio managers and investment counsellors).

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[32] This is defined in the PCSA as an "entity that provides clearing or settlement services for a clearing and settlement system".

[33] "[C]learing and settlement system" means a system or arrangement for the clearing or settlement of payment obligations or payment messages in which

(a) there are at least three participants, at least one of which is a Canadian participant and at least one of which has its head office in a jurisdiction other than the jurisdiction where the head office of the clearing house is located;

(b) clearing or settlement is all or partly in Canadian dollars; and

(c) except in the case of a system or arrangement for the clearing or settlement of derivatives contracts, the payment obligations that arise from clearing within the system or arrangement are ultimately settled through adjustments to the account or accounts of one or more of the participants at the Bank.

For greater certainty, it includes a system or arrangement for the clearing or settlement of securities transactions, derivatives contracts, foreign exchange transactions or other transactions if the system or arrangement also clears or settles payment obligations arising from those transactions.

It also includes non-Canadian entities that are otherwise engaged primarily in the business of providing financial services.

It does not include other Canadian financial services entities, but Canadian entities (federal or provincial) that are engaged primarily in the business of providing financial services might be brought within the scope of the definition of "financial institution," because the Governor in Council (i.e., the federal cabinet) is empowered to specify that a particular entity or a particular class of entity is a financial institution for the purpose of section 13. The only constraint on cabinet's power is that the entity or class be "primarily engaged in the business of providing financial services"[34].

- **Use of FOA Clearing Module or ISDA/FOA Clearing Addendum not Detrimental of the FOA Netting Provision (paragraph 3.6)**

The analysis is the same as in the main body of the opinion.

- **Enforceability of FOA Set-Off Provisions (paragraph 3.7), Set-Off under a Clearing Agreement with a Clearing Module Set-Off Provision (paragraph 3.8) and Set-Off under a Clearing Agreement with an Addendum Set-Off Provision (paragraph 3.9)**

With respect to WURA Proceedings, the analysis in the main body of the opinion applies expect with respect to Canadian Financial Institutions and Canadian branches of authorized foreign banks.

The PCSA also includes a safe-harbour for any dealings with financial collateral for an EFC. "Financial collateral" is currently defined as follows:

> financial collateral" means any of the following that is subject to an interest, or in the Province of Quebec a right, that secures payment or performance of an obligation in respect of an eligible financial contract or that is subject to a title transfer credit support agreement:
>
> (a) cash or cash equivalents, including negotiable instruments and demand deposits,
>
> (b) securities, a securities account, a securities entitlement or a right to acquire securities,
>
> (c) a futures agreement or a futures account,
>
> (d) an assignment of a right to payment or delivery against a clearing house, or

[34] Since foreign entities primarily engaged in the business of providing financial services are already in the list, in the statute this power would only be needed to designate Canadian entities.

(e) any other collateral that is prescribed[35].

The application of the PCSA is explained above.

The following chart summarizes the set-off enforceability with respect to Financial Institutions.

	Likelihood of Stay on Mutual Set-off of Accrued Claims[36]	Statutory Exemption Allowing Dealings with Financial Collateral for EFCs (i.e. Margin)
CDIC Act	Automatic stay	Yes, but subject to bridge institution exception where in CDIC Act receivership and bridge institution is incorporated
WURA	No stay likely as WURA recognizes rights of set-off. (s.73) If Client is a non-Canadian bank with Canadian branch, set-off protection applies only to transactions booked in the Canadian branch. (s.158)	Yes

- **Enforceability of the Title Transfer Provisions (paragraph 3.10)**

The analysis is the same as in the main body of the opinion in that there is a requirement to perfect the potential security interest to the extent Quebec law applies and that there are automatic stays that apply to dealing with margin, where the statutory exemptions for EFCs do not apply. In the case of a deposit taking institution insured by CDIC the safe-harbour is subject to the bridge bank exceptions discussed in our qualifications.

Margin Enforcement and
Insolvency Proceeding Stays and Exemptions

	Stay on Realization of Margin	Length of Stay on Realization of Credit Support (without statutory exemption)	Statutory Exemption Allowing Dealing Financial Collateral for Eligible Financial Contracts
WURA	Unlikely (but possible) for securities, cash or other margin with easily determined value	Up to 6 months (may be longer in restructuring proceedings)	Yes

[35] None have been prescribed as yet.

[36] Non-mutual set-off may not be enforceable in Insolvency Proceedings.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

	Stay on Realization of Margin	Length of Stay on Realization of Credit Support (without statutory exemption)	Statutory Exemption Allowing Dealing Financial Collateral for Eligible Financial Contracts
CDIC	Automatic stay on dealings with credit support	No limit; if proceeding is a liquidation, Superintendent may realize on secured party's behalf	Yes, but subject to bridge institution provisions in CDIC Act receivership
Receivership[37]	Unlikely (but possible) for securities, cash or other margin with easily determined value	No limit	No, but practice in Quebec follows the practice in CCAA and BIA so order will likely include an exemption; express exemption if PCSA applies

- **Multibranch Parties (paragraph 3.14)**

The analysis is the same as in the main body of the opinion except with respect to Canadian branches of foreign banks. Where the Insolvency Representative is liquidating a Canadian branch of a non-Canadian bank pursuant to the WURA, there is an issue with respect to the separate treatment of obligations. There is ring-fencing of Canadian assets in such proceedings.

4. ADDITIONAL QUALIFICATIONS

The following additional qualifications apply:

4.7.1 Where an order directing the incorporation of a bridge institution is made, there is (1) an automatic temporary stay that prevents reliance on the eligible financial contract safe-harbour and (2) the possibility of a permanent stay where the Agreement is assumed by a bridge institution or CDIC guarantees the payment obligations under the Agreement. These stays take precedence over the stay protections in the PCSA.[38] It is anticipated that an order incorporating a bridge institution would be made at or around the same time that the receivership order under the CDIC Act is made.

The Temporary Stay

The *Jobs and Growth Act, 2012* (Canada)[39] passed on December 14, 2012 amended the CDIC Act to provide for a new temporary stay in the

37 Unlikely proceeding for Financial Institutions, but included for completeness.

38 PCSA, s. 13(1.2).

39 S.C. 2012, c. 31.

event that an order is made directing the incorporation of a bridge institution.[40] The stay prevents reliance on the member institution's insolvency, the making of the order appointing CDIC as receiver, the making of the order directing incorporation of the bridge institution, or the assignment of the eligible financial contract to or assumption of it by the bridge institution as grounds for accelerating or terminating any eligible financial contract.[41] This stay lasts from the time the order directing incorporation of the bridge institution is made until 5:00 p.m. on the following business day[42] (Ottawa time). During this period presumably CDIC will determine whether or not the bridge institution will assume the eligible financial contracts. (This stay does not apply to an eligible financial contract between the federal member institution and a clearing house that provides clearing and settlement services for a clearing and settlement system designated under section 4 of the PCSA or a securities and derivatives clearing house as defined under subsection 13.1(3) of the PCSA.[43])

The Conditional Stay

After operation of the temporary stay, a conditional stay may become effective. The counterparty of the member institution cannot rely on the eligible financial contracts exemption if CDIC undertakes to either guarantee unconditionally the payment of any amount due or that may become due in accordance with the provisions of the contract by the member institution or ensure that all obligations arising from the contract will be assumed by the bridge institution. We refer to this as the conditional stay as it is conditional on CDIC making these undertakings. The relevant section reads as follows:

> 39.15 (7.1) If an order directing the incorporation of a bridge institution is made and the Corporation undertakes to unconditionally guarantee the payment of any

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40 CDIC Act, s.39.15(7.01).

41 There is an exemption for certain designated clearing and settlement systems or designated securities and derivatives clearing houses; CDIC Act, s.39.15(7.02).

42 A business day is a day other than Saturday, Sunday or a day on which the clearing and settlement systems operated by the Canadian Payments Association are closed; CDIC Act, s.39.15(7.03).

43 CDIC Act, s.39.15(7.02).

> amount due or that may become due by the federal member institution, in accordance with the provisions of the eligible financial contract, or to ensure that all obligations of the federal member institution arising from the eligible financial contract will be assumed by the bridge institution, the actions referred to in subsection (7) [*ed. termination, netting and dealing with financial collateral for an eligible financial contract*] are not to be taken by reason only of
>
> (a) the federal member institution's insolvency;
>
> (b) the making of an order or an order appointing the Corporation as receiver in respect of the federal member institution or the making of the order directing the incorporation of the bridge institution; or
>
> (c) the eligible financial contract being assigned to or assumed by the bridge institution.[44]

Until the CDIC undertakings referred to in the provision are made there is no impediment to relying on the eligible financial contracts exemption. The provision prevents reliance on the exemption only if the reason for termination of the agreements is one or more of the matters set out in (a) to (c) immediately above. It does not, for example, preclude relying on the exemption if there has been a performance default, such as a failure to transfer margin.

The stay is a permanent stay once the contracts have been assigned to the bridge institution.

A subsequent WURA proceeding with respect to the insolvent member institution cannot be relied on as a new Event of Default. The following scenarios may apply:

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[44] S.C. 2009, c. 2, s. 245(7).

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

1. If a Non-Defaulting Party's Transactions are transferred to and assumed by the bridge institution and a liquidation order is subsequently made with respect to the defaulting member institution, the Non-Defaulting Party would not be permitted to rely on the eligible financial contracts stay exemption in the WURA to allow it to it to exercise its termination rights with respect to the Agreement and Transactions assumed by the bridge institution.[45]

2. If the Non-Defaulting Party's Transactions are not assigned and CIDC does guarantee the payment of any amount due by the defaulting member institution, would not be permitted to rely on the eligible financial contracts stay exemption in the WURA to allow it to exercise its termination rights with respect to the Agreement and Transactions.[46]

3. If the Non-Defaulting Party's Transactions are not assigned and the insolvent member institution is to be liquidated under the CDIC Act or WURA, CDIC might chose not to provide the guarantee, in which case there would be no impediment to relying on the eligible financial contracts stay exemption.

CDIC is a federal Crown corporation that is an agent of Her Majesty in right of Canada so it is the federal Crown that ultimately stands behind the statutory obligation of CDIC to ensure that the bridge institution meets its financial obligations (where the eligible financial contracts are assumed by the bridge institution) or the CDIC guarantee of the obligations of the defaulting member institution (where the eligible financial contracts are not assigned to the bridge institution and the guarantee is provided).

4.7.2 There is a risk that Client Transactions will not receive parallel treatment to the related CCP/Clearing Member/Firm Transactions:

(a) Section 13.1 of the PCSA grants protection from insolvency law and proceeding stays to certain designated clearing houses to allow enforcement of their clearing rules relating to settlement, close-out and collateral enforcement (the "**Clearing House Protection**"). In addition, the PCSA provides wider protection

[45] CDIC Act, s.39.18(b).

[46] CDIC Act, s.39.18(b).

for the settlement rules of a clearing and settlement system designated under section 4 of the PCSA as systemically important systems. These protections are somewhat wider than those afforded to the Client as against the Clearing Member or the Clearing Member as against the Client. Consequently, there is a possibility that the CCP will be in a position to exercise its rights against the Clearing Member in circumstances where the Client is stayed or otherwise unable to exercise its rights against the Clearing Member.

For example, the PCSA section 4 designation received by a CCP provides an exemption from the temporary stay described above in the context of the CDIC bridge bank provisions such that the CCP can terminate and close out the Transactions over the designated system with the Firm or Clearing Member; however, it is not clear that this protection extends to the related Client Transactions. Consequently, it is possible that the CCP may terminate the transactions with the Firm or Clearing Member, but that the automatic termination that is intended to occur under the Clearing Agreements would be stayed.

(b) The conditional stay described above could apply to both the Client Transactions and the related Cleared Transactions (whether or not the CCP or its clearing system are designated under section 13.1 or section 4 of the PCSA) but this depends on whether CDIC provides the necessary guarantees or undertakings to implement the conditional stays. There is no statutory requirement that CDIC provide the same guarantees and undertakings to the Client with respect to the Clearing Members as it provides the CCP with respect to the Clearing Member or vice versa. Consequently, it is legally possible that the CCP may be free to exercise its termination and other close-out rights in situations where the automatic termination of and the exercise of other rights under the Client Transactions would be stayed.

(c) The bridge bank provisions of the CDIC Act allow CDIC to transfer transactions between the Clearing Member or Firm that is subject to the proceeding and its counterparties to a bridge institution and in that situation there would be a permanent

> stay of rights to terminate, close-out or deal with any margin with respect to the transferred transactions (subject to any new default). If CDIC decides to transfer the Client Transactions to a bridge institution, there is no statutory requirement that CDIC transfer the related transactions between the Clearing Member or Firm and the CCP, and vice versa. Such a situation could interfere with the operation of the Clearing Agreements.

We anticipate that CDIC would appreciate the necessity of parallel treatment of the Client Transactions and the Transactions with the CCP but there is no statutory requirement that it do so.

4.7.3 In a CDIC Act Proceeding there is an automatic stay on rights of set-off, although the insolvent institution cannot enforce a claim to the extent that it is otherwise subject to a right of set-off. The CDIC Act safe-harbour for termination and netting rights and dealing with financial collateral can be relied on with respect to EFCs, but not other Transaction types. The CDIC Act safe-harbour is subject to the bridge bank provisions discussed in the above paragraph (a).

4.7.4 **Multibranch Parties.** The analysis in paragraph 3.14 differs with respect to Canadian branches of authorized foreign banks in that the express recognition for rights of set-off is restricted to obligations arising in branch transactions.

> 158. The law of set-off, as administered by the courts, whether of law or equity, applies, in the same manner and to the same extent as if the business in Canada of the authorized foreign bank was not being wound up under this Act, only to
>
> (a) claims by creditors of the authorized foreign bank in respect of its business in Canada; and
>
> (b) proceedings for the recovery of debts due or accruing due to an authorized foreign bank in respect of its business in Canada at the commencement of the winding-up. The WURA includes provisions specifically relating to the winding-up of the assets in Canada of a branch of a non-Canadian bank.

A liquidator under the WURA has jurisdiction to liquidate only the

assets of the non-Canadian bank in respect of its business in Canada[47]. The assets in respect of its business in Canada are those the bank shows on its books and records as being the assets of the bank in respect of its business in Canada[48]. The WURA allows the claims of all creditors to be made in a liquidation, but "creditor" with respect to a foreign bank branch is deemed to be a reference to a creditor of the bank in respect of its business in Canada. If the liability is shown on the bank's books and records as a liability of the foreign branch, then the person owed that liability will be a creditor entitled to make a claim in the Canadian winding-up proceeding. Further, the EFC safe-harbours also apply differently to branches of foreign banks. The WURA provides that these protections of the EFC safe harbours can only apply to the EFCs and obligations between the authorized foreign bank in respect of its business in Canada and another party (s.22.1(1.1)).

For the reasons discussed below, we do not believe that these restrictions affect termination rights or, except in limited ways, netting rights. There is no assurance, however, that the Canadian financial institutions regulator or a court would interpret them in this way and it may be that only branch Transactions can be netted.

The provisions do, however, clearly place one limit on the claim of the Non-Defaulting Party. The Non-Defaulting Party could not claim in the liquidation of the Canadian branch more than the amount of the obligations of the foreign bank contracted through the Canadian branch of the foreign bank. Therefore, the Insolvency Representative in Canada would not include obligations with respect to all Transactions, regardless of the branch from which they were entered into in the calculation of amounts owed to and from the defaulting foreign bank.

We considered whether section 13 of the PCSA, would enhance the Non-Defaulting Party's right to claim the full amount owing by the foreign bank in the Canadian liquidation regardless of which branch contracted the obligation with respect to the terminated Transaction. Section 13 protects the right to net exposures where the Agreement is between financial institutions (which would include a foreign bank). It allows the parties to determine the net amount owing and to make a claim as a "creditor" in a Canadian insolvency proceeding for that net

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47 WURA, s.6(2).

48 Bank Act, s.523(2).

amount. Section 13 expressly states that it applies notwithstanding any insolvency law to the contrary.

By its terms section 13 takes precedence over any contrary terms in the WURA. However, this provision may not go so far as to protect a right to be a creditor for all obligations simply because they are the subject of a netting agreement. Section 13 is intended to protect termination and netting rights, not to protect a person's status as a creditor generally. Therefore, notwithstanding the PCSA, we conclude that the Insolvency Representative of the Defaulting Party in this jurisdiction could not claim more than the amount of the obligations of the foreign bank contracted through the Canadian branch. Section 13 does otherwise protect, however, the right to terminate and net transactions entered into pursuant to a master agreement to the extent that there is any question as to the effect on termination and netting rights of these provisions of the WURA. In other words, section 13 should prevent the liquidator from claiming more than the net amount owing on termination from the Non-Defaulting Party.

The question then becomes whether netting rights are affected by the limited definition of "creditor" in the WURA where section 13 does not apply (i.e. the other party is not a "financial institution"). Arguably, to allow set-off of claims contracted through a non-Canadian branch indirectly permits the Non-Defaulting Party to obtain payment of its non-Canadian claims. While the WURA is somewhat ambiguous in this regard, we are of the opinion that the Non-Defaulting Party would be entitled to net obligations with respect to all Transactions such that:

- it would not be required to make a claim less than the obligations of the foreign bank contracted through the Canadian branch if on a full net basis it would be owed at least that amount, and
- it would not be required to pay more to the liquidator of the Canadian branch than it would owe on a full net basis.

We hold this view for several reasons.

First, while the WURA only expressly extends termination rights to Canadian branch transactions, this does not affect termination rights under non-Canadian branch transactions. This limitation simply recognizes, in our view, that the Canadian legislature and court does not have jurisdiction over non-Canadian branch transactions. In other words, while it does not protect them, it does not prevent their

enforcement either.

Second, while the WURA limits the claims that can be made against the assets of the Canadian branch, it does not provide that a liquidator in enforcing a claim of the Defaulting Party or assessing a claim of a Non-Defaulting Party is permitted to ignore rights of set-off. Subsection 523(2) of the Bank Act does say that the assets of an authorized foreign bank in respect of its business in Canada, as shown by its books and records, are considered to be its assets in respect of its business in Canada. Branch records may show only the obligations of the Non-Defaulting Party with respect to transactions entered into by the Canadian branch as among its assets and the obligations of this branch as its liabilities. Nevertheless, we do not believe that subsection 523(2) is intended to alter the enforceability of a contractual relationship between the foreign bank and the Non-Defaulting Party such that the liquidator could enforce the obligations of the Non-Defaulting Party with respect to Canadian transactions without regard to its contractual rights of set-off.

However, this view is not free from doubt. Section 158 of the WURA states that the law of set-off, as administered by the courts, whether of law or equity, applies, in the same manner and to the same extent as if the business in Canada of the authorized foreign bank was not being wound up under this Act, but does go on to qualify this by saying that it only applies to (a) claims by creditors of the authorized foreign bank in respect of its business in Canada and (b) proceedings for the recovery of debts due or accruing due to an authorized foreign bank in respect of its business in Canada at the commencement of the winding-up. If a court was to determine that enforceability of a contractual netting right is restricted in scope to the set-off protection recognized by this provision, then only branch claims and obligations might be protected in a WURA Proceeding with respect to a branch of a non-Canadian bank.

The other situation to consider is where the Non-Defaulting Party is a net creditor of the Defaulting Party if only the obligations contracted through the Canadian branch are taken into account, but a net creditor with respect to a lesser amount if obligations of the Defaulting Party contracted through other branches are also taken into account. Nothing would prevent the Non-Defaulting Party from making the lesser claim (thereby respecting the global netting) and it is highly unlikely that the Canadian liquidator would insist that the larger claim

be made. On the other hand, if the Non-Defaulting Party were to make the larger claim, the liquidator could rely on its contractual rights and, if the Non-Defaulting Party was a "financial institution", section 13 of the PCSA would apply to allow a set-off of the non-Canadian obligations so as to reduce that amount owing.

In summary, although there is uncertainty as to the proper interpretation of the ring-fencing provisions, we are of the view that the Netting Provisions under the Agreement would be not be undermined by a WURA Proceeding with respect to a Defaulting Party in the sense that the liability of the Non-Defaulting Party to the Canadian liquidator could not be more than it would otherwise be under the Agreement and its claim against the Non-Defaulting Party cannot be more than it would otherwise be under the Agreement. However, the claim of the Non-Defaulting Party in a Canadian liquidation cannot be greater than the obligations of the Defaulting Party with respect to Transactions contracted through its Canadian Office.

5. MODIFICATIONS TO QUALIFICATIONS

Furthermore, the qualifications at paragraph 4 are deemed modified as follows:

(a) Qualifications with respect to the CCAA and BIA are not applicable; and

(b) The CDIC Act reorganization power has not been used in the past. Consequently there is no practice regarding conversion of the Liquidation Amount to comment on. We would expect that a requirement to value claims in Canadian currency on the date the proceeding commenced would be established by CDIC.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 2
Partnerships

Subject to the modifications and additions set out in this Schedule 2 (*Partnerships*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" which are Partnerships. For the purposes of this Schedule 2 (*Partnerships*), "***Partnerships***" means a limited or an ordinary partnership formed under the laws of a province of Canada, such as the Civil Code (Quebec).

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 2 (Partnerships);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: (Partnerships) (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Partnership could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 With respect to the partnership or partners proceedings under the *Bankruptcy and Insolvency Act* (Canada) ("**BIA**") for either (i) liquidation ("**BIA Bankruptcy**") or (ii) reorganization/ arrangement with creditors under Part III, Division I ("**BIA Proposals**");

3.1.2 With respect to any corporate general partner of a limited partnership (and unless it is a corporation incorporated under the *Canada Business Corporations Act*), proceedings under the *Winding-up and Restructuring Act* (Canada) ("**WURA**") for either (i) liquidation or (ii) reorganization/ arrangement with creditors ("**WURA Proceedings**");

3.1.3 With respect to any corporate general partner of a limited partnership

proceedings under the *Companies' Creditors Arrangement Act* (Canada) ("**CCAA**") for reorganization/ arrangement of claims of creditors of corporations ("**CCAA Plan of Arrangement**");

3.1.4 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**"); and

3.1.5 With respect to any corporate general partner of a limited partnership, Corporate plans of arrangement involving insolvent entities and providing for the reorganization/arrangement of claims of creditors ("**Corporate Plans of Arrangement**").

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, without the need for any additions, except that a provision similar to 10.1(i) of the Professional Client Agreement should be used with respect to the general partner of a limited partnership or the partners of an ordinary partnership.

4. **ADDITIONAL QUALIFICATIONS**

None.

5. **MODIFICATIONS TO QUALIFICATIONS**

None.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 3
Insurance Companies

Subject to the modifications and additions set out in this Schedule 3 (*Insurance Companies*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties which are Insurance Companies. For the purposes of this Schedule 3 (*Insurance Companies*), "***Insurance Companies***" means an insurance corporation incorporated under the *Insurance Companies Act* (Canada) or provincial incorporation legislation applicable to the incorporation of companies licensed to carry on insurance business, and Canadian branches of non-Canadian insurance companies licensed to carry on insurance business in Canada.

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 3 (Insurance Companies);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Insurance Companies (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is an Insurance Company could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Proceedings under the *Winding-up and Restructuring Act* (Canada) ("**WURA**") for either (i) liquidation or (ii) reorganization/ arrangement with creditors ("**WURA Proceedings**"); and

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, without the need for any additions.

Any opinions with respect to Insolvency Proceedings other that the WURA in the main body of the opinion do not apply. The WURA analysis applies to an

Insurance Company.

4. **ADDITIONAL QUALIFICATIONS**

None.

5. **MODIFICATIONS TO QUALIFICATIONS**

Furthermore, the qualifications at paragraph 4 are deemed modified as follows:

(a) Any qualifications relating to the BIA, CCAA, and Corporate Plans of Arrangement do not apply.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 4
Individuals

Subject to the modifications and additions set out in this Schedule 4 (*Individuals*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are Individuals. For the purposes of this Schedule 4 (*Individuals*), "***Individual***" means a natural person domiciled and resident in Quebec.

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 4 (Individuals);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Individuals (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is an Individual could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Proceedings under the *Bankruptcy and Insolvency Act* (Canada) ("**BIA**") for either:

(i) liquidation ("**BIA Bankruptcy**");

(ii) reorganization/ arrangement with creditors under Part III, Division I ("**BIA Proposals**"); or

(iii) if the Individual owes $250,000 or less (excluding debts owing on mortgages on the principal residence), reorganization/ arrangement with creditors under Part III, Division II of the BIA ("**Consumer Proposals**").

We confirm that the events specified in the Insolvency Events of Default

Clause adequately refer to all of the above Insolvency Proceedings, without the need for any additions.

Consumer Proposals are subject to the same automatic stay on the termination or acceleration of contractual obligations by reason that the Individual is insolvent or a consumer proposal has been filed as are entities subject to the more generally applicable BIA Proposal regime. As in the BIA Proposal regime, an exemption from the automatic stay applies with respect to Consumer Proposals for an EFC.[49]

4. ADDITIONAL QUALIFICATIONS

The opinions in this opinion letter are subject to the following additional qualifications:

(a) We express no opinion as to the effect of any consumer protection laws on the analysis in the memorandum. A consumer is an individual acting for personal, family or household purposes and does not include a person who is acting for business purposes.

5. MODIFICATIONS TO QUALIFICATIONS

Furthermore, the qualifications at paragraph 4 are deemed modified as follows:

(a) With respect to the Individual, qualifications relating to statutes other than the BIA do not apply.

[49] BIA, s.66.34 (7), (8), (9).

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 5
Investment Funds

Subject to the modifications and additions set out in this Schedule 5 (*Investment Funds*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are Investment Funds. For the purposes of this Schedule 5 (*Investment Funds*), "***Investment Funds***" means a corporation of the type covered by the opinion as a Corporation, a limited partnership of the type covered by Schedule 2 of this opinion, or a common law trust established under the laws of a common law province of Canada, established to provide investors with a share in profits or income arising from property acquired, held, managed or disposed of by the manager(s) of the legal entity or arrangement or a right to payment determined by reference to such profits or income, not including a Pension Entity, but including an Investment Fund trust in which a Pension Entity invests. In Canada such funds are known as (i) prospectus qualified mutual funds subject to National Instrument 81-102 (in Quebec, Regulation 81-102); (ii) pooled funds which are mutual funds that are not prospectus qualified; (iii) a non-redeemable investment fund, typically listed and prospectus qualified, but not necessarily.

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 5 (Investment Funds);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Investment Funds (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is an Investment Fund could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 With respect to any Investment Fund that is a corporation, partnership

or "income trust" as defined in the CCAA and perhaps with respect to any other Investment Fund that is in the form of a trust, proceedings under the *Bankruptcy and Insolvency Act* (Canada) ("**BIA**") for either (i) liquidation ("**BIA Bankruptcy**") or (ii) reorganization/arrangement with creditors under Part III, Division I ("**BIA Proposals**");

3.1.2 With respect to any Investment Fund that is a corporation or corporate general partner of a limited partnership (and unless it is a corporation incorporated under the CBCA), proceedings under the *Winding-up and Restructuring Act* (Canada) ("**WURA**") for either (i) liquidation or (ii) reorganization/arrangement with creditors ("**WURA Proceedings**");

3.1.3 With respect to any Investment Fund that is a corporation, corporate general partner of a limited partnership or "income trust" as defined in the CCAA, proceedings under the *Companies' Creditors Arrangement Act* (Canada) ("**CCAA**") for reorganization/arrangement of claims of creditors of corporations ("**CCAA Plan of Arrangement**");

3.1.4 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**");

3.1.5 With respect to any Investment Fund that is a corporation or corporate general partner of a limited partnership, Corporate plans of arrangement involving insolvent entities and providing for the reorganization/arrangement of claims of creditors ("**Corporate Plans of Arrangement**"); or

3.1.6 With respect to any Investment Fund in the form of a trust, voluntary wind-up by the trustee of the Investment Fund pursuant to the terms of the trust deed, agreement or declaration ("**Voluntary Wind-up**").[50]

An "income trust" is a trust which has assets in Canada if (a) its units are listed on a prescribed stock exchange on the date of the initial bankruptcy event or (b) the majority of its units are held by a trust whose units are listed on a prescribed stock exchange on the date of the initial bankruptcy event.[51]

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, except with respect to Voluntary Wind-up. We recommend use of the Trustee Annex

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[50] This is not strictly speaking an insolvency regime, but it is likely the manner in which an insolvent trust would be dealt with.

[51] BIA, s.2; CCAA, s.2(1).

so that paragraph 3.1(d) applies, which would cover such an event.

Enforceability of FOA Netting Provision (paragraph 3.3), Clearing Module Netting Provision (paragraph 3.4), Addendum Netting Provision (paragraph 3.5), FOA Set-off Provisions (paragraph 3.7), Clearing Module Set-Off Provision (paragraph 3.8), Addendum Set-Off Provision (paragraph 3.9) or Title Transfer Provisions (paragraph 3.10).

The analysis in the main body of the opinion with respect to the Insolvency Proceedings noted above will apply. In addition, there is a possibility of a voluntary wind-up. The PCSA will not apply.

Voluntary Wind-up

If the trustee of a trust is conducting a voluntary wind-up outside of a court process, then there is no stay order possible that could interfere with the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision or the Title Transfer Provisions.

4. **ADDITIONAL QUALIFICATIONS**

None.

5. **MODIFICATIONS TO QUALIFICATIONS**

None.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 6
Sovereign, State of a Federal Sovereign and Sovereign-Owned Entity

Subject to the modifications and additions set out in this Schedule 6 (*Sovereign, State of a Federal Sovereign and Sovereign-Owned Entity*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are Sovereign and Public Sector Entities. For the purposes of this Schedule 6 Sovereign, State of a Federal Sovereign and Sovereign-Owned Entity, "**Sovereign**" means Her Majesty the Queen in right of Canada acting through the Minister of Finance (**Canada**). "**State of a Federal Sovereign**" means Her Majesty the Queen in right of Quebec acting through the Quebec Minister of Finance. "**Sovereign-Owned Entity**" means a corporation wholly owned by Canada or Quebec and which is for all purposes an agent of the Canada or Quebec, and not including any public sector Pension Entity (those are considered in Schedule ●) or municipal government/local authority.

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 6 (Sovereign and Public Sector Entities);*".

[There are no applicable procedures.]

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Sovereign and Public Sector Entities (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Sovereign or Public Sector Entity could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

None of the Insolvency Proceedings would apply to Canada, Quebec or a Sovereign Owned Entity that acts solely as agent of the Crown. Legislation

would be required to wind-up or reorganize the affairs of an insolvent Sovereign or Sovereign Owned Entity.

While Parliament or a legislature could pass such legislation in the event of an insolvency, based on the law as it stands today, the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision and the Title Transfer Provisions would remain as enforceable as they are outside of an Insolvency Proceeding. In other words, no existing insolvency or other law and no Insolvency Proceeding in which an automatic or court ordered stay of either termination or netting rights interferes with those otherwise enforceable contractual rights.

(A Sovereign Owned Entity that was not an agent of the Crown for all purposes might be subject to the same Insolvency Proceedings as a Corporation as considered in the body of the main opinion.)

4. ADDITIONAL QUALIFICATIONS

4.1 The opinions in this opinion letter are subject to the following additional qualifications.

4.1.1 We have not reviewed the governing legislation for any particular Sovereign Owned Entity for the purposes of this opinion. Such legislation may alter the analysis and conclusions in this opinion.

4.1.2 The Government of Quebec acting through Her Majesty the Queen in right of Quebec (the "**Government of Quebec**") and Quebec Sovereign-Owned Entities that are agents of the Government of Quebec have immunity from set-off under Quebec law. We are of the view that the Government of Quebec and Quebec Sovereign-Owned Entities can waive such immunity and that by agreeing to the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision, they have done so. However, there is no jurisprudence on this issue and therefore our view cannot be advanced with certainty. We would also note that there is currently a bill before the Quebec National Assembly, Bill 58, *An Act to again amend various legislative provisions concerning mainly the financial sector*, which, if passed as drafted, will clarify that compensation (set-off) can be invoked against the Government of Quebec in respect of transactions that it has entered into which are referred to in the first paragraph of section 16 or an

instrument referred to in section 16.1 of the *Financial Administration Act* (Quebec). However, this provision in Bill 58 does not apply to Sovereign-Owned Entities.

4.1.3 Quebec language legislation requires that contracts with the Government of Quebec and Quebec Sovereign-Owned Entities be in French if they are concluded in Quebec and it is not clear whether an English-only contract which contravenes this requirement would be unenforceable. We believe, on the basis of jurisprudence involving a similar rule for private parties, that an English contract concluded in Quebec would be enforceable but there is no jurisprudence on this issue and therefore our view cannot be advanced with certainty.

4.1.4 As with any contract with any government, there is some possibility that the legislature could pass legislation aimed at relieving Canada or the Government of Quebec or any Sovereign Owned Entity of its contractual obligations or altering the terms of the contracts to which it is a party, or could pass debt moratorium legislation. The following factors should be considered in amelioration of this possibility. First, the passing of legislation to relieve a government from debt or other contractual obligations, particularly under contracts of a commercial nature rarely happens in Canada. Second, we do not believe a federal or provincial government of Canada has ever passed debt moratorium or similar legislation to deal with its financial difficulties.

5. MODIFICATIONS TO QUALIFICATIONS

Furthermore, the qualifications at paragraph 4 are deemed modified as follows.

The qualifications relating to the BIA, CCAA, WURA or other Insolvency Proceedings would not apply.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 7
Trustees of Private Trusts

Subject to the modifications and additions set out in this Schedule 7 (*Private Trusts*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are *Private Trusts*. For the purposes of this Schedule 7 (*Private Trusts*) "***Private Trusts***" means the trustee(s) of an arrangement without legal personality that is organized by agreement, declaration or deed of trust to carry on business, other than an Investment Fund or a Pension Entity and which is governed by the laws of a province of Canada.

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 7 (Private Trusts);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Private Trusts (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Private Trust could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Possible proceedings under the *Bankruptcy and Insolvency Act* (Canada) ("**BIA**") for either (i) liquidation ("**BIA Bankruptcy**") or (ii) reorganization/ arrangement with creditors under Part III, Division I ("**BIA Proposals**"), although its application to trusts that are not "income trusts"[52] is unclear;

[52] An "income trust" is a trust which has assets in Canada if (a) its units are listed on a prescribed stock exchange on the date of the initial bankruptcy event or (b) the majority of its units are held by a trust whose units are listed on a prescribed stock exchange on the date of the initial bankruptcy event.

3.1.2 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**"); and

3.1.3 Voluntary wind-up by the trustee of the Investment Fund pursuant to the terms of the trust deed, agreement or declaration ("**Voluntary Wind-up**").[53]

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, except for Voluntary Wind-up. We recommend use of the Trustee Annex so that paragraph 3.1(d) applies, which would cover such an event.

Voluntary Wind-up

If the trustee of a trust is conducting a voluntary wind-up outside of a court process, then there is no stay order possible that could interfere with the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision or the Title Transfer Provisions.

4. ADDITIONAL QUALIFICATIONS

None.

5. MODIFICATIONS TO QUALIFICATIONS

None.

[53] This is not strictly speaking an insolvency regime, but it is likely the manner in which an insolvent trust would be dealt with.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 8
Charitable Corporations

Subject to the modifications and additions set out in this Schedule 8 (*Charitable Corporations*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are Charitable Corporations. For the purposes of this Schedule 8 (Charitable Corporations), "***Charitable Corporations***" means corporations without share capital organized under the general legislation for the incorporation of companies that are incorporated to carry on charitable purposes, under the *Canada Corporations Act* (Canada) and Part III of the *Companies Act* (Quebec).

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 8 (Charitable Corporations);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Charitable Corporations (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Charitable Corporation could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Proceedings under the *Bankruptcy and Insolvency Act* (Canada) (**BIA**) for either (i) liquidation (**BIA Bankruptcy**) or (ii) reorganization/ arrangement with creditors under Part III, Division I (**BIA Proposals**);

3.1.2 Proceedings under the *Winding-up and Restructuring Act* (Canada) ("**WURA**") for either (i) liquidation or (ii) reorganization/ arrangement with creditors ("**WURA Proceedings**");

3.1.3 Proceedings under the *Companies' Creditors Arrangement Act* (Canada) ("**CCAA**") for reorganization/ arrangement of claims of creditors of

corporations ("**CCAA Plan of Arrangement**"); and

3.1.4 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**").

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, with the need for any addition.

4. **ADDITIONAL QUALIFICATIONS**

None

5. **MODIFICATIONS TO QUALIFICATIONS**

None.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 9
Pension Entities

Subject to the modifications and additions set out in this Schedule 9 (*Pension Entities*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are Pension Entities. For the purposes of this Schedule 9 (*Pension Entities*), "***Pension Entities***" means:

- privately established pension arrangements in the form of common law trusts governed by the *Supplemental Pension Plans Act* (Quebec) or the *Pension Benefits Standards Act* (Canada) that are not established for public sector employees; and

- the following public sector pension plans:
  - the Ontario Teachers' Pension Plan Board – **OTPPB** (which is a statutory corporation created by the *Ontario Teachers' Pension Act* (Ontario));
  - OMERS Administration Corporation – **OMERS** (which is a statutory corporation created by the *Ontario Municipal Employees Retirement System Act, 2006* (Quebec));
  - Healthcare of Ontario Pension Plan Board - **HOOPP** (formerly Hospitals of Ontario Pension Plan Board);
  - Canadian Pension Plan Investment Board – **CPPIB** - governed by the *Canadian Pension Plan Investment Board Act* (Canada);
  - Public Sector Pension Investment Board – **PSPIB** - governed by the *Public Sector Pension Investment Board Act* (Canada); and
  - La Caisse de dépôt et placement du Québec – **CDPQ** (which is a statutory corporation created by the *Act respecting La Caisse de dépôt et placement du Québec*).

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 9 (Pension Entities);*".

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Pension Entities (paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Pension Entity could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Proceedings under the *Bankruptcy and Insolvency Act* (Canada) (**BIA**) for either (i) liquidation ("**BIA Bankruptcy**") or (ii) reorganization/ arrangement with creditors under Part III, Division I ("**BIA Proposals**");

3.1.2 Proceedings under the *Companies' Creditors Arrangement Act* (Canada) ("**CCAA**") for reorganization/ arrangement of claims of creditors of corporations in the case of pension entities in the form of corporations[54] ("**CCAA Plan of Arrangement**");

3.1.3 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**");

3.1.4 Voluntary wind-up by the trustee or administrator of the pension entity if it is a trust ("**Voluntary Wind-up**"); and

3.1.5 Wind-up under the supervision of the pension regulator ("**Involuntary Wind-up**").

The process which would most likely apply in the event that the assets of a pension fund were insufficient to meet its liabilities is Involuntary Wind-up. The pension regulator in Quebec is the Régie des rentes du Québec (**Régie**) and federally is the Office of the Superintendent of Financial Institutions ("**OSFI**").

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, except Voluntary Wind-up. We recommend use of the Trustee Annex for Pension Entities that are trusts.

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[54] e.g. OTPPB or OMERS.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

Under the Quebec *Supplemental Pension Plans Act* (**Quebec SPPA**), solvency of the plan is not a listed circumstance for granting a wind-up order, but those listed circumstances are ones that would indirectly affect the solvency of the plan (e.g. pension fund with insufficient assets to pay its liabilities, employer failing to collect or pay employer contributions into pension fund).

The Federal *Pension Benefits Standards Act* ("**Federal PBSA**") provides for OSFI to declare a plan to be wound up, in whole or in part, in certain circumstances. One of those circumstances is that the plan has failed to meet the prescribed tests and standards for solvency in respect of funding. Failure of the employer to make required contributions (which indirectly is a matter of plan solvency) is also a ground for winding up.

Special Circumstances of CPPIB and PSPIB. The legislation governing CPPIB - the *Canada Pension Plan Investment Board Act* (Canada) - specifically provides that no insolvency statute or winding-up statute applies to CPPIB. Its affairs can be wound up only if Parliament enacts legislation to that effect.

> 55. No Act relating to the insolvency or winding-up of any corporation applies to the Board and in no case shall the affairs of the Board be wound up unless Parliament so provides.

Similarly, PSPIB is incorporated and governed by the *Public Sector Pension Investment Act* (Canada). Section 52 of this Act is the same as section 55 of the Act governing CPPIB.

Our reading of these provisions is that the BIA, the CCAA, the WURA and the restructuring procedure of the CDIC Act could not apply to CPPIB or PSPIB because they are statutes relating to the insolvency or winding up of a corporation. Further, they cannot be wound up under any kind of procedure, including by a pension regulator or a court appointed receiver.

Registered pension plans are financial institutions within the meaning of the PCSA.

Special Circumstances of CDPQ. The legislation governing CDPQ - the *Act respecting La Caisse de dépôt et placement du Québec* (Quebec) - provides that all of CDPQ's property "belonging to" CDPQ is the property of the Crown in right of Quebec. Therefore, in our view, none of the Insolvency Proceedings would apply to CDPQ. Further, it could not be wound up under any kind of procedure, including by a pension regulator.

In addition, it is unlikely that CDPQ is a financial institution within the meaning of the PCSA although this is not entirely clear.

- **Enforceability of FOA Netting Provision (paragraph 3.3), Clearing Module Netting Provision (paragraph 3.4), Addendum Netting Provision (paragraph 3.5), FOA Set-Off Provisions (paragraph 3.7), Clearing Module Set-Off Provision (paragraph 3.8), Addendum Set-Off Provision (paragraph 3.9) and Title Transfer Provisions (paragraph 3.10).**

Involuntary Wind-up by Pension Regulator

It is our view that in the course of winding-up a pension plan voluntarily or under the supervision of OSFI, the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision and Title Transfer Provisions would be enforceable. In addition, section 13 of the PCSA might prevent the pension regulator from compromising such rights, although it is not clear that Section 13 applies to this type of process.

Quebec SPPA

There is nothing in the Quebec SPPA that expressly imposes any stay on termination of contracts pursuant to their terms, or netting of transaction values or on liquidating credit support when a wind-up is commenced. Nor is there anything that expressly gives the regulator the power to impose any such requirement.

If the regulator purported to exercise such a power, section 13 of the PCSA might provide a basis upon which to challenge his action. Under section 13, termination rights in "netting agreements" between "financial institutions" are enforceable "notwithstanding anything in any law relating to bankruptcy or insolvency or any order of a court made pursuant to an administration of a reorganization, arrangement or receivership involving insolvency". The trustees would be a "financial institution". However, there is uncertainty as to whether section 13 applies because of the fact that the pension statute is not strictly speaking an "insolvency" law.[55]

[55] There may also be constitutional limitations to applying the PCSA to a provincial winding-up process.

In any event, as noted above, we do not believe that the Quebec regulator would have any power to prevent a party from exercising its termination rights under the Netting or Clearing Agreement to the extent they are triggered and we believe any attempt to do so could be successfully challenged in our view simply on the basis that he does not have the statutory jurisdiction to take such action.

Federal PBSA

There is nothing in the Federal PBSA that expressly imposes any stay on termination of contracts pursuant to their terms, or netting of transaction values or on liquidating collateral when a wind-up is commenced. Nor is there anything that expressly gives the regulator the power to impose any such requirement. The federal Superintendent of Financial Institutions (the pension regulator) does have wide remedial powers of a general nature. Section 11 of the Federal PBSA provides that the Superintendent can give directions to plan administrators "or any person" in respect of a pension plan who is about to commit an act or pursue a course of conduct that is contrary to safe and sound financial or business practices. The Superintendent can direct the person to refrain from committing the act or to perform a remedial act. We do not believe that this general power would give the Superintendent jurisdiction to order a party to a Transaction with the trustee/administrator of the plan to refrain from terminating its agreement.[56] Section 11 of the Federal PBSA provides that:

> Superintendent's directions to administrators
>
> 11. (1) If, in the opinion of the Superintendent, an administrator, an employer or any person is, in respect of a pension plan, committing or about to commit an act, or pursuing or about to pursue any course of conduct, that is contrary to safe and sound financial or business practices, the Superintendent may direct the administrator, employer or other person to
>
> (a) cease or refrain from committing the act or pursuing the course of conduct; and
>
> (b) perform such acts as in the opinion of the Superintendent are necessary to remedy the situation.
>
> Directions in the case of non-compliance
>
> (2) If, in the opinion of the Superintendent, a pension plan does not

[56] Given that the Superintendent of Financial Institutions is also the regulator that requires financial institutions to have robust termination and netting rights under such contracts, it would be surprising if it tried to undermine those same rights by attempting to use the section 11 power to prevent a third party institutions from exercising them.

> comply with this Act or the regulations or is not being administered in accordance with this Act, the regulations or the plan, the Superintendent may direct the administrator, the employer or any person to
>
> (a) cease or refrain from committing the act or pursuing the course of conduct that constitutes the non-compliance; and
>
> (b) perform such acts as in the opinion of the Superintendent are necessary to remedy the situation.
>
> Opportunity for representations
>
> (3) Subject to subsection (4), no direction shall be issued under subsection (1) or (2) unless the Superintendent gives the administrator, employer or other person a reasonable opportunity to make written representations.
>
> Temporary direction
>
> (4) If, in the opinion of the Superintendent, the length of time required for representations to be made under subsection (3) might be prejudicial to the interests of the members, former members or any other persons entitled to pension benefits or refunds under the pension plan, the Superintendent may make a temporary direction with respect to the matters referred to in subsection (1) or (2) that has effect for a period of not more than fifteen days.
>
> Continued effect
>
> (5) A temporary direction under subsection (4) continues to have effect after the expiry of the fifteen day period referred to in that subsection if no representations are made to the Superintendent within that period or, if representations have been made, the Superintendent notifies the administrator, employer or other person that the Superintendent is not satisfied that there are sufficient grounds for revoking the direction.

If the Superintendent purported to have such a stay power with respect to the termination or set-off rights, section 13 of the PCSA might provide a basis upon which to challenge his action. As with Quebec PBA plans, there is uncertainty as to whether section 13 applies because of the fact that the Federal PBSA is not strictly an "insolvency" law.[57]

In any event, as noted above, we do not believe that the Superintendent has any power to prevent a party from exercising its contractual rights and we believe any attempt to do so could be successfully challenged in our view simply on the basis that he does not have the statutory jurisdiction to take such action.

CPPIB, PSPIB

[57] Although unlike the Quebec case, there is no constitutional impediment to the PCSA taking priority over the provincial regime.

The analysis with respect to the federal public sector plans (CPPIB and PSBIB) is somewhat different because of the fact that they cannot be wound up without an Act of Parliament.

Given the statutory immunity from insolvency proceedings, there are no insolvency laws currently in place that could interfere with the enforceability of a termination right. CPPIB and PSPIB cannot be subject to an insolvency type proceeding unless Parliament takes the very significant step of passing legislation.

CPPIB and PSPIB are also each a "financial institution" for purposes of section 13 of the PCSA.

CDPQ

The analysis with respect to CDPQ is somewhat different because of the fact that none of the Insolvency Proceedings likely apply to CDPQ. Therefore, given the fact that Insolvency Proceedings do not apply, there are no insolvency laws currently in place that could interfere with the enforceability of a termination right unless Parliament takes the very significant step of passing legislation.

4. ADDITIONAL QUALIFICATIONS

4.1.1 CDPQ is an agent of Her Majesty in right of Quebec and thus has immunity from set-off under Quebec law. We are of the view that CDPQ can waive such immunity and that by agreeing to the FOA Netting Provision, the Clearing Module Netting Provision, the Addendum Netting Provision, the FOA Set-Off Provisions, the Clearing Module Set-Off Provision, the Addendum Set-Off Provision, it has done so. However, there is no jurisprudence on this issue and therefore our view cannot be advanced with certainty.

4.1.2 Quebec language legislation requires that contracts with CDPQ be in French if they are signed in Quebec and it is not clear whether an English-only contract which contravenes this requirement would be unenforceable. We believe, on the basis of jurisprudence involving a similar rule for private parties, that an English content concluded in Quebec would be enforceable but there is no jurisprudence on this issue and therefore our view cannot be advanced with certainty.

4.1.3 As with any contract with any government, there is some possibility that the legislature could pass legislation aimed at relieving CDPQ of its contractual

obligations or altering the terms of the contracts to which it is a party, or could pass debt moratorium legislation. The following factors should be considered in amelioration of this possibility. First, the passing of legislation to relieve a government from debt or other contractual obligations, particularly under contracts of a commercial nature rarely happens in Canada. Second, we do not believe a federal or provincial government of Canada has ever passed debt moratorium or similar legislation to deal with its financial difficulties.

5. MODIFICATIONS TO QUALIFICATIONS

Furthermore, the qualifications at paragraph 4 are deemed modified as follows:

> The qualifications respecting the Insolvency Proceedings would not apply to CPPIB, PSPIB and CDPQ.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

SCHEDULE 10
Municipal Corporations

Subject to the modifications and additions set out in this Schedule 10 (*Municipal Corporations*), the opinions, assumptions and qualifications set out in this opinion letter will also apply in respect of Parties acting as "Client" that are Municipal Corporations. . For the purposes of this Schedule 10 (Municipal Corporations), "**Municipal Corporations**" means municipalities governed by *An Act respecting the Commission municipale* (Quebec) or *An Act respecting Municipal Debts and Loans* (Quebec).

Except where the context otherwise requires, references in this Schedule to "*paragraph*" are to paragraphs in the opinion letter (but not to its Annexes or Schedules) and references to "*sections*" are to sections of this Schedule.

1. MODIFICATIONS TO TERMS OF REFERENCE AND DEFINITIONS

Paragraph 1.13.1 is deemed deleted and replaced with the following:

""***Insolvency Proceedings***" *means the procedures listed in section 3.1 of Schedule 10 (Municipal Corporations);*".

2. ADDITIONAL ASSUMPTIONS

None.

3. MODIFICATIONS TO OPINIONS

- **Insolvency Proceedings: Municipal Corporations (Paragraph 3.1)**

Paragraph 3.1 is deemed deleted and replaced with the following:

The only bankruptcy, composition, rehabilitation or other insolvency or reorganisation procedures to which a Party which is a Municipal Corporation could be subject under the laws of this jurisdiction, and which are relevant for the purposes of this opinion letter, are as follows:

3.1.1 Proceedings under the *Bankruptcy and Insolvency Act* (Canada) ("**BIA**") for either (i) liquidation ("**BIA Bankruptcy**") or (ii) reorganization/ arrangement with creditors under Part III, Division I ("**BIA Proposals**");

3.1.2 Proceedings under the *Companies' Creditors Arrangement Act* (Canada) ("**CCAA**") for reorganization/ arrangement of claims of creditors of corporations ("**CCAA Plan of Arrangement**");

3.1.3 Court administered receivership proceedings for liquidation of the Party under the national receivership provisions of the BIA ("**Receivership**"); and

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

3.1.4 Reorganization procedures under *An Act Respecting the Commission Municipale* (Quebec) or *An Act respecting Municipal Debts and Loans* (Quebec) ("**Quebec Municipal Reorganization Procedures**").

We confirm that the events specified in the Insolvency Events of Default Clause adequately refer to all of the above Insolvency Proceedings, except for the Quebec Municipal Reorganization Procedures. It would be prudent to amend the Event of Default definition to specifically add to it the exercise by the Commission Municipale of any of its powers under *An Act Respecting the Commission Municipale* (Quebec) or *An Act respecting Municipal Debts and Loans*. Sample language:

> (I) any entity such as an organization, board, commission, authority, agency or body is appointed or designated to monitor, review, oversee, recommend or declare a financial emergency or similar state of financial distress with respect to it or (II) there shall be declared or introduced or proposed for consideration by it or by any legislative or regulatory body with competent jurisdiction over it, the existence of a state of financial emergency or similar state of financial distress in respect of it.

Quebec municipalities are subject to *An Act Respecting the Commission Municipale* (Quebec) or *An Act respecting Municipal Debts and Loans*. Certain larger municipalities may be subject to their own unique legislation that may include provisions relevant to insolvency but we have not reviewed any of such legislation for the purposes of this opinion.

The most likely method of dealing with an insolvent Quebec municipality may be under the reorganization procedures of *An Act Respecting the Commission Municipale* or a convention with its creditors under *An Act respecting Municipal Debts and Loans*.

An Act Respecting the Commission Municipale provides that a municipality may be declared in default when it has not paid the interest or principal of a loan at maturity, when it has ceased to pay its current debts generally as they fall due, or when it has neglected for more than 30 days to satisfy a final judgment ordering it to pay a sum of money (Section 38(1)). The Commission municipale du Québec (the "**Commission**") is not bound to request that a municipality be declared in default except upon a written demand made by the municipality itself or by the creditors of the municipality who hold claims against it representing at least 25% of the total debt of the municipality (Section 38(2)). The Commission may petition a judge of the Superior Court for an investigation to have the municipality declared in default, and, if the

evidence offered is sufficient, the judge shall declare the municipality to be in default (Sections 39 and 41). The municipality is under the control of the Commission from the date of the judgment until the Commission declares that the municipality is no longer in default (Section 43).

Where a municipality is in default, Division VIII sets out the Commission's powers. Amongst other things, no contract for work may be given without the previous approval of the Commission, and all moneys collected for the municipality must be deposited in a bank, in the name of the Commission in trust for the municipality, while no immovable may be acquired by mutual agreement by the municipality without the authorization of the Commission and no immovable may be sold by the municipality without the Commission participating in the deed (Section 48). More generally, in any case not provided for by Section 48, the Commission shall be substituted as of right for the municipality whenever the municipality refuses or neglects to perform any acts which the Commission orders it to perform (Section 48).

Pursuant to subsection 54(b) of an *Act Respecting the Commission Municipale*, the Commission may ratify and confirm any plan of financial reorganization submitted by such municipality and interesting its creditors as a whole or any category of its creditors. The ratification and confirmation of such plan shall be legally binding on the parties, unless creditors interested in the said plan who are holders of claims representing at least 33 1/3% of the total debt affected by such plan object thereto in the manner provided by a rule of practice established in virtue of section 87.

Pursuant to section 49 of *An Act respecting Municipal Debts and Loans*, a municipality may, by by-law, authorize the making of a convention with all its creditors or creditors to whom it is indebted under one or more loan by-laws and such a convention takes effect provided it has been ratified by two-thirds of the creditors contemplated in it and the Minister of Municipal Affairs, Regions and Land Occupancy has approved the by-law authorizing it. The convention is binding on all the creditors contemplated in it. There is no further detail respecting the procedure in respect of such a convention. It is unlikely that this section would be applicable unless the municipality in question had passed a loan by-law in connection with the Agreement.

A possible scenario with respect to a municipality is that it would be voluntarily wound-up before it reached a state of insolvency under the Quebec *Winding-up Act*.

In the event of a municipal insolvency, it is more likely that this procedure would apply than the BIA, CCAA or Receivership.

Effect of Quebec Municipal Reorganization Procedures on Netting Provisions, Set-off Provisions or Title Transfer Provisions

None of the statutes discussed above provides for a specific stay of actions or proceedings against a municipality. In addition, we are not aware of any situations in which it has been argued that the above provisions of these statutes could be used to interfere with collateral enforcement rights under an agreement such as the Agreement. In the case of *An Act respecting Municipal Debts and Loans*, the convention procedure does not involve any government entity or court which could stay collateral enforcement rights. Although, under *An Act respecting the Commission municipale*, the Commission Municipale seems to have the power to set its own procedure in regard to a reorganization, while the matter is not free from doubt, we do not believe that the Commission Municipale has the power to order a stay preventing the exercise of contractual rights of termination, netting or collateral enforcement.

4. **ADDITIONAL QUALIFICATIONS**

We have not reviewed any legislation or regulation relating to any specific municipality. As noted above, some Municipal Corporations, like the Ville de Montréal, have unique legislation.

5. **MODIFICATIONS TO QUALIFICATIONS**

None.

Canada – Quebec (situs)/Prudential Regulation/Counterparty/Netting

ANNEX 1
FORMS OF FOA NETTING AGREEMENTS

1. Master Netting Agreement - One-Way (1997 version) (the "**One-Way Master Netting Agreement 1997**")

2. Master Netting Agreement - Two-Way (1997 version) (the "**Two-Way Master Netting Agreement 1997**")

3. Default, Netting and Termination Module (One-Way Netting) (2007 version) (the "**Long-Form One-Way Clauses 2007**")

4. Short Form Default, Netting and Termination Module (One-Way Netting) (2007 version) (the "**Short-Form One-Way Clauses 2007**")

5. Short Form Default, Netting and Termination Module (One-Way Netting) (2009 version) (the "**Short-Form One-Way Clauses 2009**")

6. Short Form Default, Netting and Termination Module (One-Way Netting) (2011 version) (the "**Short-Form One-Way Clauses 2011**")

7. Default, Netting and Termination Module (Two-Way Netting) (2007 version) (the "**Long-Form Two-Way Clauses 2007**")

8. Default, Netting and Termination Module (Two-Way Netting) (2009 version) (the "**Long-Form Two-Way Clauses 2009**")

9. Default, Netting and Termination Module (Two-Way Netting) (2011 version) (the "**Long-Form Two-Way Clauses 2011**")

10. Short Form Default, Netting and Termination Module (Two-Way Netting) (2007 version) (the "**Short-Form Two-Way Clauses 2007**")

11. Short Form Default, Netting and Termination Module (Two-Way Netting) (2009 version) (the "**Short-Form Two-Way Clauses 2009**")

12. Short Form Default, Netting and Termination Module (Two-Way Netting) (2011 version) (the "**Short-Form Two-Way Clauses 2011**")

13. Professional Client Agreement (2007 Version), including Module G (Margin and Collateral) (the "**Professional Client (with Security Provisions) Agreement 2007**")

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14. Professional Client Agreement (2009 Version), including Module G (Margin and Collateral) (the "**Professional Client (with Security Provisions) Agreement 2009**")

15. Professional Client Agreement (2011 Version) including Module G (Margin and Collateral) (the "**Professional Client (with Security Provisions) Agreement 2011**")

16. Professional Client Agreement (2007 Version), excluding Module G (***Margin and Collateral***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Professional Client (with Title Transfer Provisions) Agreement 2007**")

17. Professional Client Agreement (2009 Version), excluding Module G (***Margin and Collateral***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Professional Client (with Title Transfer Provisions) Agreement 2009**")

18. Professional Client Agreement (2011 Version), excluding Module G (***Margin and Collateral***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Professional Client (with Title Transfer Provisions) Agreement 2011**")

19. Retail Client Agreement (2007 Version) including Module G (Margin and Collateral) (the "**Retail Client (with Security Provisions) Agreement 2007**")

20. Retail Client Agreement (2009 Version) including Module G (Margin and Collateral) (the "**Retail Client (with Security Provisions) Agreement 2009**")

21. Retail Client Agreement (2011 Version) including Module G (Margin and Collateral) (the "**Retail Client (with Security Provisions) Agreement 2011**")

22. Retail Client Agreement (2007 Version), excluding Module G (***Margin and Collateral***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Retail Client (with Title Transfer Provisions) Agreement 2007**")

23. Retail Client Agreement (2009 Version), excluding Module G (***Margin and Collateral***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Retail Client (with Title Transfer Provisions) Agreement 2009**")

24. Retail Client Agreement (2011 Version), excluding Module G (***Margin and Collateral***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Retail Client (with Title Transfer Provisions) Agreement 2011**")

25. Eligible Counterparty Agreement (2007 Version) including Module G (***Margin***) (the "**Eligible Counterparty (with Security Provisions) Agreement 2007**")

26. Eligible Counterparty Agreement (2009 Version) including Module G (***Margin***) (the "**Eligible Counterparty (with Security Provisions) Agreement 2009**")

27. Eligible Counterparty Agreement (2011 Version) including Module G (***Margin***) (the "**Eligible Counterparty (with Security Provisions) Agreement 2011**")

28. Eligible Counterparty Agreement (2007 Version) excluding Module G (***Margin***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Eligible Counterparty (with Title Transfer Provisions) Agreement 2007**")

29. Eligible Counterparty Agreement (2009 Version) excluding Module G (***Margin***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Eligible Counterparty (with Title Transfer Provisions) Agreement 2009**")

30. Eligible Counterparty Agreement (2011 Version) excluding Module G (***Margin***) but incorporating the Title Transfer Securities and Physical Collateral Annex to the Netting Module (2007 or 2011 Version) (the "**Eligible Counterparty (with Title Transfer Provisions) Agreement 2011**")

Where an FOA Published Form Agreement expressly contemplates the election of certain variables and alternatives, the Agreements listed above shall be deemed to include any such document in respect of which the parties have made such expressly contemplated elections (and have made any deletions required by such elections, where such deletions are expressly contemplated in the event of such election by the applicable FOA Published Form Agreement), provided that any election made does not constitute an Adverse Amendment.

Each of the Agreements listed at items 13 to 30 of this Annex 1 may be deemed to

include FOA Netting Agreements identical to the relevant FOA Published Form Agreement, save for the substitution of Two Way Clauses in place of the equivalent terms in the FOA Published Form Agreement, in which case references to the Insolvency Events of Default and FOA Netting Provision in respect of such FOA Netting Agreements shall mean the Insolvency Events of Default and FOA Netting Provision in relation to the Two Way Clauses.

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ANNEX 2
List of Transactions

The following groups of Transactions may be entered into under the FOA Netting Agreements or Clearing Agreements:

(A) (Futures and options and other transactions) Transactions as defined in the FOA Netting Agreements or Clearing Agreements:

(i) a contract made on an exchange or pursuant to the rules of an exchange;

(ii) a contract subject to the rules of an exchange; or

(iii) a contract which would (but in terms of maturity only) be a contract made on, or subject to the rules of, an exchange and which, at the appropriate time, is to be submitted for clearing as a contract made on, or subject to the rules of, an exchange,

in any of cases (i), (ii) and (iii) being a future, option, contract for difference, spot or forward contract of any kind in relation to any commodity, metal, financial instrument (including any security), currency, interest rate, index or any combination thereof; or

(iv) a transaction which is back-to-back with any transaction within paragraph (i), (ii) or (iii) of this definition, or

(v) any other Transaction which the parties agree to be a Transaction;

(B) (fixed income securities) Transactions relating to a fixed income security or under which delivery of a fixed income security is contemplated upon its formation;

(C) (equities) Transactions relating to an equity or under which delivery of an equity is contemplated upon its formation;

(D) (commodities) Transactions relating to, or under the terms of which delivery is contemplated, of any base metal, precious metal or agricultural product.

(E) (OTC derivatives) Transactions which fall within paragraphs (4) to (10) of Section C of Annex 1 to Directive 2004/39/EC, including (but not limited to) interest rate swaps, credit default swaps, derivatives on foreign exchange,

and equity derivatives, provided that, where the Transaction is subject to the Terms of a Clearing Agreement, the Transaction (or a transaction which is back-to-back with the Transaction) is eligible to be cleared by a central counterparty.

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ANNEX 3
DEFINITIONS RELATING TO THE AGREEMENTS

"**Addendum Inconsistency Provision**" means (subject to any selections or amendments required or permitted to be made on the face of the ISDA/FOA Clearing Addendum) Clause 1(b) (i) of the ISDA/FOA Clearing Addendum.

"**Addendum Netting Provision**" means (subject to any selections or amendments required or permitted to be made on the face of the ISDA/FOA Clearing Addendum):

(a) Clause 8(b) (*Clearing Member Events*), 8(c) (CCP Default) and 8(d) (*Hierarchy of Events*) of the ISDA/FOA Clearing Addendum; or

(b) any modified version of such clauses provided that it includes at least those parts of paragraph 6 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow,

together with the defined terms required properly to construe such Clauses.

"**Addendum Set-Off Provision**" means (subject to any selections or amendments required or permitted to be made on the face of the ISDA/FOA Clearing Addendum):

(a) Clause 8(e) (*Set-Off*) of the ISDA/FOA Clearing Addendum, where constituted as part of a Clearing Agreement; or

(b) any modified version of such clause provided that it includes at least those parts of paragraph 8 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow,

together with the defined terms required properly to construe such Clause.

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"**Adverse Amendments**" means (a) any amendment to a Core Provision and/or (b) any other provision in an agreement that may invalidate, adversely affect, modify, amend, supersede, conflict or be inconsistent with, provide an alternative to, override, compromise or fetter the operation, implementation, enforceability or effectiveness of a Core Provision (in each case in (a) and (b) above, excepting any Non-material Amendment).

"**Clearing Agreement**" means an agreement:

(a) on the terms of the FOA Netting Agreement when used (i) in conjunction with the FOA Clearing Module and/or the ISDA/FOA Clearing Addendum, or (ii) in conjunction with a Clearing Module Netting Provision and/or an Addendum Netting Provision and with or without a Clearing Module Set-Off Provision and/or an Addendum Set-Off Provision;

(b) which is governed by the law of England and Wales; and

(c) which contains an Addendum Inconsistency Provision, a Clearing Module Inconsistency Provision, or another provision with equivalent effect to either of them.

"**Clearing Module Inconsistency Provision**" means (subject to any selections or amendments required or permitted to be made on the face of the FOA Clearing Module) Clause 1.2.1 of the FOA Clearing Module.

"**Clearing Module Netting Provision**" means (subject to any selections or amendments required or permitted to be made on the face of the FOA Clearing Module):

(a) Clause 5.2 (*Firm Events*), 5.3 (*CCP Default*) and 5.4 (*Hierarchy of Events*) of the FOA Clearing Module; or

(b) any modified version of such clauses provided that it includes at least those parts of paragraph 6 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow,

together with the defined terms required properly to construe such Clauses.

"**Clearing Module Set-Off Provision**" means (subject to any selections or amendments required or permitted to be made on the face of the FOA Clearing Module):

(a) Clause 5.5 (*Set-Off*) of the FOA Clearing Module; or

(b) any modified version of such clause provided that it includes at least those parts of paragraph 7 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow,

together with the defined terms required properly to construe such Clause.

"**Client**" means, in relation to an FOA Netting Agreement or a Clearing Agreement, the Firm's or, as the case may be, Clearing Member's counterparty under the relevant FOA Netting Agreement or Clearing Agreement.

"**Core Provision**" means those parts of the clauses or provisions specified below in relation to a paragraph of this opinion letter (and any equivalent paragraph in any Schedule to this opinion letter), which are highlighted in Annex 4:

(a) for the purposes of paragraph 3.3 (*Enforceability of FOA Netting Provision*) and 3.6 (*Use of FOA Clearing Module or ISDA/FOA Clearing Addendum not detrimental to FOA Netting Provision*), the Insolvency Events of Default Clause and the FOA Netting Provision;

(b) for the purposes of paragraph 3.4 (*Enforceability of the Clearing Module Netting Provision*), the Clearing Module Netting Provision together with the defined terms "Aggregate Transaction Value", "Firm/CCP Transaction Value" and "Relevant Collateral Value";

(c) for the purposes of paragraph 3.5 (*Enforceability of the Addendum Netting Provision*), the Addendum Netting Provision together with the defined terms "Aggregate Transaction Value", "CM/CCP Transaction Value" and "Relevant Collateral Value";

(d) for the purposes of paragraph 3.7.1, the Insolvency Events of Default Clause, the FOA Netting Provision and either or both of the General Set-off Clause and the Margin Cash Set-off Clause;

(e) for the purposes of paragraph 3.7.2, the Insolvency Events of Default Clause, the FOA Netting Provision, either or both of the General Set-off Clause and the Margin Cash Set-off Clause, and the Clearing Module Set-Off Provision and/or the Addendum Set-Off Provision;

(f) for the purposes of paragraph 3.8.1, the Clearing Module Netting Provision together with the defined terms "Aggregate Transaction Value", "Firm/CCP

Transaction Value" and "Relevant Collateral Value", and the Clearing Module Set-Off Provision;

(g) for the purposes of paragraph 3.8.2, the Clearing Module Netting Provision together with the defined terms "Aggregate Transaction Value", "Firm/CCP Transaction Value" and "Relevant Collateral Value", the Clearing Module Set-Off Provision and the FOA Set-Off Provision;

(h) for the purposes of paragraph 3.9 (*Set-Off under a Clearing Agreement with Addendum Set-Off Provision*), the Addendum Netting Provision together with the defined terms "Aggregate Transaction Value", "CM/CCP Transaction Value" and "Relevant Collateral Value", and the Addendum Set-Off Provision;

(i) for the purposes of paragraph 3.10.1, (i) in relation to an FOA Netting Agreement, the Insolvency Events of Default Clause, the FOA Netting Provision and the Title Transfer Provisions; and (ii) in relation to a Clearing Agreement, the Clearing Module Netting Provision together with the defined terms "Aggregate Transaction Value", "Firm/CCP Transaction Value" and "Relevant Collateral Value" or, as the case may be, the Addendum Netting Provision together with the defined terms "Aggregate Transaction Value", "CM/CCP Transaction Value" and "Relevant Collateral Value", and the Title Transfer Provisions; and

(j) for the purposes of paragraphs 3.10.3 and 3.10.4, the Title Transfer Provisions;

in each case, incorporated into an FOA Netting Agreement or a Clearing Agreement together with any defined terms required properly to construe such provisions, in such a way as to preserve the essential sense and effect of the highlighted parts.

References to "**Core Provisions**" include Core Provisions that have been modified by Non-material Amendments.

"**Defaulting Party**" includes, in relation to the One-Way Versions, the Party in respect of which an Event of Default entitles the Non-Defaulting Party to exercise rights under the FOA Netting Provision.

"**Eligible Counterparty Agreements**" means each of the Eligible Counterparty (with Security Provisions) Agreement 2007, the Eligible Counterparty (with Title Transfer Provisions) Agreement 2007, the Eligible Counterparty (with Security Provisions) Agreement 2009, the Eligible Counterparty (with Title Transfer Provisions)

Agreement 2009, the Eligible Counterparty (with Security Provisions) Agreement 2011 or the Eligible Counterparty (with Title Transfer Provisions) Agreement 2011 (each as listed and defined at Annex 1).

"**Firm**" means, in relation to an FOA Netting Agreement or a Clearing Agreement which includes an FOA Clearing Module, the Party providing the services under the relevant FOA Netting Agreement or Clearing Agreement which includes an FOA Clearing Module.

"**FOA Clearing Module**" means the FOA Client Cleared Derivatives Module as first published on 9 October 2013 or any subsequent published version up to the date of this opinion letter.

"**FOA Netting Agreement**" means an agreement:

(a) on the terms of the forms specified in Annex 1 to this opinion letter or which has broadly similar function to any of them, when not used in conjunction with the FOA Clearing Module and/or the ISDA/FOA Clearing Addendum and/or a Clearing Module Netting Provision and/or an Addendum Netting Provision;

(b) which is governed by the law of England and Wales; and

(c) which contains the Insolvency Events of Default Clause and the FOA Netting Provision, with or without the FOA Set-Off Provision, and with or without the Title Transfer Provisions, with no Adverse Amendments.

"**FOA Netting Agreements (with Title Transfer Provisions)**" means each of the Professional Client (with Title Transfer Provisions) Agreement 2007, the Professional Client (with Title Transfer Provisions) Agreement 2009, the Professional Client (with Title Transfer Provisions) Agreement 2011, the Retail Client (with Title Transfer Provisions) Agreement 2007, the Retail Client (with Title Transfer Provisions) Agreement 2009, the Retail Client (with Title Transfer Provisions) Agreement 2011, the Eligible Counterparty (with Title Transfer Provisions) Agreement 2007, the Eligible Counterparty (with Title Transfer Provisions) Agreement 2009 and the Eligible Counterparty (with Title Transfer Provisions) Agreement 2011 (each as listed and defined at Annex 1) or an FOA Netting Agreement which has broadly similar function to any of the foregoing.

"**FOA Netting Provision**" means (in each case subject to any selections or amendments required or permitted to be made on the face of the document in the

relevant form referred to in Annex 1):

(a) in relation to the terms of the Long Form One-Way Clauses 2007 and the Long Form Two-Way Clauses, Clause 2.2 (***Liquidation Date***), Clause 2.4 (***Calculation of Liquidation Amount***) and Clause 2.5 (***Payer***);

(b) in relation to the terms of the Short Form One-Way Clauses and the Short Form Two-Way Clauses, Clause 2.1 (***Liquidation Date***), Clause 2.3 (***Calculation of Liquidation Amount***) and Clause 2.4 (***Payer***);

(c) in relation to the terms of the Master Netting Agreements, Clause 4.2, Clause 4.4 and Clause 4.5;

(d) in relation to the terms of the Eligible Counterparty Agreements, Clause 10.1 (***Liquidation Date***), Clause 10.3 (***Calculation of Liquidation Amount***) and Clause 10.4 (***Payer***);

(e) in relation to the terms of the Retail Client Agreements, Clause 11.2 (***Liquidation Date***), Clause 11.4 (***Calculation of Liquidation Amount***) and Clause 11.5 (***Payer***);

(f) in relation to the terms of the Professional Client Agreements, Clause 11.2 (***Liquidation Date***), Clause 11.4 (***Calculation of Liquidation Amount***) and Clause 11.5 (***Payer***); or

(d) any modified version of such clauses provided that it includes at least those parts of paragraph 1 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow.

"**FOA Published Form Agreement**" means a document listed at Annex 1 in the form published by the Futures and Options Association on its website as at the date of this opinion.

"**FOA Set-off Provisions**" means:

(a) the "**General Set-off Clause**", being:

(i) in the case of Agreements in the form of the Professional Client Agreement (with Security Provisions) 2007 and Professional Client Agreement (with Security Provisions) 2009, clause 15.11 (***Set-off***);

(ii) in the case of Agreements in the form of the Professional Client Agreement (with Security Provisions) 2011, clause 15.13 (***Set-off***);

(iii) in the case of Agreements in the form of the Retail Client Agreement (with Security Provisions) 2007 and the Retail Client Agreement (with Security Provisions) 2009, clause 15.12 (***Set-off***);

(iv) in the case of Agreements in the form of the Retail Client Agreement (with Security Provisions) 2011, clause 15.13 (***Set-off***);

(v) in the case of Agreements in the form of the Eligible Counterparty Agreement (with Security Provisions) 2007 and the Eligible Counterparty Agreement (with Security Provisions) 2009, clause 14.8 (***Set-off***);

(vi) in the case of Agreements in the form of the Eligible Counterparty Agreement (with Security Provisions) 2011, clause 14.10 (***Set-off***);

(vii) in the case of the Agreements in the form of One-Way Master Netting Agreement (1997 version), clause 5 (***Set-Off***);

(viii) in the case of the Agreements in the form of Two-Way Master Netting Agreement (1997 version), clause 5 (***Set-Off***); or

(ix) any modified version of such clauses provided that it includes at least those parts of paragraph 2 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow; and/or

(b) the "**Margin Cash Set-off Clause**", being:

(i) in the case of Agreements in the form of the Professional Client Agreement (with Security Provisions) 2007 and the Professional Client Agreement (with Security Provisions) 2009, clause 8.5 (***Set-off on default***);

(ii) in the case of Agreements in the form of the Professional Client Agreement (with Security Provisions) 2011, clause 8.4 (***Set-off upon default or termination***);

(iii) in the case of Agreements in the form of the Retail Client Agreement (with Security Provisions) 2007 and the Retail Client Agreement (with Security Provisions) 2009, clause 8.7 (***Set-off on***

default),

(iv) in the case of Agreements in the form of the Retail Client Agreement (with Security Provisions) 2011, clause 8.6 (***Set-off upon default or termination***);

(v) in the case of Agreements in the form of the Eligible Counterparty Agreement (with Security Provisions) 2007 and the Eligible Counterparty Agreement (with Security Provisions) 2009, clause 7.5 (***Set-off on default***);

(vi) in the case of Agreements in the form of the Eligible Counterparty Agreement (with Security Provisions) 2011, clause 7.4 (***Set-off upon default or termination***); or

(vii) any modified version of such clauses provided that it includes at least those parts of paragraph 3 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow.

"**Insolvency Events of Default Clause**" means (in each case subject to any selections or amendments required or permitted to be made on the face of the document in the relevant form referred to in Annex 1):

(a) where the FOA Member's counterparty is not a natural person:

(i) in relation to the terms of the Long-Form Two-Way Clauses and the Long Form One-Way Clauses 2007, Clause 1 (b) to (d) (inclusive) and Clause 1 (h) and (i);

(ii) in relation to the terms of the Short Form One-Way Clauses and Short Form Two-Way Clauses, Clauses 1.1 (a) to (c) (inclusive);

(iii) in relation to the terms of the Master Netting Agreements, Clause 4.1 (i) to (iii) (inclusive);

(iv) in relation to the terms of the Eligible Counterparty Agreements, Clause 9.1 (a) to (c) (inclusive);

(v) in relation to the terms of the Retail Client Agreements and the Professional Client Agreements, Clause 10.1(a) to (c) (inclusive); or

(vi) provided that any modification of such clauses include at least those

parts of paragraph 4(a) of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow; and

(b) where the FOA Member's counterparty is a natural person:

(i) in relation to the terms of the Long-Form Two-Way Clauses and the Long Form One-Way Clauses 2007, Clause 1 (b) to (d) (inclusive) and Clause 1 (h) and (i);

(ii) in relation to the terms of the Master Netting Agreements, Clause 4.1 (i) and (iv);

(iii) in relation to the terms of the Retail Client Agreements and the Professional Client Agreements, Clause 10.1(a) and (d); or

(iv) any modified version of such clauses provided that it includes at least those parts of paragraph 4(b) of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow.

"**ISDA/FOA Clearing Addendum**" means the ISDA/FOA Client Cleared OTC Derivatives Addendum as first published on 11 June 2013, or any subsequent published versions up to the date of this opinion letter.

"**Limited Recourse Provision**" means Clause 8.1 of the FOA Clearing Module or Clause 15(a) of the ISDA/FOA Clearing Module.

"**Long Form Two-Way Clauses**" means each of the Long-Form Two-Way Clauses 2007, the Long-Form Two-Way Clauses 2009 and the Long-Form Two-Way Clauses 2011 (each as listed and defined at Annex 1).

"**Master Netting Agreements**" means each of the One-Way Master Netting Agreement 1997 and the Two-Way Master Netting Agreement 1997 (each as listed and defined at Annex 1).

"**Non-Defaulting Party**" includes, in relation to the One-Way Versions, the Party entitled to exercise rights under the FOA Netting Provision.

"**Non-material Amendment**" means an amendment having the effect of one of the amendments set out at Annex 4.

"**One-Way Versions**" means the Long Form One-Way Clauses 2007, the Short Form One-Way Clauses, the One-Way Master Netting Agreement 1997, and the FOA

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Netting Provision as published in the Retail Client Agreements and the Professional Client Agreements in each case in the form of an FOA Published Form Agreement.

"**Party**" means a party to an FOA Netting Agreement or a Clearing Agreement.

"**Professional Client Agreements**" means each of the Professional Client (with Security Provisions) Agreement 2007, the Professional Client (with Title Transfer Provisions) Agreement 2007, the Professional Client (with Security Provisions) Agreement 2009, the Professional Client (with Title Transfer Provisions) Agreement 2009, the Professional Client (with Security Provisions) Agreement 2011 or the Professional Client (with Title Transfer Provisions) Agreement 2011 (each as listed and defined at Annex 1).

"**Rehypothecation Clause**" means:

(a) in the case of Agreements in the form of the Professional Client Agreement 2011, clause 8.13 (***Rehypothecation***);

(b) in the case of Agreements in the form of the Retail Client Agreement 2011, clause 8.15 (***Rehypothecation***);

(c) in the case of Agreements in the form of the Eligible Counterparty Agreement 2011, clause 7.13 (***Rehypothecation***); or

(d) any modified version of such clauses provided that it includes at least those parts of paragraph 4 of Part 3 (*Security Interest Provisions*) of Annex 4 which are highlighted in yellow.

"**Retail Client Agreements**" means each of the Retail Client (with Security Provisions) Agreement 2007, the Retail Client (with Title Transfer Provisions) Agreement 2007, the Retail Client (with Security Provisions) Agreement 2009, the Retail Client (with Title Transfer Provisions) Agreement 2009, the Retail Client (with Security Provisions) Agreement 2011 or the Retail Client (with Title Transfer Provisions) Agreement 2011 (each as listed and defined at Annex 1).

"**Non-Cash Security Interest Provisions**" means:

(a) the "**Non-Cash Security Interest Clause**", being:

(i) in the case of Agreements in the form of the Professional Client Agreement 2007, clause 8.6 (***Security interest***);

(ii) in the case of Agreements in the form of the Professional Client Agreement 2009, clause 8.6 (***Security interest***);

(iii) in the case of Agreements in the form of the Professional Client Agreement 2011, clause 8.7 (***Security interest***);

(iv) in the case of Agreements in the form of the Retail Client Agreement 2007, clause 8.8 (***Security interest***);

(v) in the case of Agreements in the form of the Retail Client Agreement 2009, clause 8.8 (***Security interest***);

(vi) in the case of Agreements in the form of the Retail Client Agreement 2011, clause 8.9 (***Security interest***);

(vii) in the case of Agreements in the form of the Eligible Counterparty Agreement 2007, clause 7.6 (***Security interest***);

(viii) in the case of Agreements in the form of the Eligible Counterparty Agreement 2009, clause 7.6 (***Security interest***);

(ix) in the case of Agreements in the form of the Eligible Counterparty Agreement 2011, clause 7.7 (***Security interest***); or

(x) any modified version of such clauses provided that it includes at least those parts of paragraph 1 of Part 3 (*Security Interest Provisions*) of Annex 4 which are highlighted in yellow;

(b) the "**Power of Sale Clause**", being:

(i) in the case of Agreements in the form of the Professional Client Agreement 2007, clause 8.11 (***Power of sale***);

(ii) in the case of Agreements in the form of the Professional Client Agreement 2009, clause 8.11 (***Power of sale***);

(iii) in the case of Agreements in the form of the Professional Client Agreement 2011, clause 8.11 (***Power of sale***);

(iv) in the case of Agreements in the form of the Retail Client Agreement 2007, clause 8.13 (***Power of sale***);

(v) in the case of Agreements in the form of the Retail Client Agreement

2009, clause 8.13 (***Power of sale***);

(vi) in the case of Agreements in the form of the Retail Client Agreement 2011, clause 8.13 (***Power of sale***);

(vii) in the case of Agreements in the form of the Eligible Counterparty Agreement 2007, clause 7.11 (***Power of sale***);

(viii) in the case of Agreements in the form of the Eligible Counterparty Agreement 2009, clause 7.11 (***Power of sale***);

(ix) in the case of Agreements in the form of the Eligible Counterparty Agreement 2011, clause 7.11 (***Power of sale***); or

(x) any modified version of such clauses provided that it includes at least those parts of paragraph 2 of Part 3 (*Security Interest Provisions*) of Annex 4 which are highlighted in yellow; and

"**Client Money Additional Security Clause**" means:

(i) in the case of Agreements in the form of the Professional Client Agreement 2007, clause 7.8 (***Additional security***) at module F Option 4 (where incorporated into such Agreement);

(ii) in the case of Agreements in the form of the Professional Client Agreement 2009, clause 7.9 (***Additional security***) at module F Option 1 (where incorporated into such Agreement);

(iii) in the case of Agreements in the form of the Professional Client Agreement 2011, clause 7.9 (***Additional security***) at module F Option 1 (where incorporated into such Agreement);

(iv) in the case of Agreements in the form of the Retail Client Agreement 2007, clause 7.8 (***Additional security***) at module F Option 4 (where incorporated into such Agreement);

(v) in the case of Agreements in the form of the Retail Client Agreement 2009, clause 7.9 (***Additional security***) at module F Option 1 (where incorporated into such Agreement);

(vi) in the case of Agreements in the form of the Retail Client Agreement 2011, clause 7.9 (***Additional security***) at module F Option 1 (where

incorporated into such Agreement);

(vii) in the case of Agreements in the form of the Eligible Counterparty Agreement 2007, clause 6.8 (***Additional security***) at module F Option 4 (where incorporated into such Agreement);

(viii) in the case of Agreements in the form of the Eligible Counterparty Agreement 2009, clause 6.9 (***Additional security***) at module F Option 1 (where incorporated into such Agreement);

(ix) in the case of Agreements in the form of the Eligible Counterparty Agreement 2011, clause 6.9 (***Additional security***) at module F Option 1 (where incorporated into such Agreement); or

(x) any modified version of such clauses provided that it includes at least those parts of paragraph 3 of Part 3 (*Security Interest Provisions*) of Annex 4 which are highlighted in yellow.

"**Short Form One Way-Clauses**" means each of the Short-Form One-Way Clauses 2007, the Short-Form One-Way Clauses 2009 and the Short-Form One-Way Clauses 2011 (each as listed and defined at Annex 1).

"**Short Form Two Way-Clauses**" means each of the Short-Form Two-Way Clauses 2007, the Short-Form Two-Way Clauses 2009 and the Short-Form Two-Way Clauses 2011 (each as listed and defined at Annex 1).

"**Title Transfer Provisions**" means (in each case subject to any selections or amendments required or permitted to be made on the face of the document in the relevant form referred to in Annex 1):

(a) clauses 5 and 7.2 of the Title Transfer and Physical Collateral Annex to the Netting Module (2007 or 2011 Version); or

(b) any modified version of such clauses provided that it includes at least those parts of paragraph 5 of Part 1 (*Core Provisions*) of Annex 4 which are highlighted in yellow.

"**Two Way Clauses**" means each of the Long-Form Two Way Clauses and the Short-Form Two Way Clauses.

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ANNEX 4

PART 1
CORE PROVISIONS

For the purposes of the definition of Core Provisions in Annex 3, the wording highlighted in yellow below shall constitute the relevant Core Provision:

1. **FOA Netting Provision:**

a) "**Liquidation date:** Subject to the following sub-clause, at any time following the occurrence of an Event of Default in relation to a party, then the other party (the "**Non-Defaulting Party**") may, by notice to the party in default (the "**Defaulting Party**"), specify a date (the "**Liquidation Date**") for the termination and liquidation of Netting Transactions in accordance with this clause.

b) **Calculation of Liquidation Amount:** Upon the occurrence of a Liquidation Date:

i. neither party shall be obliged to make any further payments or deliveries under any Netting Transactions which would, but for this clause, have fallen due for performance on or after the Liquidation Date and such obligations shall be satisfied by settlement (whether by payment, set-off or otherwise) of the Liquidation Amount;

ii. the Non-Defaulting Party shall as soon as reasonably practicable determine (discounting if appropriate), in respect of each Netting Transaction referred to in paragraph (a), the total cost, loss or, as the case may be, gain, in each case expressed in the Base Currency specified by the Non-Defaulting Party as such in the Individually Agreed Terms Schedule as a result of the termination, pursuant to this Agreement, of each payment or delivery which would otherwise have been required to be made under such Netting Transaction; and

iii. the Non-Defaulting Party shall treat each such cost or loss to it as a positive amount and each such gain by it as a negative amount and aggregate all such amounts to produce a single, net positive or negative amount, denominated in the Non-Defaulting Party's Base Currency (the "**Liquidation Amount**").

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c) **Payer:** If the Liquidation Amount is a positive amount, the Defaulting Party shall pay it to the Non-Defaulting Party and if it is a negative amount, the Non-Defaulting Party shall pay it to the Defaulting Party. The Non-Defaulting Party shall notify the Defaulting Party of the Liquidation Amount, and by which Party it is payable, immediately after the calculation of such amount."

2. General Set-Off Clause:

"**Set-off:** Without prejudice to any other rights to which we may be entitled, we may at any time and without notice to you set off any amount (whether actual or contingent, present or future) owed by you to us against any amount (whether actual or contingent, present or future) owed by us to you. For these purposes, we may ascribe a commercially reasonable value to any amount which is contingent or which for any other reason is unascertained."

3. Margin Cash Set-Off Clause:

"**Set-off upon default or termination:** If there is an Event of Default or this Agreement terminates, we may set off the balance of cash margin owed by us to you against your Obligations (as reasonably valued by us) as they become due and payable to us and we shall be obliged to pay to you (or entitled to claim from you, as appropriate) only the net balance after all Obligations have been taken into account. [The net amount, if any, payable between us following such set-off, shall take into account the Liquidation Amount payable under the Netting Module of this Agreement.]"

4. Insolvency Events of Default Clause:

a) In the case of a Counterparty that is not a natural person:

"The following shall constitute Events of Default:

i. a party fails to make any payment when due under or to make delivery of any property when due under, or to observe or perform any other provision of this Agreement, [and such failure continues for [one/two] Business Day[s] after notice of non-performance has been given by the Non-Defaulting Party to the Defaulting Party];

ii. a party commences a voluntary case or other procedure seeking or proposing liquidation, reorganisation, moratorium, or other similar relief with respect to itself or to its debts under any bankruptcy, insolvency, regulatory, or similar law or seeking the appointment of a trustee, receiver, liquidator, conservator, administrator, custodian,

examiner or other similar official (each a "**Custodian**") of it or any substantial part of its assets, or takes any corporate action to authorise any of the foregoing;

iii. an involuntary case or other procedure is commenced against a party seeking or proposing liquidation, reorganisation, or moratorium, or other similar relief with respect to it or its debts under any bankruptcy, insolvency, regulatory, or similar law or seeking the appointment of a Custodian of it or any substantial part of its assets."

b) In the case of a Counterparty that is a natural person:

"The following shall constitute Events of Default:

i. a party fails to make any payment when due under or to make delivery of any property when due under, or to observe or perform any other provision of this Agreement, [and such failure continues for [one/two] Business Day[s] after notice of non-performance has been given by the Non-Defaulting Party to the Defaulting Party];

ii. you die, become of unsound mind, are unable to pay your debts as they fall due or are bankrupt or insolvent, as defined under any bankruptcy or insolvency law applicable to you; or any indebtedness of yours is not paid on the due date therefore, or becomes capable at any time of being declared, due and payable under agreements or instruments evidencing such indebtedness before it would otherwise have been due and payable, or any suit, action or other proceedings relating to this Agreement are commenced for any execution, any attachment or garnishment, or distress against, or an encumbrancer takes possession of, the whole or any part of your property, undertaking or assets (tangible and intangible)."

5. Title Transfer Provisions:

a) "**Default:** If a Liquidation Date is specified or deemed to occur as a result of an Event of Default, the Default Margin Amount as at that date *will* be deemed to be [a gain (if we are the Non-Defaulting Party) or a cost (if you are the Non-Defaulting Party)] [a gain by us] for the purposes of calculating the Liquidation Amount. For this purpose, "**Default Margin Amount**" means the amount, calculated in the Base Currency of the aggregate value as at the relevant Liquidation Date (as determined by us) of the Transferred Margin.

b) **Clean title:** Each party agrees that all right, title and interest in and to any Acceptable Margin, Equivalent Margin, Equivalent Dividends or Interest

which it Transfers to the other party shall vest in the recipient free and clear of any security interest, lien, claims, charges, encumbrance or other restriction. Notwithstanding the use of terms such as "Margin" which are used to reflect terminology used in the market for such transactions, nothing in these provisions is intended to create or does create in favour of either party a mortgage, charge, lien, pledge, encumbrance or other security interest in any Acceptable Margin, Equivalent Margin, Equivalent Dividends or Interest Transferred hereunder."

6. Clearing Module Netting Provision / Addendum Netting Provision:

a) [Firm Trigger Event/CM Trigger Event]

Upon the occurrence of a [Firm Trigger Event/CM Trigger Event], the Client Transactions in the relevant Cleared Transaction Set will, except to the extent otherwise stated in the [Core Provisions of the] relevant Rule Set, be dealt with as set out below:

(a) each Client Transaction in the relevant Cleared Transaction Set will automatically terminate [upon the occurrence of a Firm Trigger Event] [at the same time as the related CM/CCP Transaction is terminated or Transferred] and, following such termination, no further payments or deliveries in respect of such Client Transaction [as specified in the Confirm] or any default interest, howsoever described, on such payment obligations will be required to be made but without prejudice to the other provisions of the Clearing Agreement, and the amount payable following such termination will be the Cleared Set Termination Amount determined pursuant to this [Clause 5.22 Section 8(b)(ii)];

(b) the value of each such terminated Client Transaction for the purposes of calculating the applicable Cleared Set Termination Amount and Aggregate Transaction Values will be equal to the relevant [Firm/CM]/CCP Transaction Value or the relevant part thereof;

(c) the applicable Cleared Set Termination Amount will be determined by Client on, or as soon as reasonably practicable after, (x) if there were no outstanding Client Transactions immediately prior to the occurrence of a [Firm/CM] Trigger Event, the date on which the [Firm/CM] Trigger Event occurred, or (y) if there were outstanding Client Transactions immediately prior to the occurrence of a [Firm/CM] Trigger Event, the day on which the relevant Client Transactions [had all been/were] terminated (in either case, provided that, if [Firm/Clearing Member] gives notice to Client requiring it to

determine such amount and Client does not do so within two Business Days of such notice being effectively delivered, [Firm/Clearing Member] may determine the applicable Cleared Set Termination Amount) and, in either case, will be an amount equal to the sum, but without duplication, of (A) the Aggregate Transaction Value, (B) any amount which became payable, or which would have become payable but for a condition precedent not being satisfied, in respect of any such Client Transaction on or prior to the termination of such transactions but which remains unpaid at the time of such termination, together with interest on such amount in the same currency as such amount for the period from, and including, the original due date for payment to, but excluding, the date of termination, if applicable (expressed as a positive amount if such unpaid amount is due from [Firm/Clearing Member] to Client and as a negative amount if such unpaid amount is due from Client to [Firm/Clearing Member]), (C) an amount [(which may be zero)] equal to the Relevant Collateral Value in respect of the relevant Client Transactions and (D) any other amount attributable to the relevant Client Transactions under the Clearing Agreement[or any related Collateral Agreement], pro-rated where necessary if such amount can be partially [attributed] [attributable] to transactions other than the relevant Client Transactions, which was payable but unpaid at the time of termination and is not otherwise included [Clauses 5.2.2(c)(4) to 5.2.2(c)(C)] [Sections 8(b)(ii)(3)(A) to 8(b)(ii)(3)(C)], together with interest on such amount in the same currency as such amount for the period from, and including, the original due date for payment to, but excluding, the date of termination, if applicable (expressed as a positive amount if such unpaid amount is due from [Firm/Clearing Member] to Client and as a negative amount if such unpaid amount is due from Client to [Firm/Clearing Member]);

(d) if a Cleared Set Termination Amount is a positive number, it will be due from [Firm/Clearing Member] to Client and if a Cleared Set Termination Amount is a negative number, the absolute value of the Cleared Set Termination Amount will be due from Client to [Firm/Clearing Member], and in each case will be payable in accordance with this [Module/Addendum].

b) CCP Default

Upon the occurrence of a CCP Default, the Client Transactions in the relevant Cleared Transaction Set will, except to the extent otherwise stated in the [Core Provisions of the relevant] Rule Set, be dealt with as set out below:

1. each Client Transaction in the relevant Cleared Transaction Set will

automatically terminate at the same time as the related [Firm/CM]/CCP Transaction and following such termination no further payments or deliveries in respect of such Client Transaction[as specified in the Confirm] or any default interest, howsoever described, on such payment obligations will be required to be made but without prejudice to the other provisions of the Clearing Agreement, and the amount payable following such termination will be the Cleared Set Termination Amount determined pursuant to this [Clause 5.3 Section 8(c)];

2. the value of each such terminated Client Transaction for the purposes of calculating the applicable Cleared Set Termination Amount and Aggregate Transaction Values will be equal to the relevant [Firm/CM]/CCP Transaction Value or relevant part thereof;

3. the applicable Cleared Set Termination Amount will be determined by [Firm/Clearing Member] on, or as soon as reasonably practicable after, (x) if there were no outstanding Client Transactions immediately prior to the occurrence of a CCP Default, the date on which the CCP Default occurred, or (y) if there were outstanding Client Transactions immediately prior to the occurrence of a CCP Default, the day on which the relevant Client Transactions had all been terminated and, in either case, will be an amount equal to the sum, but without duplication, of (1) the Aggregate Transaction Value, (2) any amount which became payable, or which would have become payable but for a condition precedent not being satisfied, in respect of any such Client Transaction on or prior to the termination of such transactions but which remains unpaid at the time of such termination, together with interest on such amount in the same currency as such amount for the period from, and including, the original due date for payment to, but excluding, the date of termination, if applicable (expressed as a positive amount if such unpaid amount is due from [Firm/Clearing Member] to Client and as a negative amount if such unpaid amount is due from Client to [Firm/Clearing Member]), (3) an amount [(which may be zero)] equal to the Relevant Collateral Value in respect of the relevant Client Transactions and (4) any other amount attributable to the relevant Client Transactions under the Clearing Agreement[and any related Collateral Agreement], pro-rated where necessary if such amount can be partially [attributable] to transactions other than the relevant Client Transactions, which was payable but unpaid at the time of termination and is not otherwise included in [Clauses 5.3.3(1) to 5.3.3(3)] [Sections 8(c)(iii)(1) to 8(c)(iii)(3)], together with interest on such amount in the same currency as such amount for the period from, and including, the

original due date for payment to, but excluding, the date of termination, if applicable (expressed as a positive amount if such unpaid amount is due from [Firm/Clearing Member] to Client and as a negative amount if such unpaid amount is due from Client to [Firm/Clearing member]);

4. if a Cleared Set Termination Amount is a positive number, it will be due from [Firm/Clearing Member] to Client and if a Cleared Set Termination Amount is a negative number, the absolute value of the Cleared Set Termination Amount will be due from Client to [Firm/Clearing Member], and in each case will be payable, in accordance with this [Module/Addendum].

c) Hierarchy of Events

[If Client Transactions are capable of being terminated pursuant to more than one [Clause/Section], then the [clause/section] in respect of which a party first exercises any right to terminate Client Transactions (or, the [clause/section] pursuant to which Client Transactions are otherwise terminated, if earlier) will prevail for the purposes of the relevant Client Transactions.]

Or

[If Client Transactions are capable of being terminated pursuant to more than one [Clause/Section], then the [clause/section] in respect of which a party first exercises any right to terminate Client Transactions (or, the [clause/section] pursuant to which Client Transactions are otherwise terminated, if earlier) will prevail for the purposes of the relevant Client Transactions.]

Or

[If Client Transactions are capable of being terminated pursuant to more than one [Clause/Section], then the [clause/section] in respect of which a party first exercises any right to terminate Client Transactions (or, the clause pursuant to which Client Transactions are otherwise terminated, if earlier) will prevail for the purposes of the relevant Client Transactions.]

d) Definitions

"**Aggregate Transaction Value**" means, in respect of the termination of Client Transactions of a Cleared Transaction Set, an amount (which may be positive or negative or zero) equal to the aggregate of the [Firm/CM]/CCP Transaction Values for all Client Transactions in the relevant Cleared Transaction Set or, if there is just one [Firm/CM]/CCP Transaction Value in respect of all such Client Transactions, an amount (which may be positive or

negative or zero) equal to such [Firm/CM]/CCP Transaction Value.

"**[Firm/CM]/CCP Transaction Value**" means, in respect of a terminated Client Transaction or a group of terminated Client Transactions, an amount equal to the value that is determined in respect of or otherwise ascribed to the related [Firm/CM]/CCP Transaction or group of related [Firm/CM]/CCP Transactions in accordance with the relevant Rule Set following a [Firm/CM] Trigger Event or CCP Default (to the extent such Rule Set contemplates such a value in the relevant circumstance). If the value determined in respect of or otherwise ascribed to the related [Firm/CM]/CCP Transaction(s) under the relevant Rule Set reflects a positive value for [Firm/Clearing Member] vis-à-vis the Agreed CCP, the value determined in respect of such terminated Client Transaction(s) will reflect a positive value for Client vis-à-vis [Firm/Clearing Member] (and will constitute a positive amount for any determination under this [Module/Addendum]) and, if the value determined in respect of the related terminated [Firm/CCP]/CCP Transaction(s), under the relevant Rule Set reflects a positive value for the relevant Agreed CCP vis-à-vis [Firm/Clearing Member], the value determined in respect of [or otherwise ascribed to] such terminated Client Transaction(s) will reflect a positive value for [Firm/Clearing Member] vis-à-vis Client (and will constitute a negative amount for any determination under this [Module/Addendum]). The value determined in respect of or otherwise ascribed to the related [Firm/CM]/CCP Transaction(s) under the relevant Rule Set may be equal to zero.

"**Relevant Collateral Value**" means, in respect of the termination of Client Transactions in a Cleared Transaction Set, the value (without applying any "haircut" but otherwise as determined in accordance with the [Agreement/Collateral Agreement]) of all collateral that:

is attributable to such Client Transactions;

has been transferred by one party to the other in accordance with the [Agreement/Collateral Agreement or pursuant to Section 10(b)] and has not been returned at the time of such termination or otherwise applied or reduced in accordance with the terms of the [Agreement/relevant Collateral Agreement]; and

is not beneficially owned by, or subject to any encumbrances or any other interest of, the transferring party or of any third person.

The Relevant Collateral Value will constitute a positive amount if the relevant collateral has been transferred by Client to [Firm/Clearing Member] and it or equivalent collateral has not been returned at the time of termination or otherwise applied or reduced in accordance with the terms of the

[Agreement/Collateral Agreement] and a negative amount if the relevant collateral has been transferred by [Firm/Clearing Member] to Client and it or equivalent collateral has not been returned at the time of termination or otherwise applied or reduced in accordance with the terms of the [Agreement/Collateral Agreement].

7. Clearing Module Set-Off Provision

Firm may at any time and without notice to Client, set-off any Available Termination Amount against any amount (whether actual or contingent, present or future) owed by Firm to Client under the Clearing Agreement or otherwise. For these purposes, Firm may ascribe a commercially reasonable value to any amount which is contingent or which for any other reason is unascertained.

This Clause shall apply to the exclusion of all Disapplied Set-off Provisions in so far as they relate to Client Transactions; provided that, nothing in this Clause shall prejudice or affect such Disapplied Set-off Provisions in so far as they relate to transactions other than Client Transactions under the Agreement.

8. Addendum Set-Off Provision

(i) Any Available Termination Amount will, at the option of (A) Client, in the case of an Available Termination Amount due in respect of a CM Trigger Event and without prior notice to Clearing Member, be reduced by its set-off against any other termination amount payable by Clearing Member to Client under the Clearing Agreement at such time ("**CM Other Amounts**"), or (B) either party, in the case of an Available Termination Amount due in respect of a CCP Default, and without prior notice to the other party, be reduced by its set-off against any other termination amount payable by or to X (where "**X**" means, in the case of Section 8(i)(A), Client or, in the case of Section 8(i)(B), the party electing to set off) under the Clearing Agreement at such time ("**EP Other Amounts**" and together with CM Other Amounts, "**Other Amounts**"), provided that in the case of Section 8(i)(A) or Section 8(i)(B), at the time at which X elects to set off, where Clearing Member is X, a CM Trigger Event has not occurred and is not continuing or, where Client is X, an event of default, termination event or other similar event, howsoever described, in respect of Client in the Agreement, has not occurred and is not continuing. To the extent that any Other Amounts are so set off, those Other Amounts will be discharged promptly and in all respects. X will give notice to the other party promptly after effecting any set-off under Section 8(i)(A) or Section 8(i)(B).

(ii) For the purposes of this Section 8(ii):

(A) all or part of the Available Termination Amount or the Other Amounts

(or the relevant portion of such amounts) may be converted by X into the currency in which the other amount is denominated at the rate of exchange at which such party would be able, in good faith and using commercially reasonable procedures, to purchase the relevant amount of such currency;

(B) if any Other Amounts are unascertained, X may in good faith estimate such Other Amounts and set off in respect of the estimate, subject to the relevant party accounting to the other when such Other Amounts are ascertained; and

(C) a "termination amount" may, for the avoidance of doubt, be another Cleared Set Termination Amount or another termination amount due under the Agreement including, in either case, any such amount that has previously been reduced in part by set-off pursuant to this Section 8(e).

(iii) Nothing in this Section 8(e) will be effective to create a charge or other security interest. This Section 8(e) will be without prejudice and in addition to any right of set-off, offset, combination of accounts, lien, right of retention or withholding or similar right or requirement to which Client or Clearing Member is at any time otherwise entitled or subject (whether by operation of law, contract or otherwise), provided that, notwithstanding anything to the contrary in the Clearing Agreement or any related Collateral Agreement, no party may exercise any rights of set-off in respect of Excluded Termination Amounts.

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PART 2
NON-MATERIAL AMENDMENTS

1. Any change to the numbering or order of a provision or provisions or the drafting style thereof (e.g., addressing the other party as "you", "Counterparty", "Party A/Party B", using synonyms, changing the order of the words) provided in each case that the plain English sense and legal effect both of each such provision and of the agreement as a whole (including the integrity of any cross references and usage of defined terms) remains unchanged.

2. Any change to a provision or provisions for the purposes of correct cross-referencing or by defining certain key terms (e.g., party, exchange, currency, defaulting party or non-defaulting party) and using these terms in large caps throughout the agreement provided in each case that the plain English sense and legal effect both of each such provision and of the agreement as a whole (including the integrity of any cross references and usage of defined terms) remains unchanged.

3. A change which provides that the agreement applies to existing Transactions outstanding between the parties on the date the agreement takes effect.

4. Any change to the scope of the agreement clarifying that certain transactions (e.g., OTC derivatives governed by an ISDA Master Agreement) shall not be transactions or contracts for purposes of the agreement.

5. An addition to the list of events that constitute an Event of Default (e.g. without limitation, the failure to deliver securities or other assets, a force majeure, cross default or downgrading event the death or incapacity of a Party or its general partner any default under a specified transaction or a specified master agreement), where such addition may or may not be coupled with a grace period or the serving of a written notice on the Defaulting Party by the Non-Defaulting Party, and such addition may be expressed to apply to one only of the Parties.[58]

6. Any change to an Insolvency Event of Default (i) introducing a grace period for the filing of a petition for bankruptcy proceedings (of e.g. 15 or 30 days),

[58] Counsel to delete and if any such provisions would alter agreement so as to prevent opinion from applying.

(ii) modifying or deleting any such grace period, (iii) requiring that the filing of the petition is not frivolous, vexatious or otherwise unwarranted or (iv) that the non-defaulting party has reasonable grounds to conclude that the performance by the defaulting party of its obligations under the agreement, Transactions, or both, is endangered.[58]

7. Any change to an Insolvency Event of Default more particularly describing (i) the relevant procedures that would or would not constitute such event of default or termination event (ii) the relevant officers the appointment of which would or would not constitute such Insolvency Event of Default.[58]

8. Any change to an Insolvency Event of Default extending its scope to events occurring with respect to the credit support provider, an affiliate, a custodian or trustee of a Party.

9. Any change to an Insolvency Event of Default replacing such event of default with a provision aligned to Section 5(a)(vii) of the 1992 or 2002 ISDA Master Agreement (or relevant part thereof).[58]

10. In the case of any agreement incorporating the Two-Way Clauses, any change to the Insolvency Events of Default which has the effect of providing that when one or several specified events (which would constitute Insolvency Events of Default) occur in relation to one specified Party, such event shall not constitute an Event of Default under the agreement.

11. Any change to the agreement requiring the Non-Defaulting Party when exercising its rights under the FOA Netting Provision, Clearing Module Netting Provision, Addendum Netting Provision, FOA Set-off Provisions, Clearing Module Set-Off Provision, Addendum Set-Off Provision or Title Transfer Provisions (or other provisions) or making determinations to act in good faith and/or a commercially reasonable manner.

12. Any change modifying the currency of Liquidation Amount, Available Termination Amount, Cleared Set Termination Amount or of any amount relevant to the FOA Set-Off Provisions, Clearing Module Set-Off Provision, Addendum Set-Off Provision or Title Transfer Provisions.

13. Any change to the FOA Netting Provision, the FOA Set-Off Provisions, the Clearing Module Netting Provision, the Clearing Module Set-Off Provision, the Addendum Netting Provision or the Addendum Set-Off Provision clarifying that (i) any account subject to set-off must be owned by the same

party or (ii) the Non-Defaulting Party must, or may, notify the other party of its exercise of rights under such provision or other provision.

14. Any change to the FOA Set-Off Provision, the Clearing Module Set-Off Provision or the Addendum Set-Off Provision (a) clarifying (i) at which time set-off may be exercised by a Party (with or without limitation), (ii) the amounts that may be set-off (with or without limitation, whether in relation to the agreement(s) under which such amounts arise or to the parties from which they are due), (iii) the scope of the provision where a Party acts as agent, (iv) the use of currency conversion in case of cross-currency set-off, (v) the application or disapplication of any grace period to set-off, (vi) the exercise of any lien, charge or power of sale against obligations owed by one Party to the other; or (b) allowing the combination of a Party's accounts.

15. Any change to the FOA Netting Provision adding or taking from the amounts to be taken into account for the calculation of the Liquidation Amount.

16. Any addition to any of the Core Provisions that leaves both the plain English sense and legal effect of such provision unchanged.

17. Any change converting the Core Provisions of the FOA Netting Provision to a 'one-way' form in the style of the One-Way Master Netting Agreement 1997 (in which only the default of one Party is contemplated).

18. Including multiple forms of netting provision in respect of Client Transactions, in any of the following combinations:

- more than one ISDA/FOA Clearing Addendum or Addendum Netting Provision
- more than one FOA Clearing Module or Clearing Module Netting Provision
- one or more ISDA/FOA Clearing Addendum or Addendum Netting Provision and one or more FOA Clearing Module or Clearing Module Netting Provision

provided that the agreement specifies unambiguously that only one such netting provision shall apply in respect of any given Client Transaction.

19. Including the Title Transfer Provisions together with provisions which create a security interest over cash and/or non-cash margin, provided that a

provision in the form of, or with equivalent effect to, clauses 4.3 and/or 4.4 of the FOA Clearing Module is used or the agreement otherwise unambiguously specifies the circumstances in which the security interest or the Title Transfer provisions apply in respect of any given item of margin so that it is not possible for both the security interest and the Title Transfer Provisions to apply simultaneously to the same item of margin.

20. Adding to the definition of "Firm Trigger Event" or, as the case may be, "CM Trigger Event" (or defined terms equivalent thereto) any further events of default in relation to the Firm or, as the case may be, the Clearing Member, including those in the definition of Events of Default appearing in an FOA Published Form Agreement (including as modified in accordance with paragraph 5 above).

21. Any change to the Clearing Module Netting Provision or, as the case may be, the Addendum Netting Provision providing that any applicable Cleared Set Termination Amount will be determined by the Firm or, as the case may be, the Clearing Member in any event (even in the case of a Firm Trigger Event or, as the case may be, a CM Trigger Event).

22. Any change to the FOA Netting Provision providing that any applicable Liquidation Amount will be determined by the Defaulting Party.

23. Any addition to the Clearing Module Netting Provision or the Addendum Netting Provision providing that, if any Firm/CCP Transaction or CM/CCP Transaction and its related collateral or margin has been ported to another clearing member of the Agreed CCP Service following a Firm Trigger Event or CM Trigger Event, the Party in charge of the calculation of the Cleared Set Termination Amount can ascribe an appropriately reduced value (including zero) to the Client Transaction and related margin or collateral corresponding to the Firm/CCP Transaction or CM/CCP Transaction and its related collateral or margin so ported.

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PART 3
SECURITY INTEREST PROVISIONS

1. **Security Interest Clause:**

   "As a continuing security for the performance of the Secured Obligations under or pursuant to this Agreement, you grant to us, with full title guarantee, a first fixed security interest in all non-cash margin now or in the future provided by you to us or to our order or under our direction or control or that of a Market or otherwise standing to the credit of your account under this Agreement or otherwise held by us or our Associates or our nominees on your behalf."

2. **Power of Sale Clause:**

   "If an Event of Default occurs, we may exercise the power to sell all or any part of the margin. The restrictions contained in Sections 93 and 103 of the Law of Property Act 1925 shall not apply to this Agreement or to any exercise by us of our rights to consolidate mortgages or our power of sale. We shall be entitled to apply the proceeds of sale or other disposal in paying the costs of such sale or other disposal and in or towards satisfaction of the Secured Obligations."

3. **Client Money Additional Security Clause**

   "As a continuing security for the payment and discharge of the Secured Obligations you grant to us, with full title guarantee, a first fixed security interest in all your money that we may cease to treat as client money in accordance with the Client Money Rules. You agree that we shall be entitled to apply that money in or towards satisfaction of all or any part of the Secured Obligations which are due and payable to us but unpaid."

4. **Rehypothecation Clause**

   "You agree and authorise us to borrow, lend, appropriate, dispose of or otherwise use for our own purposes, from time to time, all non-cash margin accepted by us from you and, to the extent that we do, we both acknowledge that the relevant non-cash margin will be transferred to a proprietary account belonging to us (or to any other account selected by us from time to time) by way of absolute transfer and such margin will become the absolute property of ours (or that of our transferee) free from any security interest under this Agreement and from any equity, right, title or interest of yours. Upon any such rehypothecation by us you will have a right against us for the delivery of property, cash, or securities of an identical type, nominal value, description and amount to the rehypothecated non-cash margin, which, upon being delivered back to you, will become subject to the provisions of this Agreement. We agree to credit to you, as soon as reasonably practicable following receipt by us, and

as applicable, a sum of money or property equivalent to (and in the same currency as) the type and amount of income (including interest, dividends or other distributions whatsoever with respect to the non-cash margin) that would be received by you in respect of such non-cash margin assuming that such non-cash margin was not rehypothecated by us and was retained by you on the date on which such income was paid.".

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ANNEX 5
NECESSARY OR DESIRABLE AMENDMENTS

1. Desirable amendments

(a) For the General Set-Off Clause.

If the General Set-Off Clause is intended to be relied upon to permit set-off of obligations arising under other specific types of agreements, we recommend that those specific agreement types be specifically referred to.

(b) For Investment Funds, Trustees of Private Trusts and Pension Entities that are trusts

We recommend use of the Trustee Annex.

(c) For Municipal Corporations

We recommend amending the Event of Default definition to specifically add to it the exercise by the OMB or Ministry of Municipal Affairs of any of its powers under Part III of the Municipal Affairs Act (See Schedule 10).

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ANNEX 6
APPLICATION OF INSOLVENCY REGIMES

	BIA	WURA	CCAA	CDIC Act	BIA Receiver	Corp.plan
Banks	X	√	X	√	X	X
Corporations (other than Insurance Companies, Financial Institutions, Pension Funds)	√	Not if CBCA; Others theoretically possible but not likely	√	X	√	√
Partnerships	√	X	Only corporate general partners	X	√	Only corporate general partners
Insurance Companies—Canadian or Provincial	X	√	X	X	X	X
Financial Institutions that are trust/loan/savings corporations	X	√	If federal X; if prov. unclear but not likely	If federal √; Not presently if prov.	X	X
Financial Institutions that are Cooperative Credit Associations	√	√ (possibly if non-CPA members)	Unclear but not likely if CPA members; possibly if not CPA members	X	√	Depends on governing legislation
Individuals	√	√ (consumer proposals in certain cases)	X	X	X	X
Investment Funds that are Income Trusts*	√	X	√	X	√	X

* publicly traded.

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Investment Funds that are trusts or Private Trusts (other than Income Trusts or Pension Plans)	Unclear	X	Unclear	X	√	X
Sovereign Entities	X	X	X	X	X	X
Charitable Corporations	√	theoretically possible but not likely	√	X	√	X
Pension Entities if CPPIB, PSPIB, CDPQ	X	X	X	X	X	X
Pension Entities (not CPPIB, PSPIB, CDPQ)[59]	Unclear but not likely	X	X	X	√	X
Municipal Corporations[60]	√	X	√	X	X	X

[59] As noted in the memorandum, pension plan trusts are likely to be wound up by the trustee either voluntarily or under the supervision of the regulator.

[60] Subject to unique Quebec Municipal Reorganization Procedures.

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ANNEX 7
EFFECT OF INSOLVENCY REGIMES ON ELIGIBLE FINANCIAL CONTRACTS

	Close-Out (Termination)	Netting
BIA Bankruptcy	Enforceable based on general insolvency principles	Enforceable based on general insolvency principles
BIA Proposal	Enforceable based on express statutory provision (BIA, s.65.1(7)(8))*	Enforceable based on express statutory provision (BIA, s.65.1(9))*
CDIC Act	Enforceable based on express statutory provision (CDIC Act, s.39.15(7)*, subject to caveat re bridge institution provisions	Enforceable based on express statutory provision (CDIC Act, s.39.15(7)*, subject to caveat re bridge institution provisions
CCAA	Enforceable based on express statutory provision (CCAA, s.34(7))*	Enforceable based on express statutory provision (CCAA, s.34(8)(9)(10))*
WURA	Enforceable based on express statutory provision (WURA, s.22.1(1)(2))*	Enforceable based on express statutory provision (WURA, s.22.1(1)(2))*
BIA Receivership	Generally enforceable based on general insolvency principles; express statutory netting right if PCSA applies; some stay risk otherwise	Enforceable based on general insolvency principles; express statutory netting right if PCSA applies; some stay risk otherwise
Corp. Plan of Arrangement	Generally enforceable based on general principles if termination right provided for in the Master Agreement; some stay risk in light of *Abitibi*	Generally enforceable based on general principles if termination and netting right provided for in the Master Agreement; some stay risk in light of *Abitibi*
Voluntary Wind-up	No stay orders made in this context – enforceable based on contract enforceability generally	No stay orders made in this context - enforceable based on contract enforceability generally

* The protections apply to the eligible financial contracts only. If the PCSA applies, then enforceability of the Agreement is protected with respect to any type of transaction, including all types of transaction listed in Annex 2.

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Wind-up by Pension Regulator	No automatic stay and no stay order likely	No automatic stay and no stay order likely

ANNEX 8

Eligible Financial Contract

The concept of an EFC is relevant to the statutory safe-harbours from automatic or court ordered stays in the BIA Proposal provisions, the WURA, the CCAA and the PCSA.[61] Consequently we will begin with an analysis of this term. Each of the aforementioned Acts provides that an "eligible financial contract" is defined by the regulations to the Act. The regulations to each of the Acts are identical in terms of the definition. The definition is framed in general terms and includes a wide range of non-exclusive underlying interests (defined non-exclusively). An "eligible financial contract" is:

(a) a derivatives agreement, whether settled by payment or delivery, that

(i) trades on a futures or options exchange or board, or other regulated market, or

(ii) is the subject of recurrent dealings in the derivatives markets or in the over-the-counter securities or commodities markets;

(b) an agreement to

(i) borrow or lend securities or commodities, including an agreement to transfer securities or commodities under which the borrower may repay the loan with other securities or commodities, cash or cash equivalents,

(ii) clear or settle securities, futures, options or derivatives transactions, or

(iii) act as a depository for securities;

(c) a repurchase, reverse repurchase or buy-sellback agreement with respect to securities or commodities;

[61] Also in the CDIC Act which is relevant to Financial Institutions considered in Schedule 1.

(d) a margin loan in so far as it is in respect of a securities account or futures account maintained by a financial intermediary;

(e) any combination of agreements referred to in any of paragraphs (a) to (d);

(f) a master agreement in so far as it is in respect of an agreement referred to in any of paragraphs (a) to (e);

(g) a master agreement in so far as it is in respect of a master agreement referred to in paragraph (f);

(h) a guarantee of, or an indemnity or reimbursement obligation with respect to, the liabilities under an agreement referred to in any of paragraphs (a) to (g); and

(i) an agreement relating to financial collateral, including any form of security or security interest in collateral and a title transfer credit support agreement, with respect to an agreement referred to in any of paragraphs (a) to (h).

...

A "derivatives agreement" is:

> ... a financial agreement whose obligations are derived from, referenced to, or based on, one or more underlying reference items such as interest rates, indices, currencies, commodities, securities or other ownership interests, credit or guarantee obligations, debt securities, climatic variables, bandwidth, freight rates, emission rights, real property indices and inflation or other macroeconomic data and includes
>
> (a) a contract for differences or a swap, including a total return swap, price return swap, default swap or basis swap;
>
> (b) a futures agreement;
>
> (c) a cap, collar, floor or spread;
>
> (d) an option; and
>
> (e) a spot or forward.

For the purpose of the margin loan category, the definition of "financial intermediary" is:

(a) a clearing agency; or

(b) a person, including a broker, bank or trust company, that in the ordinary course of business maintains securities accounts or futures accounts for others.

General Criteria Relevant to all Transactions

Subject of Recurrent Dealings. A general element of the definition of "derivatives agreement" is that the agreement must be "the subject of recurrent dealings in the derivatives markets or in the over-the-counter securities or commodities markets". Any futures contract or option on futures with sufficient liquidity to trade over an organized futures market should meet this criterion. This is not by its terms restricted to Canadian markets and we believe that it would not be interpreted to refer only to Canadian markets. As to other Transactions that do not trade over an exchange, if the Transaction was sufficiently unique or very new to the global market it may not be covered by the definition of a derivatives agreement.

Financial Agreement. The definition of "derivative agreement" encompasses the concept of a "financial" agreement. We believe that the intention of the definition is not to require evidence in individual cases that transactions have a "financial" element in the particular context if the transaction is one of the listed types of contracts, such as a swap, future, option, spot or forward, and if it relates to an underlying interest that is specifically listed. In other words, such contracts should be, by definition, "financial" agreements. This approach to the definition meets the purpose of the legislation, which is to provide certain and express protection for termination, netting and collateral enforcement rights for the types of contracts that are the subject of recurrent dealings in derivatives, futures, securities, financing and commodities markets.

If this interpretation is not correct, then we believe that any Transactions that provide for cash settlement or Transactions that involve an element of financial risk management or speculation would be found to be "financial" agreements. Also, if the analysis of the Quebec Court of Appeal in *Re Androscoggin Energy LLC*[62] is applied, the presence of termination and netting rights such as the Netting Provision is itself a key indication of the financial nature of the contract. (See following note re Physical Commodity Transactions.)

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[62] (2005), 8 C.B.R. (5th) 11.

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Physical Commodity Transactions

What is a Commodity? In interpreting the former definition of EFC[63], the Alberta Court of Appeal in *Re Blue Range Resource Corporation* defined a "commodity" as a product that was interchangeable and readily identifiable as a fungible commodity, capable of being traded on a futures exchange or as the underlying asset of an over-the-counter derivative transaction. The product must trade in a volatile market, with a sufficient trading volume to ensure a competitive trading price, in order that the transaction may be marked to market and its value determined. Presumably any commodity trading on a futures market would be a commodity within the meaning of the definition. With respect to other Transactions involving commodities, our conclusion that Transactions listed in Annex 2 are EFCs is, with respect to any Transaction involving a "commodity," based on the assumption that the commodity in issue would meet these criteria.

Physical Commodity Contracts Generally. In *Blue Range*, the Alberta Court of Appeal held that physically settled gas transactions are commodity contracts within the meaning of this definition; it was considering forward contracts at a fixed price. The Quebec Court of Appeal in *Re Androscoggin Energy LLC* agreed that physical gas contracts could be EFCs, but put a gloss on the definition by also stating that the contract had to have a "financial purpose". It found that the "hallmark" of a financial purpose, and, consequently, an EFC, is the presence of termination and netting rights. Because there was no master agreement in that case, the court found that the contracts were not EFCs. While the existence of termination and netting rights is a hallmark of an EFC, it may not be determinative in a particular case.

This need for a financial purpose was reaffirmed by the Alberta Court of Queen's Bench in *Re Calpine Canada Energy Limited*[64], where the court held that a right of refusal to obtain unspecified quantities of gas from a particular field at a spot price (a call on production agreement) was not an EFC. A typical Transaction would be easily distinguishable from the Calpine type of agreement. Therefore, physical commodity Transactions documented subject to an Agreement should generally satisfy the statutory criteria.

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63 The definition of eligible financial contract that applied to commodity transactions until the most recent change to the definition of eligible financial contract was «a spot, future, forward or other commodity contract and any master agreement in respect of any such contract».

64 The definition of eligible financial contract that applied to commodity transactions until the most recent change to the definition was «a spot, future, forward or other commodity contract and any master agreement in respect of any such contract».

However, the analysis applied in these cases and which may still apply given the presence of the word "financial" as part of the definition of a "derivative agreement" suggests that while physical contracts are covered, they may not be covered if they do not also have an element of risk management or price speculation.

"Forward" contracts and "spot" contracts are not defined in the legislation. An agreement for the forward sale of a commodity at a price which is the market spot price at the time of the sale, might not be a "forward". In the *Blue Range* decision, the court included as one of the key elements of a forward contract that the price be a defined price or be determined by a pricing mechanism that would provide for a certain price. While the market price at the date of delivery may be a price that is determined by a pricing mechanism, given that the court referred to the marking to market of the forward contracts, it is likely that court meant a price other than the market spot price at the time of the delivery. Also, the inclusion of the word "financial", might also suggest that a physical commodity transaction must have a price risk management or price speculation element to it in order to enjoy the protection of the EFC safe-harbour.

Arguably such an interpretation is consistent with the policy underlying the exemption. The purpose of the EFC exemption is, in part, to allow termination of transactions that manage or redistribute financial risk (which, in the case of commodity contracts, is essentially price risk) in order to facilitate the replacement of the contract with a similar hedging contract with a solvent entity. Consequently, price risk allocation is likely an essential element of a forward.

There are, however, arguments to support the position that such a physical commodity transaction is an EFC even if it does not involve an element of price risk management or allocation.

- As noted above, one reading of the definition is that forward and spot contracts are by definition financial agreements since they are specifically listed. In that case, the need to show a price risk management or allocation element should only arise for the types of contracts that are not determined to be a spot or forward (or other listed type of contract).

- Spot contracts are specifically mentioned and they do not (unless they are rolling spots) have a price risk management element. As a result, a position can be taken that contracts for the forward sale of a commodity at a "spot" price are intended to be EFCs.

- Financial institutions, such as banks, and their commodity marketing subsidiaries are important participants in these commodity markets for liquidity purposes. It is the financial nature of the market generally that should as a policy matter drive the interpretation of the provision, not the purpose of the individual parties to the Transaction.

- On the Quebec court's analysis in *Androscoggin*, the presence of the Netting Provision in the Agreement should lead to the conclusion that such Transactions and Agreement are "financial" agreements and, consequently, EFCs.

- A restructuring of the insolvent entity is not put in jeopardy if the transaction is terminated because supply can always be purchased for the same price on the spot market if the commodity is liquid and fungible.

Consequently, we believe that there is a solid basis for the view that if the Transaction is a commodity contract it should be encompassed in the definition without requiring that the specific Transaction meet any additional criterion of having a price risk management or allocation element to it.

ANNEX 9
Deemed Trusts, Liens, Security Interests and other priority charges

Special Liens and Priorities

The laws of this jurisdiction also provide for a number of statutory super priority liens or deemed trusts that can take priority over perfected consensual security interests regardless of the law governing consensual security interests. Successful assertion of these liens can result in impediments to enforcing security interests or reversal of enforcement action. These include such debts as employee income tax remittances, Canada Pension Plan contributions, contributions to the Employment Insurance Plan, statutory vacation pay claims, employer contributions to employee pension plans, and sales tax remittances. They may take priority over certain types of collateral only and may apply only in certain circumstances. Priority also may depend on whether or not there is a bankruptcy proceeding.[65] This is a very complex area of law that cannot be adequately addressed in the context of an opinion such as this. Many of these types of super-priorities should not attach to Cash Margin.[66]

However, a prior ranking security interest might, in certain circumstances, attach to Cash Margin, where the Defaulting Party owes Canadian Revenue Agency (the Canadian federal taxing authority) with respect to amounts it did or should have withheld at source. This security interest is provided for under the *Income Tax Act* (Canada).[67] A recent decision of the Supreme Court of Canada held that the Crown's claim for income tax and employment insurance remittance arrears arising prior to the date of the exercise of the set-off right took priority over a credit institution's right to set-off loan obligations against its own term deposit liability to the borrower.[68]

The BIA also includes a secured priority charge for employee wage claims of up to $2000 per employee that can take priority over any other secured

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65 Certain Crown claims have priority outside of bankruptcy, but not if the debtor becomes bankrupt under the BIA or WURA.

66 On the other hand, assignments of receivables as collateral are clearly subordinate to Crown claims for employee income tax remittances, Canada Pension Plan and Unemployment Insurance contributions and in certain cases Goods & Services Tax on the sale of the goods or services that gave rise to the receivable.

67 Section 227(4.1)

68 Caisse Desjardins de l'Est du Drummond v. Canada, 2009 SCC 29 (S.C.C.)

creditors.

Provincially created special liens and charges are generally subordinated in federal bankruptcy proceedings under the BIA. In restructuring proceedings generally the order of priorities that would prevail in bankruptcy is adhered to (to avoid legal arbitrage among the different types of proceedings). However, there are some provincial liens and charges that could prevail over certain secured creditors. For example, the provincial lien and deemed trust over the assets of an employer for the amount of the unfunded liabilities in certain types of pension plans may prevail over cash collateral arrangements. A recent decision of the Quebec Court of Appeal held that this provincial lien extended to all unfunded liabilities in provincially regulated defined benefit pension plans (not just for funding payments actually due at the time but which would have been payable over time).[69] An appeal has been heard by the Supreme Court of Canada[70], but no decision has been rendered yet. Parties may want to determine if their counterparties have such plans for their employees and if so consult with counsel to understand the risks.

Court ordered Liens in Restructuring Proceedings

Debtor in Possession Financing Under the CCAA and BIA Proposals. In a CCAA or BIA Proposal proceeding the court has the statutory jurisdiction to authorize a security interest or a charge in favour of the debtor-in-possession financier and to order that this security interest or charge has priority over the security interest of any other secured party.[71] A similar jurisdiction to grant a priority charge is available with respect to (i) credit granted by critical suppliers to the debtor, (ii) indemnities in favour of directors and officers who continue to service the debtor company after the filing, and (iii) fees and expenses of the monitor and experts (such as lawyers and financial experts) engaged by the monitor, the debtor or any other interested person[72] for the purpose of the proceedings under the Act. Affected secured creditors are entitled to prior notice of any application requesting such a charge on the assets of the debtor.

Similar provisions apply in BIA proposal proceedings.[73]

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69 Re Indalex, 2011 ONCA 265.

70 December 1, 2011.

71 Previously courts granted such orders based on their inherent jurisdiction.

72 Where engaged by a person other than the debtor or the monitor the court must be satisfied that the security or charge is necessary for their effective participation in the proceedings.

73 Although the BIA does not expressly provide for a charge for critical suppliers.

However, there are applicable exemptions to these priorities. Both the BIA and CCAA provide that no order can be made under the Act that has the effect of subordinating "financial collateral" for an "eligible financial contract."[74]

Therefore, to the extent that the Transactions are EFCs and the Collateral is financial collateral, these court ordered priority security interests will not apply. Otherwise they will, unless the court specifically exempts them.

[74] S.C. 2007, c. 29; see CCAA, s.34(11); BIA, s. 88.

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ANNEX 10
Financial assets, securities, security entitlements and control under the Quebec STA

Financial Asset

For purposes of the Quebec STA, a financial asset is

1. a security;

2. a share or other participation in a person or an obligation of a person that, without being a security, is, or is of a type, dealt in or traded on financial markets or is a medium for investment in the area in which it is issued or dealt in or traded;

3. any property that is held by a securities intermediary for another person in a securities account if the securities intermediary has expressly agreed with the other person that the property is to be treated as a financial asset under this Act; or

4. a credit balance in a securities account, unless the securities intermediary has expressly agreed with the person for whom the account is maintained that the credit balance is not to be treated as a financial asset under this Act.

Securities: Share or participation in an issuer or obligation of an issuer

For purposes of the Quebec STA, a security is a share or similar participation in an issuer or an obligation of an issuer

1. that is represented by a security certificate in bearer form or registered form, or the transfer of which may be registered on books maintained for that purpose by or on behalf of the issuer;

2. that is one of a class or series, or by its terms is divisible into a class or series, of shares, participations or obligations; and

3. that is, or is of a type, dealt in or traded on securities exchanges or financial markets, or that is a medium for investment in the area in which it is issued or dealt in or traded and by its terms expressly provides that it is a security for the purposes of this Act.

Security certificate

A security certificate is in bearer form if it expressly states that the security is payable to the certificate bearer. A security certificate is in registered form if it specifies a person entitled to the security and if a transfer of the security may be registered on books maintained for that purpose by or on behalf of the issuer, or the security certificate states that it may be so registered.

Control

The Quebec STA provides that a secured party:

(1) has control of **a certificated security in bearer form** if the certificated security is delivered to the secured party or its agent, other than a securities intermediary (i.e. the secured party or its agent acquires possession of the security certificate) and remains published until the secured party does not have control;[75]

(2) has control of **a certificated security in registered form** if the certificated security is delivered to the secured party or its agent or, provided the endorsement is not in blank, securities intermediary and the certificate is endorsed to the secured party or in blank by an effective endorsement, or the certificate is registered in the name of the secured party at the time of the original issue or by registration of transfer by the issuer and remains published until the secured party does not have control;[76]

(3) has control of **an uncertificated security** if it is delivered to the secured party (i.e. the issuer transfers the uncertificated security from the debtor to the secured party or its agent, other than a securities intermediary)[77] or if the issuer has agreed with the secured party that it will comply with instructions that are originated by the secured party

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[75] Art. 2705 CCQ does not apply in light of the specific requirements of Art. 2714.1 CCQ. See QSTA s. 50.

[76] See Arts. 2702 to 2704, 2714.1, 2736 and 2798 CCQ.

[77] Delivery of an uncertificated security to a secured creditor occurs when (a) the issuer registers the secured creditor as the registered holder on the original issue or the registration of transfer or (b) another person, other than a securities intermediary, either, becomes the registered holder on behalf of the secured creditor or having previously become the registered holder acknowledges that the person holds for the secured creditor. QSTA, s.51.

without the further consent of the registered holder and remains published until the secured party does not have control; and

(4) has control of **a security entitlement** if the secured party becomes the entitlement holder or the securities intermediary agrees with the secured party that it will comply with entitlement orders originated by the secured party without further consent of the entitlement holder and remains published until the secured party does not have control. A person becomes the entitlement holder when the security entitlement is transferred to a securities account in the person's name.

Security entitlement

A security entitlement is established when a security or other financial asset is, or is to be, credited to a securities account maintained by a securities intermediary.

A person acquires a security entitlement and so becomes the entitlement holder if a securities intermediary

1. indicates, by book entry, that a financial asset has been credited to the person's securities account;

2. receives a financial asset from the person or acquires a financial asset for the person and, in either case, accepts it for credit to the person's securities account; or

3. becomes obligated under another law, regulation or rule or under a judgment to credit a financial asset to the person's securities account.

A person may have a security entitlement even if the securities intermediary does not itself hold the financial asset.

A person is not considered to have a security entitlement with respect to a financial asset if a securities intermediary holds the financial asset for that person and the financial asset

(1) is registered in the name of, payable to the order of or specially endorsed to that person; and

(2) has not been endorsed to the securities intermediary or in blank.