

England and Wales/IAS 32/Clearing Member/Eurex (Swaps and Options)

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5 March 2014

Dear Sirs,

IAS 32 Opinion relating to clearing members in England and Wales – as at 30 September 2013

You have asked us to give an opinion in respect of the laws of England and Wales ("this jurisdiction") in relation to certain netting and set-off provisions in the Rules of Eurex Clearing AG (the "CCP"), in respect of payments due in relation to services which involve the clearing of options or interest rate swaps, the payment or repayment of variation margin and all other amounts payable in respect of transactions cleared pursuant to such services (such amount an "Applicable Amount", and such clearing service provided in respect of such Applicable Amount, a "Service") as such provisions apply between the CCP and clearing members incorporated or with an establishment in this jurisdiction (each a "Clearing Member"). This opinion does not apply to any clearing services or transactions other than in respect of the Service specified.

We understand that your requirement is for the enforceability and validity of such netting and set-off provisions and collateral arrangements to be substantiated by a written and reasoned opinion for the purposes of demonstrating compliance with International Accounting Standard 32 ("IAS 32") and the clarification amendments made to IAS 32 in December 2011 and effective on 1 January 2014.

References herein to "this opinion" are to the opinion given in Section 3.

1. TERMS OF REFERENCE AND DEFINITIONS

- 1.1 This opinion is given in respect of the Netting Provisions of the CCP and the laws of this jurisdiction in force **as at 30 September 2013**. We express no opinion as to any provisions of the Rules of the CCP other than those on which we expressly opine.
- 1.2 This opinion is given in respect of Clearing Members which are:
 - 1.2.1 banks incorporated in this jurisdiction or incorporated in another jurisdiction but with a branch in this jurisdiction; or
 - 1.2.2 investment firms incorporated in this jurisdiction or incorporated in another jurisdiction but with a branch in this jurisdiction,which are, in either case, either English Companies or Foreign Companies including, in each case, such persons (banks) which have permission to accept deposits by virtue of Part 4A of FSMA (but not any bank which is not an English Company or a Foreign Company).
- 1.3 This opinion letter is given only in respect of payments which are Applicable Amounts in relation to Transactions cleared through the Service.
- 1.4 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.
- 1.5 We do not opine on the availability of any judicial remedy, including in respect of any net obligation resulting from any netting or set-off, whether pursuant to the Netting Provisions or otherwise.
- 1.6 This opinion letter relates solely to matters of English law and does not consider the impact of any laws (including insolvency laws) other than English law, even where, under English law, any foreign law fails to be applied. All non-contractual obligations and any other matters arising out of or in connection with this opinion letter are governed by English law. We express no opinion in this opinion letter on the laws of any other jurisdiction.
- 1.7 We express no opinion as to any provisions of any CCP Documentation or the Rules other than those to which express reference is made in this opinion letter except insofar as any such provision relates to the effectiveness of the Netting Provisions.
- 1.8 We do not express any opinion as to any matters of fact or accounting policy.

1.9 Interpretation

- 1.9.1 Terms used in this opinion letter and not otherwise defined herein shall have the meanings ascribed to them in Schedule 1 (*Definitions*) unless the context specifies otherwise.
- 1.9.2 Any reference to any legislation (whether primary legislation or regulations or other subsidiary legislation made pursuant to primary legislation) shall be construed as a reference to such legislation as the same may have been amended or re-enacted on or before the date of this opinion letter.
- 1.9.3 A reference to a "**paragraph**" is to a paragraph of this opinion letter (except where the context otherwise requires).
- 1.9.4 Headings are for ease of reference only and shall not affect the interpretation of this opinion letter.

2. ASSUMPTIONS

For the purposes of our opinions, we make the following assumptions:

- 2.1 That each Party has the capacity, power and authority under all applicable law(s) to enter into the CCP Documentation, and to perform its obligations under the CCP Documentation and Rules.
- 2.2 That each Party has taken all necessary steps and obtained and maintained all authorisations, approvals, licences and consents necessary to execute, deliver and perform the CCP Documentation and Transactions, and to ensure the legality, validity, enforceability or admissibility in evidence of the CCP Documentation and Transactions in this jurisdiction.
- 2.3 The CCP Documentation and each of the Transactions accurately reflect the true intentions of the Parties and have been entered into and are carried out by the Parties 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.
- 2.4 That the CCP Documentation, the Rules and the Transactions (including the obligations to pay Applicable Amounts) are legal, valid, binding and enforceable under the law by which they are expressed to be governed.
- 2.5 That the choice of law provisions in the CCP Documentation and the Rules has been expressly made and is clear.

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- 2.6 That the CCP Documentation has been entered into prior to the commencement of any Insolvency Proceedings under the laws of any jurisdiction in respect of either Party.
- 2.7 Save in relation to any non-performance leading to the taking of action by a Clearing Member under the Netting Provisions, each Party performs its obligations under the CCP Documentation and the Rules in accordance with their terms.
- 2.8 That, apart from any circulars, notifications and equivalent measures published by the CCP in accordance with the Rules, there are no other agreements, instruments or arrangements between the Parties which modify or supersede the terms of the Rules or the CCP Documentation; and in particular in relation to the settlement of payments due in respect of Applicable Amounts, that there are no provisions in the rules of any relevant designated system (other than the CCP itself) which purport to override or are inconsistent with the Netting Provisions.
- 2.9 The each Applicable Amount which is to be set off or netted under the BAU Netting Provisions is due and payable on the date on which the rights under the BAU Netting Provisions are to be exercised.
- 2.10 That none of the Rules has been disallowed pursuant to section 300A of FSMA.
- 2.11 That the CCP is at all material times a recognised clearing house within the meaning of section 285 of FSMA and for the purposes of Part VII and an EEA Designated System.
- 2.12 The Clearing Member is either:
 - 2.12.1 a UK Credit Institution or an EEA Credit Institution;
 - 2.12.2 an investment undertaking which provides services involving the holding of funds or securities for third parties (within the meaning of Article 1(2) of the EUIR); or
 - 2.12.3 a bank incorporated in a jurisdiction other than the United Kingdom or another member state of the EEA, with a branch in this jurisdiction.
- 2.13 That neither Party is subject to Part VII by reason of being a recognised investment exchange (as defined in section 285 of FSMA) or, in the case of the Clearing Member, by reason of being a recognised clearing house, EEA central counterparty or third country central counterparty (each as defined in FSMA).
- 2.14 That neither Party is a "*group undertaking*" in relation to the other Party as that phrase is defined in section 1161(5) of the Companies Act 2006.

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2.15 That neither Party is a "*bridge bank*" as defined in section 12 of the Banking Act 2009.

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 Governing Law

3.1.1 The choice of law provisions of the CCP Documentation and the Rules would be recognised under the law of this jurisdiction, regardless of whether or not either or both of the Clearing Member and the CCP are incorporated, domiciled or established in this jurisdiction, subject to and in accordance with, the provisions of the Contracts (Applicable Law) Act 1990 in relation to contract entered into prior to 17 December 2009 or Council Regulation (EC) No. 593/2008 of 17 June 2008 on the law applicable to contractual obligations in relation to contract entered into on or after that date. However, there are some matters which are not determined by reference to governing law, 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 CCP Documentation or the Rules insofar as they relate to non-contractual obligations arising from or connected with the CCP Documentation, the Rules or, as the case may be, any Transactions.

3.1.2 In relation to the enforceability or effectiveness of the BAU Netting Provisions in the event of Insolvency Proceedings against the Clearing Member:

(a) in relation to a UK Credit Institution, by virtue of regulation 28 of the Credit Institutions Regulations, an Insolvency Representative or court in this jurisdiction would have regard exclusively to the governing law of the BAU Netting Provisions in determining the enforceability or effectiveness of the BAU Netting Provisions;

(b) in relation to an EEA Credit Institution:

(i) a court in this jurisdiction would decline jurisdiction to commence Insolvency Proceedings in respect of such EEA Credit Institution pursuant to regulation 3(1) of the Credit Institutions Regulations; and

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- (ii) if an application was made to a court in this jurisdiction in respect of the enforceability or effectiveness of the BAU Netting Provisions, such court in this jurisdiction would refer the question of which law is applicable to determine the enforceability or effectiveness of the BAU Netting Provisions to the law governing those Insolvency Proceedings, although by virtue of article 23 of Directive 2001/24/EC on the reorganisation and winding up of credit institutions, the substantive issue should be determined in those Insolvency Proceedings in accordance with the governing law of the Rules; and
- (c) in other cases, an Insolvency Representative or a court in this jurisdiction would have regard to the governing law of the BAU Netting Provisions in determining the enforceability or effectiveness of the BAU Netting Provisions, but may also have regard to overriding principles of insolvency law in the jurisdiction in which Insolvency Proceedings have been opened.

3.1.3 In relation to the enforceability or effectiveness of the Member Default Netting Provisions or the CCP Default Netting Provisions in the event of Insolvency Proceedings against the Clearing Member:

- (a) in relation to a UK Credit Institution, by virtue of regulations 28 and 34 of the Credit Institutions Regulations, an Insolvency Representative or court in this jurisdiction would have regard exclusively to the governing law of the Member Default Netting Provisions or the CCP Default Netting Provisions (as applicable) in determining the enforceability or effectiveness of the Member Default Netting Provisions or CCP Default Netting Provisions (as applicable);
- (b) in relation to an EEA Credit Institution:
 - (i) a court in this jurisdiction would decline jurisdiction to commence Insolvency Proceedings in respect of such EEA Credit Institution pursuant to section 3(1) of the Credit Institutions Regulations; and
 - (ii) subject to paragraph 3.1.3(c), if an application is made to a court in this jurisdiction in respect of the enforceability or effectiveness of the Member Default Netting Provisions or the CCP Default Netting Provisions, such court in this jurisdiction would refer the question of which law is applicable to determine the enforceability or effectiveness of the Member

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Default Netting provisions or CCP Default Netting Provisions (as applicable) to the law governing those Insolvency Proceedings, although by virtue of articles 23 and 25 of Directive 2001/24/EC on the reorganisation and winding up of credit institutions, the substantive issue should be determined in those Insolvency Proceedings in accordance with the governing law of the Rules;

- (c) to the extent that the Member Default Netting Provisions or the CCP Default Netting Provisions constitute a close-out netting provision (as defined in the FCA Regulations) which forms part of a Financial Collateral Arrangement, a court in this jurisdiction would have regard exclusively to the governing law of the Member Default Netting Provisions or CCP Default Netting Provisions (as applicable) in determining the enforceability or effectiveness of the Member Default Netting Provisions or CCP Default Netting Provisions (as applicable); and
- (d) in other cases, an Insolvency Representative or a court in this jurisdiction would have regard to the governing law of the Member Default Netting Provisions or CCP Default Netting Provisions (as applicable) in determining the enforceability or effectiveness of the Member Default Netting Provisions or CCP Default Netting Provisions (as applicable), but may also have regard to overriding principles of insolvency law in the jurisdiction in which Insolvency Proceedings have been opened.

3.1.4 However, in those circumstances identified in paragraphs 3.1.2 and 3.1.3 above in which a court in this jurisdiction may have regard to the law of another jurisdiction in determining the enforceability or effectiveness of the Netting Provisions, to the extent that enforceability of the Netting Provisions is protected by the provisions of Part VII (as to which see the discussion in paragraph 3.4.2 below), section 183(2) of Part VII provides that a court in this jurisdiction shall not recognise or give effect to any order of a court exercising jurisdiction in relation to the insolvency law in a country or territory outside the United Kingdom or any act of a person appointed in such country or territory to discharge functions under insolvency law in so far as the making of the order or the doing of the act would be prohibited in the case of a court in the United Kingdom or a relevant office-holder by provisions made under Part VII.

Accordingly, in those circumstances, even if the courts of another jurisdiction were to make an order or an insolvency office-holder was to exercise any powers under the insolvency law of another jurisdiction in a manner which is

inconsistent with the enforceability of the Netting Provisions under their governing law, the courts of this jurisdiction would not recognise or give effect to such order or action. However, this would not prevent the courts of this jurisdiction giving effect to an order of a court in another jurisdiction as to the effect of the Netting Provisions in accordance with their governing law.

3.2 Set-off under the Netting Provisions

The courts of this jurisdiction would give effect to the enforceability and effectiveness of the Netting Provisions to achieve netting and set-off of Applicable Amounts, in accordance with the terms of Netting Provisions, on the basis of the analysis in the CCP Opinion that the Netting Provisions are enforceable and effective under their governing law.

3.3 Reasons for Opinion – Prior to onset of Insolvency Proceedings

Prior to the commencement of Insolvency Proceedings against the Clearing Member, we are of the opinion expressed in paragraph 3.2 because the courts of this jurisdiction will have regard exclusively to the governing law of the Netting Provisions in determining the enforceability or effectiveness of those provisions.

3.4 Reasons for Opinions – Following commencement of Insolvency Proceedings – Prior to a SISO Effective Date

Following the commencement of Insolvency Proceedings against the Clearing Member, but subject to the discussion in relation to the occurrence of a SISO Effective Date in paragraph 3.5 below, we are of the opinion expressed in paragraph 3.2 because, except as otherwise provided under the law of insolvency in this jurisdiction, an Insolvency Representative and the courts of this jurisdiction would have regard exclusively to the governing law of the Netting Provisions in determining the effectiveness and enforceability of the Netting Provisions. In addition, there are a number of express provisions of the law of this jurisdiction which would apply to protect the various Netting Provisions in certain circumstances as follows.

3.4.1 Impact of Section 127 of the Insolvency Act 1986

Section 127 of the Insolvency Act 1986 provides that any disposition of the property of a company following the commencement of winding-up or bank insolvency in respect of the company is void unless the court otherwise orders. However, section 164(3) of Part VII disapplies section 127 in respect of, amongst other things, any Market Contract (which will include the Transactions) or any disposition of property in pursuance of a Market Contract, the provision of margin in relation to Market Contracts and any disposition of property in accordance with the rules of the CCP as to the application of property provided as margin.

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Further, to the extent that the Netting Provisions constitute a term of a Financial Collateral Arrangement, regulation 10(1)(a) of the FCA Regulations disapplies section 127 in respect of any disposition of property arising under such Financial Collateral Arrangement. Accordingly, section 127 would not affect the effectiveness or enforceability of the Netting Provisions. In a similar vein, to the extent that the Member Default Netting Provisions or CCP Default Netting Provisions constitute a close-out netting provision (as defined in the FCA Regulations), regulation 12(1) of the FCA Regulations provides that such close-out netting provision shall take effect in accordance with its terms, and regulation 10(1)(b) of the FCA Regulations expressly prevents section 127 of the Insolvency Act 1986 from preventing such close-out netting provision taking effect in accordance with its terms.

3.4.2 *Part VII of the Companies Act 1989*

Sections 159(1)(b)-(c) of Part VII provide that the Default Rules of the CCP or other rules of the CCP as to the settlement of Market Contracts not dealt with under its default rules are not to be regarded as to any extent invalid at law on the grounds of inconsistency with the law relating to the distribution of the assets of a person in insolvency. Similarly, sections 159(2)(a)-(b) provide that an insolvency office-holder may not exercise its powers in any way so as to prevent or interfere with the settlement of a Market Contract in accordance with the rules of the CCP not dealt with under its default rules, or any action taken by the CCP under its default rules.

The Member Default Netting Provisions will form part of the Default Rules of the CCP and, accordingly, the enforceability or effectiveness of those provisions will not be affected by the commencement of Insolvency Proceedings in respect of the Clearing Member.

Although the CCP Default Netting Provisions do not form part of the Default Rules of the CCP, they are rules relating to the settlement of Market Contracts, and, accordingly, the enforceability or effectiveness of those provisions will also not be affected by the commencement of Insolvency Proceedings in respect of the Clearing Member.

The BAU Netting Provisions also constitute rules relating to the settlement of Market Contracts and accordingly the enforceability or effectiveness of those provisions will not be affected by the commencement of Insolvency Proceedings in respect of the Clearing Member. However, this protection will not apply to the extent that the set-off of Applicable Amounts pursuant to the BAU Netting Provisions does not constitute "settlement" of those Market Contracts.

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The protection of the Netting Provisions which is provided by Part VII applies notwithstanding that the Clearing Member may be subject to Insolvency Proceedings in another jurisdiction. This is because, as discussed in paragraph 3.1.4 above, the courts in this jurisdiction are prohibited by Section 183(2) of Part VII from recognising or giving effect to the order of any court outside the United Kingdom or any act by an foreign insolvency official where such order or act would be prohibited by a court or insolvency official in the United Kingdom by Part VII.

3.4.3 *Financial Collateral Regulations*

To the extent that the Applicable Member Default Netting Provisions or the CCP Default Netting Provisions constitute a term of a Financial Collateral Arrangement, or an arrangement of which a Financial Collateral Arrangement forms a part, regulation 12(1) of the FCA Regulations provides that such provision shall take effect in accordance with its terms (which would fail to be determined in accordance with its governing law), notwithstanding that the collateral-provider or collateral-taker under the arrangement is subject to winding-up proceedings or reorganisation measures (as such terms are defined in the FCA Regulations).

3.5 Impact of occurrence of SISO Effective Date

- 3.5.1 A Clearing Member which is covered by this opinion may be subject to liquidation, or in certain circumstances, administration, under the laws of this jurisdiction. In such types of Insolvency Proceedings there may be a SISO Effective Date¹.
- 3.5.2 If a SISO Effective Date occurs in respect of the Clearing Member, there would be a mandatory statutory insolvency set-off ("SISO") of all amounts due between the Clearing Member and the CCP, including all present and future amounts owed between the Clearing Member and the CCP and any other present and future amounts owing between the Clearing Member and the CCP (including the Applicable Amounts) so that only a single net sum is payable, notwithstanding the terms of the Netting Provisions or any other contract between the Clearing Member and the CCP. Under the laws of this jurisdiction it is not possible to contract out of SISO.

SISO may be implemented, in a winding-up, under Rule 4.90 of the Insolvency Rules 1986 ("Rule 4.90"); in an administration, under Rule 2.85 of

¹ These Insolvency Proceedings do not apply to an EEA credit institution. These Insolvency Proceedings may apply to an investment firm incorporated in another jurisdiction if it provides services involving the holding of funds or securities for third parties, or the centre of its main interests or an establishment is located in this jurisdiction.

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the Insolvency Rules 1986 ("Rule 2.85"); in a bank insolvency, under Rule 72 of the Bank Insolvency (England and Wales) Rules 2009 ("Rule 72"); in a bank administration, under Rule 2.85 as applied by the Bank Administration (England and Wales) Rules 2009; in relation to an investment bank special administration, under Rule 164 of the Investment Bank Special Administration (England and Wales) Rules 2011 ("Rule 164"); or, in relation to a special administration (bank insolvency) or a special administration (bank administration), under Rule 164 as applied by Rule 165 of the Investment Bank Special Administration (England and Wales) Rules 2011 (each an "Insolvency Set-Off Rule").

SISO would, in our view, result in a net amount payable between the Parties in respect of such amounts, subject to the other qualifications set out in this opinion and subject also to the inclusion in any SISO of other mutual obligations between the Parties. The net amount payable between the Parties by result of SISO may be different from the amount that would have been payable under the Netting Provisions.

3.5.3 It should, however, be noted that, notwithstanding the preceding paragraph, certain amounts may be excluded from any SISO as follows.

- (a) If an amount due between the parties does not constitute a provable debt, SISO does not apply to that amount. A debt which is secured is not provable unless the secured party chooses to prove its debt rather than enforce its security. Accordingly, if the Clearing Member has provided security for its obligations in respect of Transactions, and such security is not waived, amounts due in respect of those Transactions would fall outside SISO to the extent of the security. However, in relation to collateral provided to the CCP in respect of the net obligation of the Clearing Member to the CCP, the restriction on SISO by virtue of the existence of security would apply to a set-off of the net obligation against other sums owing between the CCP and the Clearing Member, and would not operate so as to undermine the creation of the net obligation.
- (b) If an amount due between the parties is not "mutual" with any other amount due between them, SISO does not apply. For these purposes, "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:

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- (i) where a Party is acting as agent for another person, in which case sums owed by (or to) the agent acting in its capacity as such are not mutual with sums owed to (or by) it arising from obligations such Party incurs as principals;
- (ii) where a Party is acting as a trustee, in which case sums owed by (or to) the trustee acting in its capacity as such are not mutual with sums owed to (or by) it arising from obligations such Party incurs in its own interest;
- (iii) 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), in which case sums owed by (or to) the partnership are not mutual with sums owed to (or by) a partner acting in his or her or its own interest;
- (iv) 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 (including, without limitation, pursuant to section 111 of FSMA).

(c) SISO may also not apply to amounts which arise under Transactions entered into at certain times:

- (i) after the Clearing Member had entered administration;
- (ii) at a time when the CCP had notice that an application for an administration order in respect of the Clearing Member was pending or that any person had given notice of intention to appoint an administrator in respect of the Clearing Member;
- (iii) at a time when the CCP had notice that a meeting of creditors of the Clearing Member had been summoned under section 98 of the Insolvency Act 1986 (which requires a company which goes into creditors' voluntary winding-up to cause a meeting of creditors to be summoned for a day not later than the fourteenth day after the day on which there is to be held a shareholders' meeting at which the resolution for voluntary winding-up is to be proposed) or that a petition for the winding-up or an application for a bank insolvency order of the Clearing Member was pending; or

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- (iv) during a winding-up or bank insolvency of the Clearing Member,

and, where the court has made a recognition order in respect of a foreign main proceeding under the Cross-Border Insolvency Regulations in respect of the insolvent Clearing Member, it appears that an amount may also be excluded from a SISO if the Transaction under which such amount arose was entered into after the making of the recognition order, or after the CCP had notice that a recognition application was pending.

3.5.4 If the CCP commences Default Proceedings prior to the occurrence of a SISO Effective Date, section 159(4) of Part VII provides that a debt or other liability arising out of a Market Contract which is the subject of Default Proceedings may not be proved in a winding up or bankruptcy until the completion of the Default Proceedings. Further, any such debt or other liability shall not be taken into account for the purposes of any set-off until the completion of the Default Proceedings. However, sections 163(1)-(2) of Part VII provide that any net sum determined pursuant to the default rules of the CCP shall be provable or payable to the relevant insolvency office-holder and shall be taken into account for the purposes of any SISO in the same way as a debt due before the commencement of the Insolvency Proceedings. Accordingly, unless a SISO Effective Date has occurred prior to the commencement of the Default Proceedings, amounts payable in respect of Market Contracts which are subject to the Default Proceedings shall be excluded from any SISO, and only any net sum determined pursuant to the Applicable Member Default Netting Provisions shall be included in any SISO.

Further, even if the CCP has not commenced Default Proceedings in relation to the Clearing Member, to the extent that the Netting Provisions are protected by Part VII (as discussed in paragraph 3.4.2 above) the occurrence of a SISO Effective Date would not affect the effectiveness or enforceability of the Netting Provisions.

3.6 Conditions

There are no rules of law in this jurisdiction which would require the fulfilment of any conditions before the exercise of rights of set-off under the Netting Provisions. It is not the case, as far as the laws of this jurisdiction are concerned, that such rights are enforceable only on the occurrence of some future event.

4. QUALIFICATIONS

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

4.1 Banking Act 2009

- 4.1.1 The Banking Act 2009 (the "**Banking Act**") provides for various remedies for a failing UK bank, which include the ability of the Treasury or the Bank of England to cause the transfer of securities issued by a UK bank or property of a UK bank to another person, by means of a "*share transfer order*", a "*share transfer instrument*", or a "*property transfer instrument*".
- 4.1.2 Section 75 of the Banking Act gives power to the Treasury to change the law (except the Banking Act itself) for the purpose of enabling the powers granted to the Financial Conduct Authority, the Prudential Regulation Authority, the Treasury and the Bank of England under Part I of the Banking Act to be used effectively. Such changes might affect private law rights and might be used with retrospective effect. Furthermore, under sections 23 and 40, a share transfer instrument or order, or a property transfer instrument, may include incidental, consequential or transitional provisions which might have impact on private law rights.
- 4.1.3 A property transfer instrument may apply to only part of a UK bank's assets and liabilities (such a transfer being referred to as a "*partial property transfer*"). This may be the case because the property transfer instrument concerned expressly applies to only part of the UK bank's business or because it is ineffective in relation to foreign property, which may include Transactions or obligations arising under Transactions which are governed by the laws of a non-UK jurisdiction. A partial property transfer could apply so as to cause the transfer of some, but not all, of the Transactions (or obligations arising under Transactions), with the result that the ability to set-off or net the amounts due in respect of different Transactions against the amounts due in respect of others is impaired.

However, in this regard, Article 3 of the Banking Act 2009 (Restriction of Partial Property Transfers) Order 2009 (the "**Safeguards Order**") prohibits a partial property transfer which applies to some, but not all, of the "*protected rights and liabilities*" between a particular person and a UK bank. "**Protected rights and liabilities**" means rights and liabilities which a party is entitled to set off or net under a set-off arrangement, netting arrangement or title transfer Financial Collateral Arrangement, so long as they are not "*excluded rights*" or "*excluded liabilities*".

Accordingly, Article 3 of the Safeguards Order protects the Party which is not the affected UK bank against the adverse consequences of a partial property transfer affecting the Netting Provisions or Transactions except if any Transaction is not a "*relevant financial instrument*" as defined in the Safeguards Order, Article 3 may not apply in relation to that Transaction. For

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these purposes "*relevant financial instrument*" means: (a) an instrument listed in section C of Annex I to the Markets in Financial Instruments Directive (2004/39/EC), read with Chapter VI of the Commission Regulation 1287/2006/EC; (b) any option, future, swap, forward, contract for differences or other derivative contract not falling within (a); and (c) any combination of the foregoing, a deposit, a loan, an instrument falling within article 77 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (disregarding the exclusions in article 77(2)(b) to (d)) or any contract for the sale, purchase or delivery of transferable securities, currency of any country, territory or monetary union, any precious metal or any other commodity.

4.2 Other insolvency issues

- 4.2.1 In the case of a Clearing Member which is a UK Credit Institution, Regulation 34 of the Credit Institutions Regulations provides that the effect of a relevant reorganisation or a relevant winding up on a netting agreement shall be determined in accordance with the law applicable to that agreement. Accordingly, to the extent that the Member Default Netting Provisions or the CCP Default Netting Provisions constitute a netting agreement, whether or not the Member Default Netting Provisions would be enforceable following the commencement of Insolvency Proceedings would be a matter to be determined under that governing law and not by the law of this jurisdiction.
- 4.2.2 Under section 239 of the Insolvency Act 1986 anything done or suffered to be done by a company within a specified period ending with the onset of insolvency (being, in broad terms, the earliest of: the date of the commencement of winding-up; the date on which an administration application is made; the date of filing with the court of a notice of intention to appoint an administrator; or the date of the company entering administration; or, where the court has made a recognition order in respect of a foreign proceeding under the Cross-Border Insolvency Regulations, the date of opening of the foreign proceeding) of that company may be set aside as a preference. The thing done or suffered will be liable to be set aside if at the time it was done or suffered that company was unable to pay its debts or became unable to pay its debts within the meaning of section 123 of the Insolvency Act 1986 in consequence of the thing done or suffered and that thing has the effect of putting any person in a better position, in the event of that company going into insolvent liquidation, than that person would have been in if the thing had not been done or suffered. However, the court would not make such an order if it was satisfied that the company which gave the preference was not influenced to give it by a desire to put that person in such better position. In relation to a transfer of margin, we assume that the margin provider would not, in providing the margin, be influenced by a desire to put

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the margin taker in such a better position (although the margin provider's motivation is a matter of fact).

4.2.3 There are provisions in the Companies Act 2006 and the Insolvency Act 1986 for schemes of arrangement or voluntary arrangements in respect of companies to be agreed by creditors or, in some cases, shareholders of the company. The courts will not sanction a scheme of arrangement under sections 895-901 of the Companies Act 2006 unless reasonable efforts were made to notify those creditors whose rights would be affected by the scheme of the meeting to approve that scheme. In relation to voluntary arrangements under Part I of the Insolvency Act 1986, a creditor can be bound by the arrangement even if it has not been given notice of the creditors' meeting to approve the arrangement. In the case of either a scheme of arrangement or a voluntary arrangement, approval at the creditors' meeting of its terms does not require unanimity of the affected creditors, whether or not present at the meeting.

Such arrangements could affect both set-off rights of creditors and the value of claims which the creditors may have against the insolvent Party. If any set-off or netting had occurred pursuant to the Netting Provisions before the approval of such an arrangement, any provision of such an arrangement which purports to unwind the application of the Netting 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.

4.2.4 The courts of Scotland have exclusive jurisdiction in relation to liquidation of a Party incorporated under the laws of Scotland (a "**Scottish Party**"). Accordingly, the courts of this jurisdiction may defer to the courts of Scotland in relation to any question arising in Insolvency Proceedings relating to a Scottish Party.

4.2.5 The 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 426 of the Insolvency Act 1986, a court with insolvency law jurisdiction in England has a discretion to apply the law of one of a list of specified jurisdictions to the insolvency of an entity if so requested by the competent court of that other jurisdiction. Those

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specified jurisdictions are currently the other parts of the United Kingdom, the Channel Islands, the Isle of Man, Anguilla, Australia, the Bahamas, Bermuda, Botswana, Brunei, Canada, Cayman Islands, Falkland Islands, Gibraltar, Hong Kong, Ireland, Malaysia, Montserrat, New Zealand, South Africa, St. Helena, Turks and Caicos Islands, Tuvalu and the Virgin Islands. In exercising its discretion, the English court must have regard to the rules of private international law. However, in respect of the Member Default Netting Provisions, see the comments in paragraph 3.1.4.

4.2.6 Under the Cross-Border Insolvency Regulations, a court may recognise a foreign insolvency proceeding, and in consequence of such recognition may limit the application of English insolvency law, or apply certain of the provisions of English insolvency law at times, or in circumstances, where they would not otherwise be available. However, in respect of the Member Default Netting Provisions, see the comments in paragraph 3.1.4.

4.3 General

4.3.1 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, the English courts may recognise the extinction of those claims or liabilities. In particular, in relation to any Transaction which is governed by a law other than the law of this jurisdiction, such proceedings may affect whether or not that Transaction is available for inclusion in any netting or set-off pursuant to the Netting Provisions.

4.3.2 Where any Party to the Netting Provisions is vested with a discretion or may determine a matter in its opinion, that Party may be required to exercise its discretion in good faith, reasonably and for a proper purpose, and to form its opinion in good faith and on reasonable grounds. Any provision in the Netting Provisions providing that any calculation, determination or certification is to be conclusive and binding may not be effective if such calculation, determination or certification is fraudulent or manifestly incorrect and an English court may regard any certification, determination or calculation as no more than *prima facie* evidence.

4.3.3 If a Party is controlled by or otherwise connected with a person (or is itself) resident in, incorporated in or constituted under the laws of a country which is the subject of United Nations, European Community or UK sanctions implemented or effective in the United Kingdom under the United Nations Act 1946, the Emergency Laws (Re-enactments and Repeals) Act 1964 or the Anti-terrorism, Crime and Security Act 2001, or under the Treaty establishing the European Community, or is otherwise the target of any such sanctions,

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then the obligations of the other Party under the relevant agreement may be unenforceable or void.

5. CONCLUDING REMARKS

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

6. RELIANCE

6.1 This opinion is given for the benefit of the Futures and Options Association (the "**FOA**"). This opinion may be disclosed to:

- 6.1.1 the International Swaps and Derivatives Association, Inc. ("**ISDA**");
- 6.1.2 such of the FOA's members (excluding associate members) or ISDA's members (excluding associate members) as subscribe to the FOA's opinions library and whose terms of subscription give them access to this opinion (each a "**subscribing member**") and the officers, employees, and professional advisors of such subscribing member;
- 6.1.3 any affiliate of a subscribing member (being a member of the subscribing member's group, as defined by the UK Financial Services and Markets Act 2000) and the officers, employees, and professional advisors of such affiliate; and
- 6.1.4 the officers, employees and professional advisors of the FOA,

(each a "**Relevant Person**"). Each Relevant Person is authorised to make a copy of this opinion available to its auditors solely as evidential matter in support of their evaluation of a Relevant Person's management's assertion that the requirements of IAS 32 have been met, and a copy of this opinion may be furnished to them in connection therewith. In authorising Relevant Persons to make copies of this opinion available to their auditors for such purpose, we are not undertaking or assuming any duty or obligation to Relevant Persons or their auditors or establishing any lawyer-client relationship with them. Further, we do not undertake or assume any responsibility with respect to financial statements of any Relevant Person.

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6.2 We accept responsibility only to the FOA in relation to the matters opined on in this opinion.

Yours faithfully,

Christopher C. [Signature]

Clifford Chance LLP

SCHEDULE 1 DEFINITIONS

The following terms used in this opinion letter have the following meanings:

"BAU Netting Provisions" means, in respect of each Service, the rules identified as such in Annex 1 (*Clearing Rules and Netting Provisions*) (which are contained in the Rules).

"CCP" means, in respect of each Service, the entity identified as such in Annex 1 (*Clearing Rules and Netting Provisions*).

"CCP Default Netting Provisions" means, in respect of each Service, the rules identified as such in Annex 1 (*Clearing Rules and Netting Provisions*) (which are contained in the Rules).

"CCP Documentation" means, in respect of each Service, the documents, agreements, acts and other things pursuant to which the Rules are made contractually binding between the Parties.

"CCP Opinion" means the legal opinion issued by Clifford Chance Partnerschaftsgesellschaft dated 20 December 2013 entitled "IAS 32 – Germany – CCP – Pre-Opinion – Eurex (swaps, options and repos)".

"Clearing Member" means has the meaning given in the introduction to this opinion letter.

"Credit Institution Regulations" means the Credit Institutions (Reorganisation and Winding Up) Regulations 2004.

"Cross-Border Insolvency Regulations" means the Cross-Border Insolvency Regulations 2006.

"Default Proceedings" means default proceedings as defined in Part VII, being proceedings taken by the CCP pursuant to the Default Rules.

"Default Rules" means, in respect of each Service, those parts of the CCP Documentation for that Service which constitute "default rules" for the purposes of Part VII, being the rules of the CCP which provide for the taking of action in the event of a Clearing Member appearing to be unable, or likely to become unable, to meet its obligations in respect of one or more market Contracts connected with the CCP and includes, in the case of a recognised central counterparty, EEA central counterparty or third country central counterparty:

- (a) the default procedures referred to in Article 48 of EMIR; and
- (b) any rules of the CCP which provide for the taking of action in accordance with a request or instruction from a Clearing Member under the default procedures referred to in Article 4(4) of Commission Delegated Regulation No.149/2013 relating to

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EMIR in respect of assets or positions held by the CCP for the account of an indirect client or group of indirect clients.

"EEA Credit Institution" means an EEA Credit Institution as defined in the Credit Institutions Regulations, which means an EEA undertaking which qualifies as a credit institution under Directive 2000/12/EC but which is not a UK Credit Institution; and a reference to a **"UK Credit Institution"** is to a UK Credit Institution as so defined, which means an undertaking whose head office is in the United Kingdom with permission under Part IV of FSMA to accept deposits or to issue electronic money, but does not include insurance companies or credit unions within the meaning of section 31 of the Credit Unions Act 1979.

"EEA Designated System" means a system which has been designated for the purposes of the Settlement Finality Directive in another EEA State within the meaning of regulation 26(2)(a) of the Settlement Finality Regulations

"EEA Insurer" means an EEA Insurer as defined in the Insurers (Reorganisation and Winding Up) Regulations 2004.

"English Company" means a company which is formed and registered under the Companies Act 2006 or the former Companies Acts (as defined in section 1171 of the Companies Act 2006) and does not include a company formed and registered in Ireland under any of the former Companies Acts

"ESMA" means the European Securities and Markets Authority.

"EUIR" means Regulation (EU) No. 1346/2000 on insolvency proceedings.

"EMIR" means Regulation (EU) No. 648/2012 on OTC derivatives, central counterparties and trade repositories.

"FCA Regulations" means the Financial Collateral Arrangements (No. 2) Regulations 2003.

"Financial Collateral Arrangement" means an arrangement defined as such in the FCA Regulations.

"Foreign Company" is a company (other than a *"Societas Europaea"* established pursuant to EU Council Regulation No. 2157/2001 of 8 October 2001 on the European Company Statute) which is incorporated or formed under the laws of another jurisdiction with a branch or branches established or located in this jurisdiction.

"FSMA" means the Financial Services and Markets Act 2000.

"IAS 32" means International Accounting Standard 32.

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"Insolvency Proceedings" means:

- (a) liquidation (including provisional liquidation), administration, bank insolvency, bank administration, investment bank special administration, special administration (bank insolvency), special administration (bank administration), administrative receivership, receivership, voluntary arrangements and schemes of arrangement and, in the case of a small company (as defined in section 382 of the Companies Act 2006), a moratorium;² and
- (b) any analogous proceedings under the laws of any other jurisdiction,

and:

- (i) in relation to a UK bank, "**liquidator**" and "**administrator**" include a bank liquidator and bank administrator respectively; and, in relation to a UK investment bank, these terms include an individual appointed as administrator pursuant to the investment bank special administration procedure, the special administration (bank insolvency) procedure or the special administration (bank administration) procedure under the Investment Bank Regulations (each being an "**Insolvency Representative**"); and
- (ii) in relation to a UK bank, "**liquidation**" and "**administration**" include a bank insolvency and a bank administration respectively; and, in relation to a UK investment bank, these terms include an investment bank special administration, a special administration (bank insolvency) and/or a special administration (bank administration) under the Investment Bank Regulations, as the context may require;

"Investment Bank Regulations" means the Investment Bank Special Administration Regulations 2011.

"Market Contract" means a market contract as defined in section 155 of Part VII and includes, for the purposes of this opinion, any Transaction entered into between the Clearing Member and the CCP.³

"Member Default Netting Provisions" means, in respect of each Service, the rules identified as such Annex 1 (*Clearing Rules and Netting Provisions*) (which are contained in the Rules).

² Note, the proposed special administration regime for investment firms is expected to be introduced in either late 2013 or early 2014. At this stage, the information available in respect of this proposed regime is not sufficient for this to be addressed in this opinion.

³ Part VII 155(2B)(a)-(b) (in relation to a recognised central counterparties) and 155(3) (in relation to a recognised clearing house which is not a recognised central counterparty).

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"Netting Provisions" means, in respect of each Service, the BAU Netting Provisions, the CCP Default Netting Provisions and the Member Default Netting Provisions in respect of that Service.

"Part VII" means Part VII of the Companies Act 1989, together with the provisions of Parts II and IV of the Schedule to the Recognition Requirements Regulations.

"Party" means the CCP or the Member and a reference to "Parties" is a reference to the CCP and a particular Member

"Recognition Requirements Regulations" means the Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations 2001.

"Rules" means, in respect of each Service, the rules of the CCP in force as at 30 September 2013. Except where otherwise defined herein, terms defined in the Rules of the CCP have the same meaning in this opinion letter.

"Service" means a clearing service identified in Annex 1 (*Service and Netting Provisions*).

"Settlement Finality Directive" means Directive 98/26/EC of the European Council on settlement finality in payment and securities settlement systems.

"Settlement Finality Regulations" means the Financial Markets and Insolvency (Settlement Finality) Regulations 1999.

"SISO" means has the meaning given to it in paragraph 3.5.2.

"SISO Effective Date" means:

- (a) in respect of any SISO which takes effect pursuant to Rule 4.90 of the Insolvency Rules 1986, the date on which a winding up order is made in respect of the Clearing Member;
- (b) in respect of any SISO which takes effect pursuant to Rule 2.85 of the Insolvency Rules 1986, the date on which the administrator gives notice under Rule 2.95 of the Insolvency Rules 1986 of a proposed distribution;
- (c) in respect of any SISO which takes effect pursuant to Rule 72 of the Bank Insolvency (England and Wales) Rules 2009, the date on which a winding up order is made in respect of the Clearing Member; or
- (d) in respect of any SISO which takes effect pursuant to Rule 164 of the Investment Bank Special Administration (England and Wales) Rules 2011, the date on which the

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administrator gives notice under Rule 175 of the Investment Bank Special Administration (England and Wales) Rules 2011 of a proposed distribution.

"Transaction" means, in respect of a Service, a transaction which is registered at the CCP in respect of the Service.

"UK bank" means an undertaking incorporated in or formed under the law of any part of the United Kingdom and having its head office in the United Kingdom, which has permission under Part IV of FSMA to accept deposits; but for the purposes of this opinion does not include insurance companies or credit unions within the meaning of section 31 of the Credit Unions Act 1979.

"UK Clearing House" means a recognised clearing house incorporated in the United Kingdom which is not a Recognised Central Counterparty.

"UK investment bank" means an undertaking to which the Investment Bank Regulations apply (being, broadly, an institution which is incorporated in the United Kingdom, authorised under FSMA to safeguard and administer investments or deal in investments as principal or agent, and holds assets for clients).

ANNEX 1

SERVICE AND NETTING PROVISIONS

Service	CCP	CCP Type	Applicable Amounts ¹	BAU Netting Provisions	Member Default Netting Provisions	CCP Default Netting Provisions
Eurex (options and interest rate swaps)	Eurex Clearing AG	Recognised Overseas Clearing House	variation margin other amounts payable in respect of Transactions	Chapter I, Part 1, Condition 1.3.1 Chapter I, Part 3, sub-part A, Condition 2.3	Chapter I, Part 1, Condition 7.2.1 Chapter I, Part 1, Condition 7.3	Chapter I, Part 1, Condition 9

¹ Terms used in this column have the meanings given to them in the Rules.