

2006 MODEL NETTING ACT¹

Part I : Netting

1. Definitions

In this Act:

"Bank" means the Central Bank of [*insert applicable jurisdiction*];

"cash" means money credited to an account in any currency, or a similar claim for repayment of money, such as a money market deposit;

"collateral" means any of the following:

- (i) cash in any currency;
- (ii) securities of any kind, including (without limitation) debt and equity securities;
- (iii) guarantees, letters of credit and obligations to reimburse; and
- (iv) any asset commonly used as collateral in [*insert applicable jurisdiction*];

"collateral arrangement" means any margin, collateral or security arrangement or other credit enhancement related to or forming part of a netting agreement or one or more qualified financial contracts entered into thereunder, including (without limitation):

- (i) a pledge or any other form of security interest in collateral, whether possessory or non possessory;
- (ii) a title transfer collateral arrangement; and
- (iii) any guarantee, letter of credit or reimbursement obligation by or to a party to one or more qualified financial contracts, in respect of those qualified financial contracts;

"insolvent party" is the party in relation to which an insolvency proceeding under the laws of [*insert applicable jurisdiction*] has been instituted;

"liquidator" means the liquidator, receiver, trustee, conservator or other person or entity which administers the affairs of an insolvent party during an insolvency proceeding under the laws of [*insert applicable jurisdiction*];

"netting" means the occurrence of any or all of the following:

- (i) the termination, liquidation and/or acceleration of any payment or delivery obligations or entitlements under one or more qualified financial contracts entered into under a netting agreement;
- (ii) the calculation or estimation of a close-out value, market value, liquidation value or replacement value in respect of each obligation or entitlement or group of obligations or entitlements terminated, liquidated and/or accelerated under (i);

¹ Version 2, incorporating minor revisions to version 1 published in March 2006.

(iii) the conversion of any values calculated or estimated under (ii) into a single currency; and

(iv) the determination of the net balance of the values calculated under (ii), as converted under (iii), whether by operation of set-off or otherwise;

"netting agreement" means (i) any agreement between two parties that provides for netting of present or future payment or delivery obligations or entitlements arising under or in connection with one or more qualified financial contracts entered into under the agreement by the parties to the agreement (a "master netting agreement"), (ii) any master agreement between two parties that provides for netting of the amounts due under two or more master netting agreements (a "master-master netting agreement") and (iii) any collateral arrangement related to or forming part of one or more of the foregoing;

"non-insolvent party" is the party other than the insolvent party;

"party" means a person constituting one of the parties to a netting agreement;

"person" includes [individuals], [partnerships], [corporations], [regulated entities such as banks, insurance companies and broker-dealers], [or any other body corporate whether organized under the laws of *[insert applicable jurisdiction]* or under the laws of any other jurisdiction], [and any unit or political sub-division of central or regional government], [and any international or regional development bank or other international or regional organization];

"qualified financial contract" means any financial agreement, contract or transaction, including any terms and conditions incorporated by reference in any such financial agreement, contract or transaction, pursuant to which payment or delivery obligations are due to be performed at a certain time or within a certain period of time and whether or not subject to any condition or contingency. Qualified financial contracts include (without limitation):

- (a) a currency, cross-currency or interest rate swap;
- (b) a basis swap;
- (c) a spot, future, forward or other foreign exchange transaction;
- (d) a cap, collar or floor transaction;
- (e) a commodity swap;
- (f) a forward rate agreement;
- (g) a currency or interest rate future;
- (h) a currency or interest rate option;
- (i) an equity derivative, such as an equity or equity index swap, equity forward, equity option or equity index option;
- (j) a derivative relating to bonds or other debt securities or to a bond or debt security index, such as a total return swap, index swap, forward, option or index option;
- (k) a credit derivative, such as a credit default swap, credit default basket swap, total return swap or credit default option;
- (l) an energy derivative, such as an electricity derivative, oil derivative, coal derivative or gas derivative;
- (m) a weather derivative, such as a weather swap or weather option;
- (n) a bandwidth derivative;
- (o) a freight derivative;
- (p) an emissions derivative, such as an emissions allowance or emissions reduction transaction;
- (q) an economic statistics derivative, such as an inflation derivative;
- (r) a property index derivative;
- (s) a spot, future, forward or other securities or commodities transaction;
- (t) a securities contract, including a margin loan and an agreement to buy, sell, borrow or lend securities, such as a securities repurchase or reverse repurchase agreement, a securities

- lending agreement or a securities buy/sell-back agreement, including any such contract or agreement relating to mortgage loans, interests in mortgage loans or mortgage-related securities;
- (u) a commodities contract, including an agreement to buy, sell, borrow or lend commodities, such as a commodities repurchase or reverse repurchase agreement, a commodities lending agreement or a commodities buy/sell-back agreement;
 - (v) a collateral arrangement;
 - (w) an agreement to clear or settle securities transactions or to act as a depository for securities;
 - (x) any other agreement, contract or transaction similar to any agreement, contract or transaction referred to in paragraphs (a) to (w) with respect to one or more reference items or indices relating to (without limitation) interest rates, currencies, commodities, energy products, electricity, equities, weather, bonds and other debt instruments, precious metals, quantitative measures associated with an occurrence, extent of an occurrence, or contingency associated with a financial, commercial or economic consequence, or economic or financial indices or measures of economic or financial risk or value ;
 - (y) any swap, forward, option, contract for differences or other derivative in respect of, or combination of, one or more agreements or contracts referred to in paragraphs (a) to (x); and
 - (z) any agreement, contract or transaction designated as such by the Bank under this Act;

"title transfer collateral arrangement" means a margin, collateral or security arrangement related to a netting agreement based on the transfer of title to collateral, whether by outright sale or by way of security, including (without limitation) a sale and repurchase agreement, securities lending agreement, securities buy/sell-back agreement or an irregular pledge.

2. **Powers of the Bank.** The Bank may, by notice issued under this section, designate as "qualified financial contracts" any agreement, contract or transaction, or type of agreement, contract or transaction, in addition to those listed in this Act.

3. **Enforceability of a Qualified Financial Contract.** A qualified financial contract shall not be and shall be deemed never to have been void or unenforceable by reason of [*insert the applicable law*] relating to games, gaming, gambling, wagering or lotteries.

4. **Enforceability of a Netting Agreement.**

(a) **General rule.** The provisions of a netting agreement will be enforceable in accordance with their terms, including against an insolvent party, and, where applicable, against a guarantor or other person providing security for a party and will not be stayed, avoided or otherwise limited by

- (i) any action of the liquidator,
- (ii) any other provision of law relating to bankruptcy, reorganization, composition with creditors, receivership, conservatorship or any other insolvency proceeding an insolvent party may be subject to, or
- (iii) any other provision of law that may be applicable to an insolvent party,

subject to the conditions contained in the applicable netting agreement.

(b) **Limitation on obligation to make payment or delivery.** After commencement of insolvency proceedings in relation to a party, the only obligation, if any, of either party to make payment or delivery under a netting agreement shall be equal to its net obligation to the other party as determined in accordance with the terms of the applicable netting agreement.

(c) Limitation on right to receive payment or delivery. After commencement of insolvency proceedings in relation to a party, the only right, if any, of either party to receive payment or delivery under a netting agreement shall be equal to its net entitlement with respect to the other party as determined in accordance with the terms of the applicable netting agreement.

(d) Limitation on powers of the liquidator. Any powers of the liquidator to assume or repudiate individual contracts or transactions will not prevent the termination, liquidation and/or acceleration of all payment or delivery obligations or entitlements under one or more qualified financial contracts entered into under or in connection with a netting agreement, and will apply, if at all, only to the net amount due in respect of all of such qualified financial contracts in accordance with the terms of such netting agreement;

(e) Limitation of insolvency laws prohibiting set-off. The provisions of a netting agreement which provide for the determination of a net balance of the close-out values, market values, liquidation values or replacement values calculated in respect of accelerated and/or terminated payment or delivery obligations or entitlements under one or more qualified financial contracts entered into thereunder will not be affected by any applicable insolvency laws limiting the exercise of rights to set off, offset or net out obligations, payment amounts or termination values owed between an insolvent party and another party.

(f) Preferences and fraudulent transfers. The liquidator of an insolvent party may not avoid:

(i) any transfer, substitution or exchange of cash, collateral or any other interests under or in connection with a netting agreement from the insolvent party to the non-insolvent party; or

(ii) any payment or delivery obligation incurred by the insolvent party and owing to the non-insolvent party under or in connection with a netting agreement

on the grounds of it constituting a [preference] [transfer during a suspect period] by the insolvent party to the non-insolvent party, unless there is clear and convincing evidence that the non-insolvent party (i) made such transfer or (ii) incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the insolvent party was indebted or became indebted, on or after the date (i) such transfer was made or (ii) such obligation was incurred.

(g) Preemption. No stay, injunction, avoidance, moratorium, or similar proceeding or order, whether issued or granted by a court, administrative agency, liquidator or otherwise, shall limit or delay application of otherwise enforceable netting agreements in accordance with subsections (a), (b) and (c) of this section of this Act.

(h) Realization and liquidation of collateral. Unless otherwise agreed by the parties, the realization, appropriation and/or liquidation of collateral under a collateral arrangement shall take effect or occur without any requirement that prior notice shall be given to, or consent be received from, any party, person or entity, provided that this subsection is without prejudice to any applicable provision of law requiring that the realization, appropriation and/or liquidation of collateral is conducted in a commercially reasonable manner.

(i) Scope of this provision.

(i) For the purposes of this section, a netting agreement shall be deemed to be a netting agreement notwithstanding the fact that such netting agreement may contain provisions relating to agreements, contracts or transactions that are not qualified financial contracts in terms of Part I section 1 of this Act, provided, however, that, for the purposes of this section, such netting agreement shall be deemed to be a netting agreement only with respect to those

agreements, contracts or transactions that fall within the definition of "qualified financial contract" in Part I section 1 of this Act.

(ii) For the purposes of this section, a collateral arrangement shall be deemed to be a collateral arrangement notwithstanding the fact that such collateral arrangement may contain provisions relating to agreements, contracts or transactions that are not a netting agreement or qualified financial contract entered into thereunder in terms of Part I section 1 of this Act, provided, however, that, for the purposes of this section, such collateral arrangement shall be deemed to be a collateral arrangement only with respect to those agreements, contracts or transactions that fall within the definition of "netting agreement" or "qualified financial contract" entered into thereunder in Part I section 1 of this Act.

(iii) For the purposes of this section, a netting agreement and all qualified financial contracts entered into thereunder shall constitute a single agreement.

(iv) For the purposes of this section, the term "netting agreement" shall include the term "multibranch netting agreement" (as defined in Part II of this Act), provided, however, that in a separate insolvency of a branch or agency of a foreign party (as defined in Part II of this Act) in [*insert applicable jurisdiction*] the enforceability of the provisions of the multibranch netting agreement shall be determined in accordance with Part II of this Act.

Part II : Multibranch Netting

1. Additional Definitions

In this Act:

"branch/agency net payment entitlement" means with respect to a multibranch netting agreement the amount, if any, that would have been owed by the non-insolvent party to the foreign party after netting only those qualified financial contracts entered into by the non-insolvent party with the branch or agency of the foreign party in [*insert applicable jurisdiction*] under such multibranch netting agreement.

"branch/agency net payment obligation" means with respect to a multibranch netting agreement the amount, if any, that would have been owed by the foreign party to the non-insolvent party after netting only those qualified financial contracts entered into by the non-insolvent party with the branch or agency of the foreign party in [*insert applicable jurisdiction*] under such multibranch netting agreement;

"foreign party" is a party whose home country is a country other than [*insert applicable jurisdiction*];

"global net payment entitlement" means the amount, if any, owed by the non-insolvent party (or that would be owed if the relevant multibranch netting agreement provided for payments to either party, upon termination of qualified financial contracts thereunder, under any and all circumstances) to the foreign party as a whole after giving effect to the netting provisions of a multibranch netting agreement with respect to all qualified financial contracts subject to netting under such multibranch netting agreement;

"global net payment obligation" means the amount, if any, owed by the foreign party as a whole to the non-insolvent party after giving effect to the netting provisions of a multibranch netting agreement with respect to all qualified financial contracts subject to netting under such multibranch netting agreement;

"home country" means the country where a party to a netting agreement is organized or incorporated;

"home office" means the home country office of a party to a netting agreement that is a bank;

"multibranch netting agreement" means a netting agreement between two parties under which at least one party enters into qualified financial contracts through – in addition to its home office – one or more of its branches or agencies located in countries other than its home country;

"party" means, for purposes of this Part II of this Act, a person constituting one of the parties to a multibranch netting agreement.

2. **Enforceability of a Multibranch Netting Agreement in an Insolvency of a Branch or Agency of a Foreign Party.**

(a) Limitation on the non-insolvent party's right to receive payment.

(i) The liability of an insolvent branch or agency of a foreign party or its liquidator in [*insert applicable jurisdiction*] under a multibranch netting agreement shall be calculated as of the date of the termination of the qualified financial contracts entered into under such multibranch netting agreement in accordance with its terms and shall be limited to the lesser of (i) the global net payment obligation and (ii) the branch/agency net payment obligation. The liability under this section of the insolvent branch or agency of the foreign party or its the liquidator shall be reduced by any amount otherwise paid to or received by the non-insolvent party in respect of the global net payment obligation pursuant to such multibranch netting agreement which if added to the liability of the liquidator under this section would exceed the global net payment obligation.

(ii) The liability of the liquidator of an insolvent branch or agency of a foreign party under a multibranch netting agreement to the non-insolvent party shall be reduced by the fair market value of, or the amount of any proceeds of, collateral that secures or supports the obligations of the foreign party under the multibranch netting agreement and has been applied to satisfy the obligations of the foreign party pursuant to the multibranch netting agreement to the non-insolvent party.

(b) Limitation on the foreign party's rights to receive payment based on payments made in accordance with insolvency proceedings relating to the foreign party in other jurisdictions. The liability of the non-insolvent party under this section shall be reduced by any amount otherwise paid to or received by the liquidator or any other liquidator or receiver of the foreign party in its home country or any other country in respect of the global net payment entitlement pursuant to such multibranch netting agreement which if added to the liability of the non-insolvent party under this section would exceed the global net payment entitlement. The liability of the non-insolvent party under this section to the liquidator pursuant to such multibranch netting agreement also shall be reduced by the fair market value of, or the amount of any proceeds of, collateral that secures or supports the obligations of the non-insolvent party and has been applied to satisfy the obligations of the non-insolvent party pursuant to such multibranch netting agreement to the foreign party.

3. **Limitation on the terms of the multibranch netting agreement relating to a collateral arrangement.** The non-insolvent party to a multibranch netting agreement which has a perfected security interest in collateral, or other valid title, lien or security interest in collateral enforceable against third parties pursuant to such multibranch netting agreement, may retain all such collateral and upon termination of such multibranch netting agreement in accordance with its terms apply such collateral in satisfaction of any claims secured by the collateral, provided that the total amount so applied to such claims shall in no event exceed the global net payment obligation, if any. Any excess collateral shall be returned to the foreign party.