



2018 ISDA Model Netting Act and Guide

International Swaps and Derivatives Association, Inc.

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TABLE OF CONTENTS

INTRODUCTION.....		i
1. THE IMPORTANCE AND BENEFITS OF CLOSE-OUT NETTING.....		1
2. THE OBJECTIVES OF NETTING LEGISLATION.....		6
3. DEFINING THE SCOPE OF NETTING LEGISLATION.....		8
Defining the product scope of netting legislation.....		8
Defining the counterparty scope of netting legislation.....		10
Defining “netting agreement” and “netting”.....		11
4. CONFIRMING THE ENFORCEABILITY OF NETTING AGREEMENTS.....		14
Enforceability outside of insolvency proceedings.....		15
Enforceability in the case of insolvency proceedings.....		16
Enforceability in the case of financial institution resolution.....		19
5. MULTIBRANCH NETTING.....		19
6. GOVERNING LAW APPROACH TO ENSURING ENFORCEABILITY OF CLOSE-OUT NETTING.....		20
7. PROVISION-BY-PROVISION COMMENTARY.....		23
Drafting approach and structure of the 2018 MNA		23
Part I (Netting): section 1 (Definitions).....		24
Part I (Netting): section 2 (Powers of the Authority).....		25
Part I (Netting): section 3 (Enforceability of a Qualified Financial Contract).....		26
Part I (Netting): section 4 (Enforceability of a Netting Agreement).....		26
Optional Part II (Multibranch Netting): section 1 (Additional Definitions).....		29
Optional Part II (Multibranch Netting): section 2 (Enforceability of a Multibranch Netting Agreement against an Insolvent Local Branch).....		31
Optional Part II (Multibranch Netting): section 3 (Collateral for a Multibranch Netting Agreement).....		32

APPENDIX A	2018 ISDA Model Netting Act.....	33
APPENDIX B	2013 UNIDROIT Principles on the Operation of Close-out Netting Provisions.....	43
APPENDIX C	ISDA Netting and Collateral Opinions.....	47
APPENDIX D	Status of Netting Legislation.....	51
APPENDIX E	Differences between the 2018 and 2006 versions of the Model Netting Act.....	55

INTRODUCTION

In Appendix A to this Guide the International Swaps and Derivatives Association, Inc. (“ISDA”) publishes the 2018 Model Netting Act (the “2018 MNA”). The 2018 MNA is a model law intended to set out, by example, the basic principles necessary to ensure the enforceability of bilateral close-out netting, including bilateral close-out netting on a multibranch basis, as well as the enforceability of related financial collateral or margin arrangements.¹

The 2018 MNA is an updated version of our 2006 Model Netting Act,² which was in turn an updated version of our 2002 Model Netting Act,³ itself an updated version of our original Model Netting Act published in 1996. The 1996, 2002 and 2006 Model Netting Acts have each been used successfully as models for netting legislation in a number of jurisdictions and as a guide for policy makers and educators as to the basic principles that should underlie a comprehensive statutory regime for close-out netting.

The revisions to the Model Netting Act in 2002 and then again 2006 took into account developments in the financial markets by extending the coverage of the Model Netting Act to reflect the evolution of new products and the extension of the protection to financial collateral arrangements entered into in connection with a netting agreement.⁴ Notwithstanding the financial crisis of 2008, it has not until relatively recently been considered necessary to revise the 2006 Model Netting Act, which continues to provide a strong template for a broad and effective legislative regime for close-out netting.

This new edition of the Model Netting Act reflects recent developments in the financial markets, in particular over the last ten years the widespread adoption of bank and other financial institution resolution regimes, the phased introduction of mandatory initial and variation margin requirements for most of the wholesale derivatives markets and the continued growth of Islamic finance derivatives.

ISDA has found that an increasing number of jurisdictions are seeking guidance on the implementation of a comprehensive legislative regime for close-out netting and related financial collateral arrangements in order to increase the safety, efficiency and international competitiveness of their domestic financial markets and to improve access to the international financial markets for their leading financial institutions and large end users. ISDA has prepared this updated guidance to meet that need.

The purpose of this Guide is to provide practical advice and guidance to governmental officials and other policy makers in countries that are currently considering implementing netting legislation. In preparing this guidance, we have drawn on:

¹ In this Guide we refer to “netting law” or “netting legislation” and to “netting” or “close-out netting” for ease of reference. All of these references are intended to encompass both the close-out netting and financial collateral aspects of the legislation. The terms “financial collateral” and “margin” are, unless context indicates otherwise, used interchangeably in this Guide.

² In connection with the 2006 Model Netting Act, ISDA published a “Memorandum on the Implementation of Netting Legislation: A Guide for Legislators and Other Policy-Makers” dated March 2006. This Guide incorporates, updates and extends that guidance, applying it to the 2018 MNA.

³ See Thomas J Werlen and Sean M Flanagan, “The 2002 Model Netting Act: A Solution for Insolvency Uncertainty”, *Butterworths Journal of International Banking and Financial Law* (April 2002), pp 154-164, for a detailed discussion of the 2002 Model Netting Act, including the background to the development of that version of the Model Netting Act as well as the original version published in 1996.

⁴ Note that the terms “netting agreement” and “master agreement” mean the same thing. In this Guide and in the text of the 2018 MNA set out in Appendix A, the term “netting agreement” is used for consistency. Each version of the ISDA Master Agreement is an example of a netting agreement, as defined in the 2018 MNA. For further detail, see the discussion in part 3 and in para 7.6 of this Guide.

- Our experience over the past 30 years of dialogue with law makers, regulators and other government officials in countries around the world, from a variety of legal traditions, seeking to implement netting legislation locally in order to strengthen and modernize their national financial markets and to ensure the competitiveness of their leading financial institutions and other professional financial market participants in the global marketplace
- Our collection of detailed reasoned legal opinions, annually updated, on close-out netting under the ISDA Master Agreements from over sixty jurisdictions⁵

In preparing this Guide, we have had regard to the experience and concerns of civil law as well as common law jurisdictions. We intend the general principles discussed in this Guide to be of assistance to national authorities in jurisdictions representing all legal traditions. We recognize that in many countries it will not necessarily be feasible, as a matter of theory or practice, to implement the 2018 MNA *verbatim* in the form in which we have published it in Appendix A. This Guide provides guidance as to how legislators in civil law jurisdictions might, in principle, adapt their legislation to give effect to the substantive provisions of the 2018 MNA.

In preparing the 2018 MNA we have sought to avoid using legal concepts that would be specific to a given legal culture, for example, common law as opposed to civil law. The 2018 MNA is generic in the sense that its provisions are self-contained and generally do not rely on jurisdiction-specific concepts.

We are aware that actual netting legislation sharing the same purpose as the 2018 MNA will often need to be in a form which substantially differs from the generic form set out in the 2018 MNA. This may be for a variety of reasons, ranging from technical (for example, taking into account existing local legal concepts or doctrines) to legal cultural (for example, the detailed style of drafting adopted in the 2018 MNA may be considered inappropriate in jurisdictions of the civil law tradition).

We demonstrate in this Guide how the 2018 MNA may, nonetheless, be used even in civil law jurisdictions as a starting point for the preparation of appropriate legislation. We also make certain methodological suggestions to facilitate the effective translation of the provisions of the 2018 MNA into a body of provisions that takes into account these various local requirements while achieving effectively the purposes of the 2018 MNA.

This Guide does not necessarily deal with all issues that might arise in a particular jurisdiction seeking to implement netting legislation that meets local economic, social and other relevant policy requirements and that is appropriately adapted to local conditions and the local legal culture. ISDA is always willing to provide further assistance and practical support, including information regarding global financial market practice, to national lawmakers, regulators and other government officials engaged in developing netting legislation or other law reform initiatives relating to the financial markets. Any requests for such assistance may be directed, confidentially if appropriate, to the Chief

⁵ A list of the jurisdictions from which ISDA has obtained netting and collateral opinions appears on the ISDA website at www.isda.org, together with a list of the jurisdictions around the world that have enacted or are considering enacting netting legislation. See also Appendices C and D for the position as at the date of publication of this Guide. In relation to a number of countries for which ISDA has not yet commissioned a full netting opinion, ISDA has obtained from local counsel a memorandum regarding various legal issues in that country, which ISDA refers to as an **informal country update**. An informal country update is not a legal opinion and cannot be relied upon as such. It is simply general guidance, intended to be helpful to ISDA members interested in dealing with derivative market participants organized or based in the relevant country. A list of countries from which ISDA has obtained an informal country update from local counsel appears on the ISDA website at www.isda.org.

Executive Officer or to the General Counsel of ISDA, details of whom are available on the ISDA website at www.isda.org.

THIS GUIDE IS INTENDED AS GENERAL GUIDANCE TO GOVERNMENTAL OFFICIAL AND OTHER POLICY MAKERS, ALTHOUGH THE GUIDE MAY ALSO BE OF INTEREST TO OTHER PERSONS INVOLVED AND/OR INTERESTED IN THE FINANCIAL MARKETS. THIS GUIDE SHOULD NOT BE CONSIDERED TO BE LEGAL ADVICE OR RELIED ON AS SUCH. PARTIES SHOULD CONSULT WITH THEIR LEGAL ADVISERS AND ANY OTHER ADVISER THEY DEEM APPROPRIATE PRIOR TO MAKING ANY DECISION IN RELATION TO ANY ISSUE RAISED BY OR CONSIDERED IN THIS GUIDE. MORE GENERALLY, ISDA ASSUMES NO RESPONSIBILITY FOR ANY USE TO WHICH THIS GUIDE OR ANY OTHER DOCUMENT, DEFINITION OR PROVISION IT HAS PUBLISHED MAY BE PUT.

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2018 ISDA MODEL NETTING ACT AND GUIDE

1. THE IMPORTANCE AND BENEFITS OF CLOSE-OUT NETTING

- 1.1 Close-out netting of derivative transactions under a netting agreement, such as the ISDA Master Agreement,⁶ is the single most important mechanism for reduction of credit risk in the derivatives market.
- 1.2 The nature and mechanism of close-out netting is discussed in some detail in paragraphs 3.18 to 3.24 of this Guide, but it may be broadly defined as a contractual process set out in a netting agreement under which, following an event of default or termination event,⁷ the following three stages occur:
 - (a) Transactions under the netting agreement are terminated by notice given by the non-defaulting party or, in certain circumstances,⁸ automatically.
 - (b) The terminated transactions are valued at their current mark-to-market value (that is, replacement value) at or about the time of early termination.
 - (c) A net balance is calculated equal to the difference between (i) the aggregate mark-to-market value of terminated transactions “in the money” to the non-defaulting party and (ii) the aggregate mark-to-market value of terminated transactions “out of the money” to the non-defaulting party. If (i) exceeds (ii), the net amount is paid to the non-defaulting party. If (ii) exceeds (i), the net amount is, normally,⁹ paid to the defaulting party.
- 1.3 Close-out netting should be distinguished from payment netting. Payment netting takes place during the normal business of a solvent firm and involves combining offsetting cash flow obligations between two parties on a given day in a given currency into a single net payable or receivable. Its purpose is to facilitate efficient settlement and to reduce settlement risk. As it operates prior to a default or termination event, its enforceability does not normally need to be

⁶ References in this Guide to the “ISDA Master Agreement” apply equally to each version of the ISDA Master Agreement published in 1987, 1992 and 2002, unless context indicates otherwise. References to specific provisions of the ISDA Master Agreement are to the provisions of the ISDA 2002 Master Agreement, but, unless context indicates otherwise, those references apply equally to the corresponding provisions of earlier versions of the ISDA Master Agreement. A capitalized term used without definition in this Guide has the meaning given to that term in the ISDA Master Agreement, unless context indicates otherwise. For example, when we refer to a “termination event”, we are referring generically to an event the occurrence of which gives one or both parties the right to terminate relevant transactions governed by a netting agreement in circumstances not involving a default. When we refer to “Termination Event”, we are referring to that term as defined in Section 14 of the ISDA Master Agreement.

⁷ Where we refer in this Guide to a “termination event”, as opposed to an “event of default”, we are referring to a provision entitling a party to terminate early some or all of the transactions under the netting agreement as a result of the occurrence of an event that is not characterized as a default of a party under the netting agreement. Examples include the Termination Events set out in Section 5(b) of the ISDA 2002 Master Agreement, which allow one or both parties to terminate relevant transactions upon the occurrence of events such as illegality, force majeure, imposition of withholding tax and so on.

⁸ Principally, in relation to certain formal steps that may occur in relation to the opening of insolvency proceedings against the defaulting party. In the 1992 and 2002 versions of the ISDA Master Agreement, automatic early termination only applies if the parties make an election to that effect.

⁹ Under the 1987 Interest Rate and Currency Exchange Agreement and, if “First Method” was elected by the parties, under the 1992 ISDA Master Agreement, no payment was due from non-defaulting party to the defaulting party in circumstances where (ii) exceeded (i). In the 1994 revision of the Basel Capital Accord, the Basel Committee of Banking Supervisors dubbed such a provision a “walk-away clause” and said that close-out netting under a netting agreement containing such a clause would not be eligible for recognition as risk-reducing for regulatory capital purposes. For this reason, it is no longer commonly used in netting agreements.

protected by legislation. In this Guide we are only concerned with close-out netting and not payment netting.¹⁰

- 1.4 Statistics published each year by the Bank for International Settlements consistently show that close-out netting reduces the gross mark-to-market value of outstanding derivative transactions across all asset classes by over 80 per cent. For example, netting benefit, measured as the difference between gross mark-to-market value and credit exposure after netting was over 85 per cent as of mid-2009.¹¹ A similar measure for banks chartered in the United States was even greater, at about 90 per cent of mark-to-market value.¹²
- 1.5 Financial collateral (also known as “margin”)¹³ for derivatives is taken to secure the net exposure of the collateral taker under a netting agreement.¹⁴ Close-out netting is therefore the primary form of credit risk reduction used in the global derivatives market. Financial collateral deals only with the net credit exposure that remains. Upon a default, close-out netting occurs first and only then is financial collateral applied. Under a title transfer based financial collateral arrangement, enforcement typically occurs via the close-out netting mechanism.
- 1.6 Close-out netting and financial collateral are closely related and interdependent concepts. It is important therefore that netting legislation should deal not only with close-out netting in the strict sense, but also with financial collateral. This is especially so given the increasing importance of financial collateral in the regulatory regime that has been developed and implemented globally since the financial crisis, as discussed in more detail below.
- 1.7 The importance of close-out netting and financial collateral for ensuring the stability and resilience of the financial system has been noted and emphasised by regulatory authorities around the world, including international bodies such as the Basel Committee on Banking Supervision (BCBS) and the Financial Stability Board (FSB).
- 1.8 In March 2010 the BCBS said the following:

“Much progress has been made over the last two decades in achieving legal certainty for close-out netting of financial contracts and collateral arrangements. Legal reform efforts have successfully been adopted in most major jurisdictions, especially for the termination, liquidation and close-out netting of OTC bilateral financial contracts upon an event of default, including an insolvency event, at a banking institution. Less progress has been

¹⁰ There is a third form of netting known as netting by novation. It is similar to payment netting in that it operates prior to a default only and is principally intended to reduce settlement risk. It is more complicated operationally than payment netting. It developed originally as a risk reduction technique in the foreign exchange market, but that usage fell away when close-out netting under a netting agreement was first recognised as eligible, subject to conditions, for recognition as risk-reducing under the Basel Capital Accord as amended in 1994. It remains relevant to multilateral netting arrangements operated by clearing houses and central clearing counterparties. Because it operates prior to default, it does not give rise to the same legal issues as close-out netting and is therefore not further discussed in this Guide.

¹¹ See David Mengle, “The Importance of Close-Out Netting” (ISDA Research Note, No 1, 2010), available from the ISDA website at <http://www.isda.org>.

¹² Ibid.

¹³ See n 1.

¹⁴ Financial collateral arrangements to secure the gross exposure of the collateral taker in respect of derivative transactions is comparatively rare and is generally only used where there is a material doubt about the enforceability of close-out netting under the laws of the jurisdiction in which the collateral provider would be subject to insolvency proceedings, which is normally the jurisdiction where it is organized.

made in some emerging market jurisdictions. Further convergence and the strengthening of national frameworks are strongly desirable.”¹⁵

- 1.9 In October 2011 the FSB issued its *Key Attributes of Effective Resolution Regimes for Financial Institutions* (the “**FSB Key Attributes**”) which it revised and re-issued in October 2014, elaborating its guidance but without making changes to the text of the twelve Key Attributes. The *FSB Key Attributes* set out the consensus of the G20 Heads of State and Government on the core elements of an effective resolution regime for financial institutions. In the *FSB Key Attributes*, the FSB underlines the importance of close-out netting and financial collateral arrangements and how they must be safeguarded in the event of a resolution. It also emphasises, of course, that they must not hamper the effective implementation of resolution measures. The *FSB Key Attributes* therefore strikes a careful balance between these potentially conflicting policy goals. In Key Attribute 4, the FSB says that:
- (a) subject to appropriate safeguards, entry into resolution or the exercise of a resolution power should not trigger early termination rights (the necessary first stage in the close-out netting process and a pre-condition for the enforcement of financial collateral); and
 - (b) a resolution authority should have the power to stay early termination rights in other circumstances, but subject to strict conditions, including that the stay should not exceed 2 business days.
- 1.10 Further guidance on this is set out in Appendix I – Annex 5 (Temporary stay on early termination rights) to the *FSB Key Attributes*. It is clear under the *FSB Key Attributes* that the members of the FSB understands the systemic importance of ensuring that close-out netting and financial collateral arrangements are safeguarded in a resolution and can ultimately be effectively enforced.
- 1.11 The resolution regimes that have been implemented to date in G20 jurisdictions reflect, to a greater or lesser extent, the balance struck in the *FSB Key Attributes*. For example, Article 118 of the EU Bank Recovery and Resolution Directive (the “**BRRD**”),¹⁶ the EU Financial Collateral Arrangements Directive (the “**FCAD**”)¹⁷ is made subject to the effect of the BRRD, which itself reflects the principles of Key Attribute 4 summarised in paragraph 1.9 above.¹⁸
- 1.12 Without close-out netting, financial institution counterparties would be required to manage their credit risk on a gross basis, meaning liquidity and credit capacity within the system would be sharply reduced. Market and credit risk in relation to derivative transactions are also more difficult to estimate and to manage on a gross basis.

¹⁵ BCBS, *Report and Recommendations of the Cross-border Bank Resolution Group* (March 2010), para 106. See more generally Recommendation 8 and accompanying text in paras 105-114. The full text of the report is available from the BCBS website at: <http://www.bis.org/publ/bcbs169.pdf>.

¹⁶ Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms [2014] OJ L173/190.

¹⁷ Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements [2002] OJ L168/43.

¹⁸ Article 68 of the BRRD provides, broadly, that entry into resolution or the exercise of a resolution power, cannot trigger early termination rights. Articles 69, 70 and 71 confer the power on a resolution authority to suspend certain obligations, to restrict enforcement of security interests and to impose a temporary stay on contractual early termination rights, but subject in each case to a time limit roughly consistent with the 48 hour limit mentioned in Key Attribute 4. Articles 73 to 80 set out various safeguards, most importantly for present purposes, Article 77, which ensures protection for financial collateral, set-off and netting agreements.

- 1.13 Where there is a sufficiently high degree of legal certainty as to the enforceability of close-out netting, financial supervisors permit it to be recognized as risk-reducing for the purposes of determining the level of regulatory capital a supervised institution must hold in respect of its derivatives positions, enhancing the efficiency of use of regulatory capital and reducing the associated cost. This is an extremely important aspect of the use of close-out netting and it is therefore critical that close-out netting be enforceable, including in the event of insolvency of a party, with a high degree of legal certainty.
- 1.14 As noted in part 2 of this Guide, in many jurisdictions under traditional laws and rules developed long before the emergence of the modern derivatives market there is often uncertainty as to the enforceability of derivative transactions, close-out netting or related financial collateral arrangements.¹⁹ Over the past thirty years, dozens of countries have enacted some form of netting legislation.²⁰ This Guide, as noted in the Introduction, is intended to provide guidance to those jurisdictions that are contemplating introducing netting legislation or are contemplating amending and updating existing netting legislation.
- 1.15 At the international level, relevant developments include the following:
- (a) On 25 June 2004 the United Nations Commission on International Trade Law (UNCITRAL)²¹ adopted its Legislative Guide on Insolvency Law in which UNCITRAL endorsed the importance of safeguards for financial contracts, particularly in relation to close-out netting and related collateral arrangements.²²
 - (b) On 9 October 2009 the International Institute for the Unification of Private Law (UNIDROIT)²³ adopted and opened for signature its Convention on Substantive Rules for Intermediated Securities (generally known as the “Geneva Securities Convention”). The Geneva Securities Convention includes an optional Chapter V setting out special provisions in relation to collateral transactions. While the Convention has not yet come into force, it provides a model for legislation on financial collateral arrangements involving intermediated securities.²⁴ Some consideration was given at the time the

¹⁹ In some jurisdictions close-out netting has traditionally worked on the basis of general principles without the need for specific netting legislation. This was the case, for example, in England and Wales until the introduction of bank resolution legislation in the form of the Banking Act 2009 necessitated the introduction of a specific legislative safeguard to protect close-out netting from disruption due to the exercise by the UK resolution authority of a partial property transfer power. Close-out netting continues to work against an English corporate counterparty on the basis of general principles, without the need for specific netting legislation. In most countries, however, there is the potential for some uncertainty, particularly in relation to the effect of mandatory stays under insolvency reorganization statutes (such as Chapter 11 of the US Bankruptcy Code) and the effect of certain powers of a resolution authority under financial institution resolution regimes, in particular, bail-in, contract modification and partial property transfer powers.

²⁰ See Appendix D.

²¹ UNCITRAL is a body established by the United Nations (UN) as its core legal body for the promotion of law reform in the field of international trade law. UNCITRAL comprises 60 member states of the UN elected by the UN General Assembly for a term of six years. ISDA participates as an Observer from time to time at UNCITRAL Working Group meetings on topics of relevance to the financial markets. UNCITRAL produces conventions, model laws and legislative guides and recommendations as part of its mission to promote modernization and harmonization of rules for international business. Further information about UNCITRAL is available on its website at: www.uncitral.org.

²² See, in particular, Chapter H (Financial contracts and netting) at pp 156-158 and Recommendations 101-107 at pp 158-159.

²³ UNIDROIT is an independent international organization, headquartered in Rome, established in 1926 as an auxiliary organ of the League of Nations and re-established in 1940 on the basis of an intergovernmental treaty. Its purpose is to promote law reform and harmonization in the field of private law, with a particular emphasis on commercial law, and to formulate uniform law instruments, principles and rules to achieve that objective. Currently 63 countries are member states of UNIDROIT. Further information about UNIDROIT is available on its website at: www.unidroit.org.

²⁴ Given that the Geneva Securities Convention is concerned only with intermediated securities, optional Chapter V does not address cash collateral. Optional Chapter V was to a considerable extent modelled on the EU Financial Collateral Arrangements Directive. ISDA participated as an Observer in diplomatic sessions at UNIDROIT during which the proposed text of the Convention was debated by member state delegations. In December 2017 UNIDROIT published a *Legislative Guide on Intermediated Securities*. The document intends to provide principles and rules to legislators and regulators worldwide and complements the Geneva Securities Convention. Of particular relevance to

Convention was drafted to addressing the question of close-out netting, given the close connection between close-out netting and financial collateral arrangements. Ultimately, however, it was not considered appropriate to do so in the context of a convention focused on intermediated securities. Instead, UNIDROIT initiated the project discussed in (c) below.

- (c) In 2013 UNIDROIT published its *Principles on the Operation of Close-Out Netting Provisions* (the “**UNIDROIT Netting Principles**”), intended to provide guidance to national legislators of countries seeking to revise or introduce national legislation relevant to the functioning of close-out netting.²⁵ The eight core principles are reproduced in Appendix B, together with a link on the UNIDROIT website to the full document, which includes a detailed commentary. The 2018 MNA reflects the UNIDROIT Netting Principles, but goes further, providing a model of specific legislative drafting dealing with various points in more detail than was possible in the UNIDROIT Netting Principles.

1.16 We have already noted the close connection between close-out netting and financial collateral arrangements and how financial collateral arrangements in the derivatives and related financial markets assume the enforceability of close-out netting as a pre-condition. One of the principal international responses to the financial crisis of 2008 has been the introduction of mandatory margin rules for non-centrally cleared derivatives, following the joint publication by the BCBS and the International Organization of Securities Commissions (IOSCO) of their *Margin Requirements for Non-Centrally Cleared Derivatives* (September 2013, revised and re-issued March 2015) (the “**BCBS-IOSCO Margin Framework**”)²⁶ The BCBS-IOSCO Margin Framework was developed by a joint working group of the BCBS and IOSCO known as the Working Group on Margin Requirements (WGMR), which had been established in October 2011 to develop the proposals that led to the adoption of the framework and which consulted extensively with the financial industry.²⁷ The margin rules are therefore known informally in the market as the “WGMR margin rules” or “WGMR requirements” (and similar phrases). They have been widely implemented,²⁸ with final margin rules having been issued in a number of jurisdictions, including the United States, the European Union, Japan, Switzerland and Canada, and with a number of other jurisdictions currently considering draft rules.

1.17 Where it is not possible to take financial collateral (margin) on a net basis from a counterparty located in a country where there is material legal uncertainty regarding the enforceability of close-out netting (a “**Non-Netting Jurisdiction**”), special rules have had to be introduced. In some jurisdictions this has resulted in exemptions from the mandatory margin rules²⁹ but in other jurisdictions this has resulted in more onerous requirements,³⁰ in particular the requirement to collect margin gross from a counterparty organized in a Non-Netting Jurisdiction. Ultimately, economic and practical factors stemming from the mandatory margin rules are

derivatives are Part VII of the Guide (Special Provisions in Relation to Collateral Transactions) as well as Parts VIII (on conflict of laws) and Part IX (on other instruments and regulations).

²⁵ See UNIDROIT, *Principles on the Operation of Close-out Netting Provisions* (2013), at para 11. ISDA participated as an Observer in the Study Group that produced the UNIDROIT Netting Principles.

²⁶ Both versions are available from the website of the Bank for International Settlements (BIS), which hosts the BCBS. The March 2015 version is available at the following link: <http://www.bis.org/bcbs/publ/d317.htm>.

²⁷ ISDA took a leading role in responding to those consultations.

²⁸ On a phased basis as recommended in the BCBS –IOSCO Framework.

²⁹ For example, in the EU and Japan.

³⁰ For example, in the US.

likely to result in a dramatic reduction in trading activity with counterparties organised in Non-Netting Jurisdictions, until such jurisdictions are able to put in place legislation ensuring the enforceability of close-out netting.

2. THE OBJECTIVES OF NETTING LEGISLATION

- 2.1 The primary purpose of netting legislation is to ensure the enforceability of close-out netting upon the occurrence of an event of default or termination event under the netting agreement, both prior to and following the commencement of insolvency proceedings, in accordance with the terms of the netting agreement between the parties. Generally speaking, however, pre-insolvency enforceability of close-out netting is not problematic under the laws of most jurisdictions and no special legislation is necessary to ensure it.³¹ The principal challenge is to ensure the enforceability of close-out netting post-insolvency.
- 2.2 The principal objective of netting legislation is to provide legal certainty. A high degree of legal certainty as to the enforceability of close-out netting is required by financial institutions not only to ensure safe and sound management of credit risk but also under international standards for the recognition of close-out netting as risk-reducing for the purposes of bank regulatory capital requirements. That high standard is reflected in the bank regulatory capital rules implemented in the leading financial markets.³² Accordingly, even in jurisdictions where close-out netting is likely to be enforceable post-insolvency on the basis of general principles, netting legislation may be necessary to resolve any material uncertainty and put the question beyond reasonable doubt in order to meet the necessary high standard.
- 2.3 Netting legislation can take a narrow technical approach, identifying each issue under local law that raises a doubt about an important aspect of close-out netting (for example, whether a contractual right to terminate transactions early due to the commencement of a particular type of insolvency proceeding is enforceable) and then enacting a specific rule to address it. This may achieve the desired result in a precise and economical way, but the resulting legislation may be technical and not accessible to non-specialist lawyers.
- 2.4 Alternatively, legislators may choose to adopt a broader approach, which goes beyond addressing the already identified issues and more generally confirms the effectiveness of close-out netting and the various intermediate steps. This is the approach adopted by the 2018 MNA, the provisions of which analytically approach the close-out netting process in its various phases (pre-insolvency in respect of the potential conflict between gaming laws and the enforceability of qualified financial contracts, post-insolvency, single-branch and multi-branch), while systematically addressing the legal issues which have been found to apply most commonly, principally, of course, insolvency laws.
- 2.5 The principal benefits of this approach are that the resulting legislation is:
 - (a) more accessible and self-explanatory; and

³¹ There may be specific issues in relation to the enforceability of certain types of transaction, for example, under gaming or wagering laws, under insurance legislation or under other relevant law.

³² See, for example, art 296 of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms (often referred to as the “Capital Requirements Regulation” or the “CRR”).

- (b) more robust than narrow specific legislation that addresses a limited number of known issues but provides no protection against subsequent developments.

2.6 Whichever approach is taken, we suggest, as a first step, that careful consideration should be given to identifying in detail the relevant areas of local law that could potentially conflict with the effectiveness of netting agreements, so that all relevant issues are adequately covered by local legislation. These would typically fall in one or more of the following categories:

- (a) insolvency laws (including provisions of local law enacted for the prevention of insolvency), which most frequently are the primary obstacle;
- (b) any specific mandatory provisions enacted for the protection of debtors generally (in addition to insolvency law) or for the protection of certain categories of debtors;
- (c) gaming or wagering laws; and
- (d) less frequently, other principles of domestic law.³³

2.7 We suggest that careful consideration be given to identifying any local policy considerations that may be relevant in the context for the adoption of netting legislation, so that the scope of the netting legislation is defined with clarity.

2.8 Defining the scope of the legislation has a technical aspect (defining, for example, through the use of legal definitions or legal concepts the transactions or the parties that will benefit from the netting law) but also has a more political aspect, since by defining the scope of the netting law the legislator will necessarily make policy choices. For example, law makers may decide that, because the benefit of netting legislation involves a regime that derogates from the normally applicable insolvency rules, these derogations may only be justified:

- (a) in favor of certain eligible counterparty types (in which case the scope of the legislation will be restricted by reference to such counterparty types); and/or
- (b) in relation to specific types of financial market activity (in which case the scope of the legislation will be restricted by reference to such matters).

2.9 In order to be able to define clearly the scope of the netting legislation (see below), those drafting the legislation must decide beforehand a specific policy that will apply in the relevant jurisdiction in relation to the financial transactions covered by the netting legislation. Obviously, these policy choices will be influenced by broader policies reflected in the laws of the relevant jurisdiction. For example, a jurisdiction in which insolvency law is more favorable to the insolvent party than to its creditors might be tempted to draft netting legislation that reflects this policy.

³³ Examples of issues falling under this category might be (i) a requirement that a contract must satisfy a certain requirement, for example, notarization, in order to ensure its formal validity or (ii) a requirement that a contract must satisfy a certain requirement, for example, translation into a local language, to ensure its enforceability in a local court. Law makers and other national policy makers should consider whether such requirements are practical and efficient in relation to financial transactions between a local counterparty and a foreign counterparty, given the international nature of the financial markets.

- 2.10 In formulating its policy choices, law makers in a jurisdiction should, however, distinguish between regulatory policy issues and systemic risk issues. It may be appropriate, by law or regulation, to limit certain types of financial activity to certain types of market participants subject to appropriate conditions and limitations. It does not necessarily, however, make sense to limit the effectiveness of close-out netting by reference to types of market participants. The systemic risk reduction of effective close-out netting benefits all potential market participants, including corporations, insurance companies, special purpose vehicles used for structured financings, governmental authorities, charitable organizations hedging in the market, private individuals and so on. In other words, it reduces credit risk both for solvent and insolvent parties, and reduces the risk of a large insolvency have a “domino” effect on the solvency of other market participants who have dealt with the insolvent.
- 2.11 Although existing netting legislation in some countries does limit eligibility for the benefits of close-out netting to certain categories of market participant, such limitations do not necessarily make sense from a systemic risk point view. They potentially lead to difficult issues of characterization in relation to certain market participants, therefore creating legal uncertainty, and require periodic updating to reflect the continuing evolution of a dynamic market.

3. DEFINING THE SCOPE OF NETTING LEGISLATION

- 3.1 Once the policy choices in relation to the scope of the netting legislation have been made, those drafting the legislation will need to translate those choices into draft statutory provisions that are consistent with the relevant local legal concepts and categories.
- 3.2 We suggest that the provisions of the 2018 MNA will be helpful in this exercise, as the 2018 MNA may be read as a “check-list” of issues, among other things, permitting legislators that assess whether local legal concepts used to define the scope of the draft legislation are compatible with the overall purpose of the legislation.

Defining the product scope of netting legislation

- 3.3 While it is in theory possible to draft netting legislation that would cover all types of financial transactions without distinction, the scope of most actual netting legislation will seek to clarify in some way or other the types of financial transaction that benefit from the netting regime. It is clearly important to do this in a way that both provides that greatest amount of legal certainty as to scope but also is capable of accommodating continuing development and innovation in the financial markets.
- 3.4 Section 1 of Part I of the 2018 MNA provides a definition of “qualified financial contract”, which lists the various types of financial transaction that should ideally be covered. It also includes broad wording at the end of the definition intended to capture all types of financial transaction of a comparable nature in a way that is flexible enough to accommodate the development of new products. This avoids the need to introduce amending legislation periodically in order to keep pace with the markets, as happened in a number of countries that introduced early netting statutes that were relatively restricted in scope.
- 3.5 In a number of jurisdictions, the specific style of the definition of “qualified financial contract” in section 1 of Part I of the 2018 MNA may be felt to be inappropriate to the extent that it uses

current market terminology to specify a detailed list of product types rather than relying on existing legal concepts and/or broader, more generic terms. Legislators may prefer, for example, to consider referring to broad legal concepts such as “forward contracts” or “forward financial instruments”. The definition of the “qualified financial contract” should be broad enough to cover not only derivative types of transactions but also related types of transactions that are intended to benefit from the same favorable netting regime, such as repurchase transactions, securities lending transactions, margin loans and, of course, related financial collateral arrangements.

- 3.6 While it is obviously possible to define qualifying transactions using traditional legal concepts in the relevant jurisdiction, legislators should consider the following:
- (a) A single existing category will often be insufficient to cover the broad range of products meant to be covered by the 2018 MNA. For instance, in many civil law jurisdictions, the concept of a “forward contract” would typically cover derivatives generally but would not cover many products listed by the 2018 MNA, such as “spot” transactions, securities lending, repurchase transactions, collateral, clearing and settlement transactions and so on. It will therefore be necessary generally to use a combination of concepts to ensure a sufficiently broad coverage.
 - (b) Traditional legal concepts originating decades ago may be inappropriate to describe with clarity and certainty more recent products listed by the 2018 MNA or to cover future financial innovations.
- 3.7 As a result, certain jurisdictions that have traditionally tended to use their existing legal concepts have introduced a more pragmatic approach by introducing descriptive language in their statutory provisions on financial matters as this often proves to be the only efficient way to clearly cover a broad range of products which may span traditional legal categories.
- 3.8 In addition to the use of generic language of the type reflected at the end of the definition of “qualified financial contract” in section 1 of Part I of the 2018 MNA, Part I.2 of the 2018 MNA provides that the central bank or other relevant financial authority of the relevant jurisdiction should be able to designate as “qualified financial contracts” any agreement or contract in addition to those already listed in the 2018 MNA. Where the relevant authority has this power, it may use it in relation to a newly developed product, to enhance legal certainty in relation to that developing market.
- 3.9 Such provisions would give more flexibility to the definition of the financial instrument to be covered by the netting legislation. However, local legislators should check whether this suggestion makes sense from a constitutional perspective under local law. If such an approach is not possible under the laws of the relevant jurisdiction, it is particularly important to make sure that the definition of “qualified financial contract” covers all types of financial products, currently existing or contemplated, which are supposed to be included in the netting legislation.
- 3.10 Finally, we suggest that the definition of the product scope of future netting legislation may be a good opportunity to clarify certain legal issues that may interfere with the enforceability of certain financial transactions defined under the netting law. For example, there has been some uncertainty under the laws in some jurisdictions where derivatives markets have developed as to

whether derivative transactions (or certain types of derivative transaction) fall within the scope of gaming or wagering laws and, if so, whether they are therefore unenforceable. In some jurisdictions the question has arisen whether credit derivative transactions such as credit default swaps (CDS) should be characterized as guarantees or as insurance contracts, with possibly negative consequences for enforceability of those transactions in certain circumstances. Although these issues are, strictly speaking, separate from the issue of the enforceability of close-out netting, local legislators may wish to take the opportunity to clarify any identified uncertainty in this regard. Where these issues have arisen in jurisdictions in the past, local legislation has been enacted to clarify, possibly subject to certain conditions, that financial market transactions such as derivatives are excluded from the effect of gaming, wagering, guarantee or insurance laws.

Defining the counterparty scope of netting legislation

- 3.11 After defining which type of financial transactions will be covered by the netting legislation, those preparing draft legislation should, if appropriate, define the parties who will be eligible to benefit from the special netting regime. As set out above, the choice of the eligible parties is important in terms of policy considerations.
- 3.12 Counterparty scope was heavily debated during the drafting and implementation of the FCAD, which covers a number of issues related to netting. The FCAD offered EU Member States the option to exclude non-regulated entities (that is, mainly corporate entities) from the scope of national legislation implementing the FCAD (the so-called “opt-out” of article 1(3) of the FCAD). When implementing the FCAD, most European jurisdictions decided to include both financial and non-financial entities within the scope of the netting legislation. Certain countries initially excluded non-financial entities, but later extended the scope to include them. An alternate solution was adopted by France, which decided that non-financial entities should benefit from the netting regime for transactions entered into with a “regulated” entity (that is, mainly a financial entity, an investment fund or certain public law governed entities) where these transactions are linked to financial instruments.
- 3.13 The definition of “person” in section 1 of Part I of the 2018 MNA may be used as a framework for excluding certain persons from the scope of the netting legislation:

“‘person’ includes an [individual], [partnership], [corporation], [other regulated entities such as a bank, investment firm, securities or commodities dealer, insurance company or investment manager], [or any other body corporate whether organized under the laws of [insert name of 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];”
- 3.14 Once again, those preparing draft legislation may consider referring to the exact legal concepts in the law of the relevant jurisdiction to define the relevant persons. For example, if the laws of the relevant jurisdiction provide for a definition of “bank”, it may be useful in terms of clarity to refer to this definition.

3.15 There are, however, as discussed in parts 2.10 to 2.11 of this Guide, strong policy and practical considerations in favour of adopting as broad a scope as possible for close-out netting legislation and dealing with other policy concerns via financial regulation or other appropriate legislation that does not affect the enforceability of close-out netting against the broad range of financial market participants.

Defining “netting agreement” and “netting”

3.16 Once the eligible transactions and eligible parties (if necessary) have been defined, the draft netting legislation needs to define the netting agreements that will be covered. Section 1 of Part I of the 2018 MNA sets out a broad definition of “netting agreement” which covers master agreements and master-master netting agreements³⁴ as well as collateral arrangements related to these types of agreements:

“‘netting agreement’ means an agreement between two persons that provides for netting, including, without limitation:

- (a) an agreement that provides for the netting of amounts due under two or more netting agreements; and
- (b) a collateral arrangement relating to or forming part of a netting agreement;”

3.17 It is worth noting that this definition avoids relying on jurisdiction-specific legal concepts and simply attempts to describe the economic effects intended by the parties in their netting agreement. This approach may prove difficult to translate in certain legal systems that traditionally organize or regulate a specific legal concept of “set-off” (for example, the concept of *compensation* under the French civil code), which refers to a payment mechanism whereby respective obligations may be discharged.

3.18 The definition of “netting agreement” in section 1 of Part I of the 2018 MNA uses the term “netting”, which is itself defined in section 1 of Part I of the 2018 MNA as follows:

“‘netting’ means the operation of a set of provisions in an agreement between two persons that:

- (a) may be commenced by notice given by one person to the other person upon the occurrence of an event of default with respect to the other person or other termination event or that may, in certain circumstances, occur automatically as specified in the agreement; and
- (b) has the following effect:
 - (i) the termination, liquidation and/or acceleration of any present or future payment or delivery rights or obligations arising under or in connection with one or more qualified financial contracts entered into under the agreement;

³⁴ An example of a standard form master-master netting agreement is the Cross-Product Master Agreement jointly published in February 2000 by ISDA and a number of other trade associations.

- (ii) the calculation or estimation of a close-out value, market value, liquidation value or replacement value in respect of each right and obligation or group of rights and obligations terminated, liquidated and/or accelerated under (i) and the conversion of each such value into a single currency; and
- (iii) the determination of the net balance of the values calculated under (ii), whether by operation of set-off or otherwise, giving rise to the obligation of one person to pay an amount equal to the net balance to the other person;”

- 3.19 The foregoing definition reflects a process that may be given effect as a matter of legal substance in one of broadly two ways. Some netting agreements rely on acceleration of obligations, according to an agreed methodology, which results in multiple obligations that are then reduced to a net balance by operation of contractual set-off. This is the approach taken by the netting agreements most commonly used for securities repurchase transactions and for securities lending transactions. It is also the basis of close-out netting under foreign exchange related netting agreements.
- 3.20 The other common approach to close-out netting is for individual transactions simply to be terminated, without acceleration of the individual obligations due under those transactions, and for the obligations due under the transactions to be discharged, in consideration of a separate single obligation arising under the close-out netting provision. That single obligation is calculated by reference to the market replacement values of the terminated transactions, but it is a pure calculation. No contractual set-off is involved in the principal close-out netting mechanism, since set-off can only occur if there is more than one obligation, and only one obligation arises under the close-out provision. If amounts have become due prior to the early termination of the transactions, they will normally be included in the final net calculation, and so contractual set-off occurs in relation to those, but only to that limited extent.
- 3.21 This latter approach to close-out netting is the approach taken under the ISDA Master Agreement, and it is used in some other financial market standard form netting agreements. It is sometimes referred to as a “flawed asset” or “conditional novation” approach to close-out netting. It is important that any definition of “netting” is broad enough to encompass this form of netting, given that it more widely used in the derivatives market than the contractual set-off based approach by virtue of its use in the ISDA Master Agreement.
- 3.22 Many netting agreements provide that once a net balance has been determined (whether using the contractual set-off based approach or the conditional novation approach) under the close-out netting provision, then that net amount is available for contractual set-off by the non-defaulting party against other amounts due between the parties outside the scope of the netting agreement.³⁵ That is separate from and subsequent to the operation of the close-out netting provision.
- 3.23 It is important to remember that netting involves the termination of obligations under transactions, but not of the netting agreement itself, which must continue to operate in order to provide for the process of close-out netting, for the payment of any close-out amount due as a

³⁵ See, for example, Section 6(f) of the ISDA 2002 Master Agreement.

result of the operation of that process, including any related interest amount, and for other continuing obligations, if any, under the agreement between the parties.

- 3.24 It is also worth noting that the substance of the definition of “netting” in the 2018 MNA is reflected in the definition of “close-out netting provision” in Article 2(1)(n) of the FCAD, although the definition in the 2018 MNA is more detailed. In particular, the definition of “close-out netting provision” in Article 2(1)(n) of the FCAD makes it clear that it is not limited to arrangements that rely on contractual set-off.
- 3.25 The 2018 MNA does not list specific types of netting agreement, for example, the ISDA 2002 Master Agreement. This avoids restricting the netting regime to specific agreements only, and the risk that an adapted or amended form of the agreement might fall outside the scope of the legislation, potentially creating material legal uncertainty as to the enforceability of the agreement. In certain jurisdictions the use of specific domestic documentation governed by the law of the jurisdiction is common. It is consequently suggested that the netting legislation should adopt a broad definition covering domestic as well as international industry standard documents, irrespective of their governing law and to avoid restrictions limiting, for example, eligible agreements to those approved by a specific authority. In many countries where such restrictions had been initially introduced (for example, France), they have proved inappropriate both for reasons of principle and for practical purposes. It is indeed questionable whether any public authority has relevant competence to determine the appropriateness of a given standard to govern privately negotiated contracts. In addition, such restrictions create legal uncertainty, as the relevant public authority will inevitably take considerably more time to approve new documentation or evolutions of existing documentation than the time it will typically take for the markets to adopt such documentation.
- 3.26 In respect of the close-out netting provisions, the netting legislation will, as set out above, need to specify that the eligible transactions which are subject to the close-out netting can be governed by one or more netting agreements to allow the use of bridge or master-master-agreements between various agreements governing different types of transactions. For example, it is now commonplace in the market for parties to enter into a master-master-agreement to provide for close-out netting of close-out amounts due under separate derivatives, securities repurchase and securities lending netting agreements between the parties.
- 3.27 It is also worth noting that the definition of “netting agreement” in section 1 of Part I of the 2018 MNA refers to collateral arrangements in order to ensure that the protective benefit of the legislation extends to related collateral arrangements.
- 3.28 Broadly speaking, internationally, financial collateral arrangements are based on either the creation of a security interest in financial collateral or the transfer of title to such financial collateral. The legal analysis of each approach, and which approach is preferable in relation to a counterparty organized and/or operating in a particular jurisdiction, will depend on relevant domestic law. The 2018 MNA does not seek to deal with these issues in detail.
- 3.29 We note that optional Chapter V (Special Provisions in Relation to Collateral Transactions) of the Geneva Securities Convention provides a model for a set of principles suitable for modern financial collateral transactions, dealing with both security and title transfer financial collateral arrangements and promoting convergence in operative effect and consistency of legal treatment

between the two approaches. Chapter V is limited, however, to financial collateral in the form of intermediated securities, which is not surprising given the context in which it appears. It was, however, inspired by the FCAD, which similarly provides a common set of principles for both security and title transfer financial collateral arrangements and which deals with financial collateral in the form of cash as well as intermediated securities.

- 3.30 Although the 2018 MNA does not provide a detailed set of principles to govern financial collateral arrangements, it does, as noted above, extend the protective effect of the MNA to those arrangements when entered into in conjunction with a netting agreement. We also note specifically in relation to title transfer collateral arrangements that such arrangements are often integrated into the mechanism of the netting agreement to which they relate. In the 2018 MNA they are therefore included within the definition of “qualified financial contract”. Both security and title transfer financial collateral arrangements are included within the definition of “netting agreement” in the 2018 MNA.

4. CONFIRMING THE ENFORCEABILITY OF NETTING AGREEMENTS

- 4.1 Once the scope of the netting legislation has been defined, adequate operative provisions will be required to ensure the enforceability of close-out netting upon the occurrence of any termination event or event of default under the netting agreement, both prior to and following commencement of insolvency proceedings, in each case in accordance with the terms of the parties’ contract.
- 4.2 In most jurisdictions where there is any doubt under existing law as to the full enforceability of close-out netting under a netting agreement, the source of that doubt lies in potentially applicable principles of insolvency law. However, as discussed above, local legislators should make sure that any proposed netting legislation also resolves any other legal issue which could potentially interfere with such enforceability. Accordingly, in this part 4 of this Guide, we consider the enforceability of a netting agreement against a counterparty in the absence of insolvency proceedings, after commencement of insolvency proceedings against the counterparty and, in a case where the counterparty is a financial institution, after its entry into a resolution regime. Before turning to consider each of these areas, we set out some general observations.
- 4.3 Netting legislation should confirm the enforceability of close-out netting upon the occurrence of any event of default or other termination event under the netting agreement, both prior to and following commencement of insolvency proceedings, in each case in accordance with the terms of the parties’ contract, subject, in the case of resolution, to the considerations set out in paragraphs 4.32 to 4.34 below. Section 4(a) of Part I of the 2018 MNA expressly confirms that the provisions of a netting agreement will be enforceable in accordance with their terms even if the counterparty is subject to insolvency proceedings.
- 4.4 The 2018 MNA does not set out a list of events of default or termination events that would allow the parties to the netting agreement to terminate the underlying transactions. These events will be provided by the netting agreement entered into by the parties. When referring to the termination of the transactions, we suggest that local legislators use the approach adopted by the 2018 MNA and simply refer to the agreement of the parties.

- 4.5 Netting legislation should not require “termination” of the netting agreement itself since only transactions terminate. The netting agreement should survive so that its netting provisions can effectively be performed.
- 4.6 Netting legislation should also provide that the inclusion of non-eligible transactions under a netting agreement does not affect the enforceability of close-out netting for the remaining eligible transactions under the netting agreement.³⁶ For example, if the netting legislation specifies a variety of different types of derivative and related financial transactions as within scope, but does not expressly include spot transactions (which are not, strictly speaking, derivative transactions), then the inclusion under the netting agreement of spot transactions should not prevent the parties from enjoying the protection of the netting legislation in relation to all transactions falling clearly within its express scope. The spot transactions would themselves not benefit from the netting legislation,³⁷ but otherwise the netting agreement would be unaffected by inclusion of the spot transactions.
- 4.7 In this respect, section 4(i) of Part I of the 2018 MNA refers expressly to the fact that a netting agreement should be enforceable even if this netting agreement contains transactions that are not “qualified financial contracts”. In this case, under the 2018 MNA, the netting arrangement should only apply to the agreements, contracts or transactions that fall within the definition of “qualified financial contract”. The definition of “qualified financial contract” is, of course, intentionally broad, so it is unlikely that any transaction that, in economic terms, is a derivative transaction would fall outside its scope. But the definition does not include conventional loans,³⁸ debt securities or other types of financial transactions that are not derivative transactions.³⁹ The 2018 MNA has, however, been amended relative to the 2006 version of the Model Netting Act to make clear that certain types of structure used for the purpose of effecting Shari’a compliant instruments, agreements or transactions fall within the scope of the “qualified financial contract”.⁴⁰
- 4.8 Finally, once the relevant transactions are terminated, the provisions of the netting agreement provide for the calculation of a single net amount which, in principle, will be owed by one party to the other. Consequently, the netting legislation should specify that the only obligation or entitlement due to or from a party to a netting agreement upon close-out netting of transactions is its net obligation or entitlement as determined in accordance with the terms of the netting agreement. This is the objective of sections 4(b) and 4(c) of Part I of the 2018 MNA.

³⁶ It sometimes occurred under early netting legislation with a defined product scope that new developments, such as equity derivatives in the early 1990s or credit derivatives in the mid- to late 1990s were not expressly covered. In some jurisdictions, notably the US, Japan and Ireland, this raised a question as to whether the inclusion of these transactions somehow adversely affected the eligibility of the whole netting agreement for the protection of the netting legislation. This has sometimes been referred to as “bad apple” risk, after the adage “one bad apple spoils the whole barrel”. In the case of the US, Japan and Ireland netting legislation, this risk was subsequently eliminated by amendment to the netting legislation.

³⁷ Although the spot transactions do not benefit from the netting legislation under this scenario, it might still be possible to net them under the netting agreement under general principles of law, but perhaps with a lower level of legal certainty. That would be a matter for the relevant jurisdiction.

³⁸ It does cover margin loans, which are loans, typically made by a securities broker-dealer, to a customer where the loans is collateralized by securities held by the securities broker-dealer for the customer.

³⁹ Spot forward foreign exchange transactions, which as already noted are not derivatives in the strict sense, are included because of the close relationship between spot forward foreign exchange trading and trading of forward foreign exchange transactions and currency options.

⁴⁰ See clause (z) of the definition of “qualified financial contract”.

Enforceability outside insolvency proceedings

- 4.9 It is quite likely that most of the civil law jurisdictions would recognize the enforceability of netting agreements outside the scope of insolvency proceedings.
- 4.10 If this is not the case in a jurisdiction considering the introduction of netting legislation, the netting legislation should include appropriate provisions to ensure the enforceability of close-out netting and collateral arrangements upon the occurrence of any event of default or termination event under the netting agreement in accordance with the terms of the parties' contract.
- 4.11 One example of such an issue is dealt with in section 3(a) of Part I of the 2018 MNA, which provides that qualified financial contracts shall not be unenforceable by reason of laws relating to gaming contracts. That is only one example of a pre-insolvency enforceability issue, but it has arisen sufficiently often in jurisdictions with newly developing derivative markets that it was considered desirable to include such a provision in the 2018 MNA (and in prior versions of the Model Netting Act).
- 4.12 Another example of a pre-insolvency enforceability issue is dealt with in section 3(b) of Part I of the 2018 MNA, which provides that if the parties to a qualified financial contract considered it to be Shari'a compliant at the time they entered into it, then a party cannot subsequently seek to repudiate it or avoid its obligations under the qualified financial contract. This provision has been drafted to address situations that have arisen in recent years where, subsequent to entry into a Shari'a compliant transaction, a party has sought to avoid its obligations on the basis that an Islamic scholar has changed his view about a transaction's compliance with the principles of the Shari'a. The provision is to ensure certainty, finality and fairness to a party who has in good faith entered into hedging or other arrangements in reliance on the enforceability of the relevant transaction.
- 4.13 An issue that has arisen in some jurisdictions is whether a netting agreement needs to be registered with a public authority for certain purposes. Any such registration requirement needs to be closely scrutinized to ensure that it effectively serves an identifiable and important policy objective, without creating an undue burden or imposing unnecessary cost on market participants. Without careful handling, a registration requirement creates cost, leads to inefficiency and therefore increases, rather than decreases system risk. In any jurisdiction where such a registration requirement is imposed, it must be made clear, if necessary by an appropriate provision in netting legislation, that the enforceability of the netting agreement is not affected by any failure to register or any defect in the registration process. Otherwise, the registration requirement raises an unacceptable level of legal risk. The 2018 MNA does not include a specific provision dealing with this issue, but if such an issue arises, it would be appropriate to insert the provision in section 3 of the 2018 MNA, as an additional section 3(c) if sections 3(a) and 3(b) are also being adopted.
- 4.14 Pre-insolvency enforceability provisions should, of course, only be included in netting legislation if strictly necessary. Provisions that are merely declaratory or confirmatory of existing law risk creating confusion and therefore undermining, rather than enhancing, legal certainty.

Enforceability in the case of insolvency proceedings

- 4.15 The principal focus of netting legislation has always been on ensuring enforceability of a netting agreement against a party that is subject to insolvency proceedings. This is because mandatory insolvency rules come into operation that could potentially disrupt close-out netting and/or a related collateral arrangement.
- 4.16 The netting legislation should refer to all forms of insolvency proceedings that could potentially apply to a party in that jurisdiction, and the protective provisions of the netting legislation should apply regardless of which form of insolvency proceedings applies in an individual case. The definition of “insolvency proceedings” in section 1 of Part I of the 2018 MNA should be adapted to refer to all relevant forms of insolvency proceeding, including proceedings that are principally concerned with the liquidation or winding up of a party (whether voluntary or compulsory and whether or not judicially supervised),⁴¹ proceedings that provide for some form of reorganization, rehabilitation, receivership, conservatorship or administration of the party and any other form of collective proceedings affecting the rights of creditors generally, including a statutory scheme for a voluntary arrangement or composition with creditors.⁴² In addition, the netting legislation should ideally cover “all similar proceedings” to ensure that any new types of proceedings which could be introduced under the relevant law will be included in the scope of the netting legislation.
- 4.17 It is a normal feature of insolvency proceedings that one or more persons is appointed to administer the affairs of the insolvent party during the insolvency proceeding. Such a person may be referred to in English-speaking jurisdictions as an insolvency practitioner, an insolvency representative, an insolvency office-holder, a liquidator, an administrative receiver, a receiver, a trustee in bankruptcy, a conservator, an administrator or by some similar name. The 2018 MNA uses the generic term “insolvency practitioner” to refer to such an individual.⁴³ An insolvency practitioner is generally granted the power to manage the assets of the insolvent party and various other powers, including the power to recover or “claw back” payments made or assets transferred by the insolvent party during a relevant period prior to commencement of the insolvency proceedings. These powers, if exercised by an insolvency practitioner, can in certain circumstances disrupt the effectiveness of close-out netting, unless close-out netting is protected by an appropriate safeguard.
- 4.18 Examples of various insolvency rules and powers that may undermine the enforceability of close-out netting and how they should be addressed in netting legislation are discussed below.
- 4.19 The discussion in paragraphs 4.20 to 4.31 assumes that ordinary corporate insolvency proceedings apply. Special considerations arise in the case of the resolution of a financial institution, as discussed in paragraphs 4.32 to 4.34.

⁴¹ E.g., liquidation judiciaire in France under the Code de Commerce, winding up proceedings in England under the Insolvency Act 1986 and liquidation under Chapter 7 of the US Bankruptcy Code.

⁴² E.g., redressement judiciaire in France under the Code de Commerce, reorganization under Chapter 11 of the US Bankruptcy Code and administration in England under the Insolvency Act 1986.

⁴³ The same term is used for a similar purpose in Regulation 2015/848/EU of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast).

Prohibition of early termination

4.20 The insolvency laws of many jurisdictions limit the effectiveness of contractual early termination provisions that are triggered by the opening of insolvency proceedings. Given the importance of termination in the close-out netting process, the 2018 MNA goes beyond the general affirmation of the enforceability of netting agreements provided in section 4(a) of Part I and provides in section 4(g) of Part I that an insolvency practitioner shall not be able to prevent the termination of any qualified financial contracts or the acceleration of any payment owed under these qualified financial contracts.

“Cherry-picking”

4.21 Under insolvency legislation, an insolvency practitioner often has the right to assume, affirm or require the continuation of contracts or transactions that are favourable to the insolvent party coupled with the power to disclaim, reject or repudiate contracts or transactions that are not favourable to the insolvent party. This assumption/disclaimer power is sometimes referred to as a “cherry-picking” power. The insolvency office-holder in such a case has the power to keep the “good” cherries (contracts beneficial to the insolvent party) and to reject the “bad” cherries (contracts burdensome to the insolvent party). Contractual close-out netting arrangements under netting agreements originally developed in the mid-1980s precisely to overcome this problem.

4.22 If an insolvency office-holder were allowed to “cherry-pick” transactions under a netting agreement, then the solvent party would, in effect, be forced to pay the full amount of any obligations owed under the affirmed transactions (those “in the money” to the insolvent party), while claiming as an unsecured creditor for the transactions that are disclaimed (those “out of the money” to the insolvent party). Obviously, in such circumstances the solvent party would find that its credit exposure was gross and not net, and close-out netting would therefore have been undermined.

4.23 The ISDA Master Agreement makes it clear in Section 1(c) that the ISDA Master Agreement and all Transactions under it together form a single agreement between the parties, and that the parties have entered into it and each Transaction in reliance on this fact. The single agreement nature of the ISDA 2002 Master Agreement is also reflected in the close-out netting provisions where under Section 6(c)(ii) no further obligations are owed in respect of Terminated Transactions, but without prejudice to the separate obligation arising under Section 6(e) to pay the Early Termination Amount. Thus, in the event of insolvency proceedings, the contractual position is that there are no individual “cherries” to pick, but merely one net claim due under Section 6(e).

4.24 In some jurisdictions, however, it is necessary for the sake of legal certainty for this clear contractual position to be protected by specific legislation. To ensure that “cherry-picking” cannot disrupt close-out netting, legislators should therefore consider introducing in the netting legislation a provision similar to section 4(d) of Part I of the 2018 MNA.

Limitations on set-off

- 4.25 Many bankruptcy laws limit the availability of set-off in an insolvency. For example, in certain civil law jurisdictions, respective obligations are only available for set-off when they have fallen due; even when they are due, set-off will only be possible with respect to respective obligations which either arise under the same agreement or are otherwise strongly interconnected (this is sometimes referred to as the “connexity” requirement). Such requirements might jeopardize the effectiveness of netting agreements. The provisions of the netting law will need to address these issues as suggested in section 4(e) of Part I of the 2018 MNA, which provides for the recognition of set-off in a way which is compatible with the mechanisms of typical netting agreements.

Preferences

- 4.26 The netting legislation will need to ensure that any payment or transfer of collateral made in respect of the net credit exposure of a party under the netting agreement during any “preference period” or “suspect period” is not treated as a preference, and therefore void or voidable, provided that, in effect, the payment or transfer of collateral is made under the normal operation of the terms of a transaction or collateral arrangement and not with an intention to hinder, delay, or defraud any relevant creditor.
- 4.27 Section 4(f) of Part I of the 2018 MNA expressly sets out that an insolvency practitioner of an insolvent party may not avoid a payment or transfer of collateral on the ground of it constituting a preference or transfer during a preference or suspect period by the insolvent party to the non—insolvent party, subject to the qualification set out in section 4(f).

Other considerations

- 4.28 The 2018 MNA takes the approach of affirming, in each case where provisions of insolvency law could conflict with the terms of a netting agreement or collateral arrangement, that the enforceability of the netting agreement and collateral arrangement should be unaffected by those provisions. In this respect, a jurisdiction might prefer not to list each and every situation that could be problematic under local insolvency law but instead to override or disapply all the provisions of the insolvency law that would apply to the relevant type of counterparty in case of insolvency proceedings.
- 4.29 French law, for example, specifies in an article of its monetary and financial code that close-out netting is valid under French law and in a subsequent article confirms that none of its insolvency provisions may interfere with the application of the first article.
- 4.30 Consequently, by “disapplying” all the insolvency law provisions instead of affirming in certain specific situations that the netting and collateral arrangements will be valid, French law sets out clearly that insolvency law may not be used to challenge the principle of the validity of close—out netting and precludes the risk of failing to enumerate any specific cases which could be problematic.
- 4.31 In any event, as set out above, section 4 of Part I of the 2018 MNA should be used by those preparing legislation as a “check-list” to consider when drafting provisions to “disapply”

insolvency law provisions that might conflict with the enforceability of a netting agreement or collateral arrangement. Please note that the list of issues addressed by the 2018 MNA is not exhaustive and other issues may need to be considered under the laws of the relevant jurisdiction.

Enforceability in the case of financial institution resolution

- 4.32 In the case of the resolution of a financial institution, the need to confer special protection by netting legislation on the enforceability of close-out netting under a netting agreement and financial collateral under a related collateral arrangement needs to be balanced with the need to ensure that resolution measures are effective.
- 4.33 How this balance should be struck was the subject of detailed consideration at an international level by the members of the FSB and reflected in the *FSB Key Attributes*, as discussed in paragraphs 1.9 to 1.10. This international consensus was reflected in Principle 8 of the UNIDROIT Netting Principles.
- 4.34 The 2018 MNA takes these developments into account by the addition of section 4(j) of Part I of the 2018 MNA. There was no comparable provision in prior versions of the Model Netting Act, which pre-dated the widespread adoption of financial institution resolution measures internationally following the financial crisis in 2008.

5. MULTIBRANCH NETTING

- 5.1 Netting legislation should permit netting under a netting agreement against a multibranch party. A multibranch party is one that has a head office in one jurisdiction and various branches in other jurisdictions. Netting against such an entity is referred to in the 2018 MNA as “multibranch netting”. By “branch” we mean a local establishment of the foreign entity. The head office and each branch of the foreign entity should form a single legal entity under the law of the jurisdiction of organization of the foreign entity.⁴⁴ This is particularly relevant to financial institutions, given that it is principally financial institutions (and specifically banks) that typically operate on a multibranch basis.
- 5.2 Optional Part II of the 2018 MNA provides detailed provisions intended to ensure the effectiveness of multibranch netting in the event of the cross—border insolvency of a multibranch bank. They are not relevant where the local establishment is, in fact, a locally organised subsidiary of a foreign parent company, since the local subsidiary would be a separately legal entity and not a “branch” in the sense used above.
- 5.3 Optional Part II of the 2018 MNA is optional because it is generally only necessary where under local insolvency law there is a risk that the local assets and/or liabilities of an insolvent local branch of a foreign financial institution could be subject to “ring-fencing”, meaning that the local branch would be treated as though it were a stand-alone legal entity and subject to local insolvency proceedings in respect of its local assets and/or liabilities without regard to

⁴⁴ Generally speaking, if that is the case, then under normal principles of private international law, each other jurisdiction where a branch is located will recognize that the foreign entity and each of its branches, including any local branch in that jurisdiction, form a single legal entity. Where that is not the case, then the local branch in that jurisdiction may be treated as though it were a stand-alone entity, giving rise to a risk of ring-fencing, as discussed in para 5.3.

assets held or liabilities incurred outside the jurisdiction. Such ring-fencing would potentially undermine the effectiveness of the netting mechanism, which is supposed to operate globally on the basis of all respective obligations and entitlements of the parties, irrespective of the place of booking of individual transactions.

- 5.4 The multibranch provisions of the 2018 MNA are broadly based on New York banking law provisions that expressly enforce multibranch close-out netting for derivatives transactions in a constructive attempt to reconcile the ring-fencing of New York branches and the interest in enforcing multibranch close-out netting. It is necessary for local legislators to consider whether ring-fencing applies in their own jurisdiction and, if so, consider the appropriateness of provisions similar to those set out in Optional Part II of the 2018 MNA. Obviously, if ring-fencing does not apply, then those provisions should not be necessary. Part I is designed so that it may be enacted on a stand-alone basis in such a case.⁴⁵
- 5.5 A number of changes have been made to the drafting of Optional Part II of the 2018 MNA relative to Part II of the 2006 version of the Model Netting Act. These drafting changes have been made to improve the clarity and therefore certainty of interpretation of the multibranch netting provisions. They are not, however, intended to change the substantive approach taken in the 2006 and 2002 versions of the Model Netting Act.

6. GOVERNING LAW APPROACH TO ENSURING ENFORCEABILITY OF CLOSE-OUT NETTING

- 6.1 The basic approach of the 2018 MNA, in common with the prior versions of the Model Netting Act, is to provide a legislative framework for a jurisdiction that ensures the enforceability of a netting agreement and a related collateral arrangement under the law of that jurisdiction, regardless of the governing law of the netting agreement or the collateral arrangement. In other words, the enforceability of the netting agreement and collateral arrangement is protected and safeguarded, whether governed by the law of that jurisdiction or by the law of any other jurisdiction.
- 6.2 Another approach to ensuring the enforceability of close-out netting is to provide that the enforceability of the netting agreement will be governed by the law chosen by the parties to govern the netting agreement. This is the approach taken in Article 25 of the EU Winding Up Directive for Credit Institutions (the “**WUDCI**”),⁴⁶ which is discussed in more detail below. It is a simpler approach and can be achieved by enacting a provision that reads as follows:

“Governing law of the netting agreement. Without prejudice to [insert reference to relevant statutory provisions (i) providing that a party may not terminate transactions with a financial institution in resolution by reason only of its entry into resolution or the exercise by the relevant resolution authority of a resolution measure or power and (ii) providing for a temporary stay of no more than 48 hours in accordance with the FSB Key Attributes], the enforceability of a netting

⁴⁵ If considering enacting a statute modelled on Part I of the 2018 MNA without Part II, the only changes necessary to the model (apart from any necessary or desirable adaptations for local purposes) would be the deletion of the reference to “Part I” in the heading, deletion of the words “this Part of” before the words “this Act” each time they appear in section 4(i) and the deletion of sub-section (iv) of section 4(i). For convenience, the necessary deletions are noted by footnotes in the text of the 2018 MNA in Appendix A.

⁴⁶ Directive 2001/24/EU of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions [2001] OJ L125/15.

agreement, including each transaction entered into under the netting agreement and any related collateral arrangement, shall be governed solely by the law:

- (a) expressly chosen by the parties and specified in the agreement as its governing law; or
- (b) if no governing law is specified in the agreement, determined in accordance with the rules of the *lex fori* for determining the law applicable to contractual obligations in civil and commercial matters in the absence of an express choice of law by the parties.

For the purposes of this provision, the governing law of an agreement includes the insolvency law of the jurisdiction whose law is applicable under (a) or (b) above, such insolvency law applying, however, only to the extent that there are insolvency proceedings in the jurisdiction whose law is applicable under (a) or (b) in respect of either party.”

6.3 Of course, parties entering into a netting agreement and seeking to rely on such a legislative provision should ensure that they:

- (a) have expressly chosen a governing law (to avoid any uncertainty that might arise if the relevant law is left to the court to determine according to the domestic choice of law rules of the jurisdiction); and
- (b) have chosen a governing law under which the enforceability of close-out netting is robust to a high degree of legal certainty.

6.4 As noted in paragraph 6.2 above, Article 25 of the WUDCI takes this approach. Article 25 reads in its entirety as follows:

“**Netting agreements.** Without prejudice to Articles 68 and 71 of Directive 2014/59/EU, netting agreements shall be governed solely by the law of the contract which governs such agreements.”

6.5 “Directive 2014/59/EU” is the BRRD.⁴⁷ Articles 68 and 71 are the provisions of the BRRD that have the effect described in the language in italics in the model provision set out in paragraph 6.2 above. In context, it is clear that Article 25 is principally concerned with the enforceability (as opposed to other legal aspects) of netting agreements. In our model provision in paragraph 6.2, we have made this explicit.

6.6 An unfortunate aspect of Article 25 has been a lack of clarity, giving rise to some confusion in the market and differences of interpretation between lawyers across the EU, as to the intended scope of the reference to “the law of the contract”. In particular, the question has arisen whether the scope of the reference should be limited to:

- (a) the contract law of the relevant jurisdiction;

⁴⁷ See n 16.

- (b) all of the relevant private law of the jurisdiction excluding insolvency law (but including, for example, tort, property law, agency law, company law and so on to the extent those have a bearing on an issue arising under the contract); or
- (c) all of the law of the relevant jurisdiction, including its insolvency law.

6.7 Interpretations (b) and (c) are preferable to (a), as issues other than contract law issues may arise in relation to the enforceability of a netting agreement. The advantage of interpretation (c) over interpretation (b) is that it avoids the need to consider the classification of a legal issue for purposes of determining whether the legal issue is within scope. If, however, interpretation (c) is correct, a further question arises whether the insolvency law of the jurisdiction is to be applied to the question of the enforceability of the netting agreement:

- (i) even in the absence of relevant insolvency proceedings in that jurisdiction; or
- (ii) only to the extent that there are actual insolvency proceedings in that jurisdiction.

6.8 If approach (i) is the correct approach, it would be necessary for a court seeking to determine the enforceability of the netting agreement under that law to apply the insolvency law of the relevant jurisdiction on a hypothetical or counterfactual basis, as though insolvency proceedings had been opened in respect of the defaulting party. This is because the application of most substantive rules of insolvency law is dependent, directly or indirectly, on the timing of the opening of insolvency proceedings. Approach (i) is therefore inherently uncertain, running counter to the objective of enhancing certainty as to the enforceability of netting agreements. The final paragraph in the model provision set out in paragraph 6.2 above avoids this difficulty by making it clear that the insolvency law of the relevant jurisdiction only applies if there are actual insolvency proceedings in that jurisdiction.

6.9 It should be clear that if the approach set out in paragraph 6.2 above is taken, it is not necessary to enact further netting legislation in the form of the 2018 MNA, except perhaps as to specific issues such as those dealt with in section 3 of Part I of the 2018 MNA. The 2018 MNA seeks to ensure the enforceability of a netting agreement under the law of the jurisdiction enacting the netting legislation. The provision in paragraph 6.2 exports the question of the enforceability of the netting agreement to the law of another country, chosen by the parties.⁴⁸ The two approaches are therefore fundamentally different.

6.10 Although the approaches are different, they are not incompatible. They simply achieve the same result by different routes. It may be that local legislators will wish to consider combining the approaches in a single legislative package to provide extra reassurance to international financial market participants dealing with local counterparties.⁴⁹ In such a case, the provision in paragraph 6.2 above can be added as an additional sub-section (k) to section 4 of Part I of the 2018 MNA.

⁴⁸ Assuming our advice in paragraph 6.3 has been followed.

⁴⁹ This is more or less the current position in the EU in relation to a counterparty to a netting agreement that is a credit institution that would be subject to WUDCI. If one takes, for example, the case of a French bank counterparty entering into an ISDA Master Agreement under English law, close-out netting against the French bank is enforceable under French netting legislation, but Article 25 would apply, referring the question of enforceability to English law (subject, possibly, to the questions of interpretation discussed in paras 6.6 to 6.8).

7. PROVISION-BY-PROVISION COMMENTARY

Drafting approach and structure of the 2018 MNA

- 7.1 The original Model Netting Act published by ISDA in 1996 was inspired by successful netting legislation introduced in the United States at federal level, modifying the US Bankruptcy Code. Each subsequent version of the Model Netting Act has, for consistency, preserved the same structure and approach. A number of countries have successfully used a version of the Model Netting Act as the basis for its domestic legislation. However, as we have already acknowledged in the Introduction to this Guide, the drafting style of the 2018 MNA is not necessarily suitable for all legal traditions.
- 7.2 Nonetheless, ISDA is aware of a number of jurisdiction where a prior version of the Model Netting Act has been used successfully as (a) a checklist of relevant issues to address and (b) a drafting model to address those issues, even where that drafting has required adaptation to meet local legislative drafting standards, conventions and practices.
- 7.3 The 2018 MNA is divided into two Parts:
- (a) Part I sets out provisions dealing with the enforceability generally of netting agreements, both prior to and in the event of insolvency proceedings. Part I can be used on a self-standing basis, if Part II is not needed.
 - (b) Part II is, as already explained, optional and sets out provisions dealing with the enforceability of multibranch netting where such provisions are necessary due to local “ring-fencing” or similar provisions, as discussed in part 5 of this Guide.
- 7.4 The provision-by-provision commentary below is intended to provide helpful brief guidance on the individual terms of the 2018 MNA, with convenient cross-references, where appropriate, to other paragraphs of this Guide. It should be read in conjunction with the rest of this Guide. It is not intended to be a detailed, much less exhaustive, commentary, nor is it intended as legal advice, and it should not be relied upon as such.
- 7.5 The commentary below is intended to be of assistance, in particular, to governmental officials and other policy makers in a country that would currently be considered a Non-Netting Jurisdiction, in the sense we have used that term in paragraph 1.17 above. A reference in the commentary below to a “Local Party” is to a party organized in that jurisdiction, that could be subject to insolvency proceedings (as defined in section 1 of Part I of the 2018 MNA) and would therefore, in such a case, be an insolvent party (as defined in section 1 of Part I of the 2018 MNA) for the purposes of netting legislation modelled on the 2018 MNA. A reference below to a “Counterparty” is to the other party to the relevant netting agreement or related collateral arrangement, seeking to enforce against the Local Party.

Part I (Netting): section 1 (Definitions)

- 7.6 Section 1 of Part I of the 2018 MNA sets out key definitions used in the remainder of Part I of the 2018 MNA. Particularly important definitions include “person”, “qualified financial contract”, “netting” and “netting agreement. Regarding these definitions, see the discussion in part 3 of this Guide,
- 7.7 In addition, the following points may be helpful in relation to the terms “netting” and “netting agreement”:
- (a) Sub-clause (a) of the definition of “netting” refers, in effect, to the triggering of the close-out netting process. Sub-clause (b) describes the netting process itself.
 - (b) As discussed elsewhere in this Guide,⁵⁰ the 2018 MNA recognises that in certain circumstances it is justified and, indeed, important for a party’s early termination rights under a netting agreement to be limited by provisions of the resolution legislation to the effect that (i) a party may not terminate transactions solely on the basis of other party’s entry into resolution and (ii) a party’s right to terminate transactions in other circumstances may be subject to a temporary stay of no more than 48 hours in accordance with the *FSB Key Attributes*. Any such limitations, however, strictly speaking only affect what event or circumstance is permitted to trigger the process of close-out netting. Under no circumstances should any aspect of sub-clause (b) of the definition, which describes the process of close-out netting, be restricted in the case of resolution or in any other case.
 - (c) In sub-clause (a) of the definition of “netting” the words “with respect to the other person” are deliberately placed after the words “event of default” and not after the words “termination event. The reason for this is as follows:
 - (i) An event of default necessarily always occurs in relation to a party to the agreement, whereas the position in relation to a termination event is less clear-cut.
 - (ii) A termination event is an event that permits a party to terminate transactions early, but not on the basis of a default. Instead, some event or circumstance has occurred that makes it necessary or desirable that some or all of the transactions should be terminated. Classic examples include a legislative or regulatory change that makes it illegal or uneconomic to continue a particular type of transaction or a tax change that makes it uneconomic to continue a particular type of transaction.
 - (iii) As illustrated by Section 5(b) of the ISDA Master Agreement, which party is entitled to terminate following a termination event and in relation to which transactions will depend on the circumstances. By contrast, with an event of

⁵⁰ See paras 1.9-1.11 and 4.32-4.34.

default, there is always a defaulting party and a non-defaulting party, and it is always the case that all transactions are terminated.⁵¹

- (d) The definition of “netting” uses the terms “agreement” and “person” rather than “netting agreement” and “party”, to avoid circularity. “Netting agreement” is then defined by reference to “netting”, and “party” is defined by reference to “netting agreement”.

7.8 In prior versions of the Model Netting Act, section 1 of Part I included the defined term “Bank”. This has been changed to “Authority”, for the reasons discussed in paragraphs 7.10 to 7.13 below in relation to section 2 of Part I of the 2018 MNA.

7.9 In prior versions of the Model Netting Act, section 1 of Part I included the defined term “liquidator” rather than the term “insolvency practitioner”, which is used in the 2018 MNA. The latter definition has been used in the 2018 MNA better to reflect the fact that an insolvent party active in the financial markets is as likely, if not likelier, to enter initially into some form of reorganization proceedings, rather than liquidation proceedings, even if the reorganization eventually ends with a liquidation in whole or in part of the insolvent party.⁵²

Part I (Netting): section 2 (Powers of the Authority)

7.10 The definition of “qualified financial contract” is, as discussed in paragraphs 3.3 to 3.10 above, intended to be broad in order not only (a) to capture all existing types of derivative and related financial transactions that might be subject to a netting agreement, but also (b) to allow for continuing innovation and development in the financial markets.

7.11 Nonetheless, there could be uncertainty as to whether a certain type of transaction falls within the scope of the netting legislation. In such a case, the appropriate public supervisory authority for the financial markets in the jurisdiction may determine that it would be beneficial to systemic stability to specify that a particular type of transaction is protected by the netting legislation. It would do so in accordance with the power granted by section 2 of Part I of the 2018 MNA.

7.12 Although section 2 provides that the relevant authority would exercise its power “by notice”, the drafting should be adapted as appropriate to reflect the normal means by which the authority would exercise its rule-making powers. Accordingly, rather than “by notice”, it may be preferable to use the phrase “by regulation”, “by promulgation of a rule”, “by order”, “by decree” or some similar phrase that more accurately reflects the appropriate local mechanism.

7.13 When the first three versions of the Model Netting Act were prepared in 1997, 2002 and 2006, it was assumed that the central bank would be the appropriate authority to exercise the power granted by this section. It is now recognised that in many jurisdictions the relevant authority may not be the central bank but another public body with specific supervisory authority over the financial markets. Accordingly, the defined term “Bank” from prior versions has been replaced by “Authority” in section 1 of Part I of the 2018 MNA.

⁵¹ This is true, at any rate, in relation to the ISDA Master Agreement. Following a default, all transactions should be terminated in order to preserve the correct net position as between the parties. A non-defaulting party should not have the right to terminate some, but not all transactions. Such a right is likely to be at risk of successful challenge by an insolvency practitioner under the insolvency law of most, if not all, jurisdictions where there is a developed derivatives market.

⁵² See also para 4.17 above.

Part I (Netting): section 3 (Enforceability of a Qualified Financial Contract)

(a) Gaming and wagering laws

7.14 As discussed in paragraph 4.11 above, section 3(a) addresses a pre-insolvency enforceability issue that often arises in a jurisdiction that is beginning to develop its local derivatives market. Longstanding gaming and wagering laws, which generally pre-date the development of modern financial markets may inadvertently catch derivative transactions, notwithstanding that such transactions are entered into for investment or financial risk management purposes.

(b) Qualified financial contract considered Shari'a compliant at its inception

7.15 With the growth of Islamic finance over the past fifteen years, situations have sometimes arisen where, after parties have entered into a Shari'a compliant transaction, a party has sought to repudiate or avoid the transaction on the basis that a relevant Islamic scholar has changed his view on the Shari'a compliance of the transaction. This provision seeks to address that risk, as discussed in further detail in paragraph 4.12 above.

Part I (Netting): section 4 (Enforceability of a Netting Agreement)

(a) General rule

7.16 Section 4(a) sets out the most important single rule in the 2018 MNA. It is drafted to apply to all possible insolvency proceedings that could be commenced in relation to a Local Party. This is key. If section 4(a) applies to some, but not all, relevant types of insolvency proceeding that could be applied to the Local Party, then the purpose of the netting legislation is defeated, since the Counterparty cannot be sure *a priori* that the Local Party will not be subject to a form of insolvency proceedings that is not within the protection of this rule. In such a case, the jurisdiction would continue to be considered a Non-Netting Jurisdiction, even though it had enacted netting protection for some types of insolvency proceeding.⁵³

7.17 Strictly speaking, sections 4(b) to 4(h) should not be necessary if section 4(a) is interpreted broadly to give it its full effect. Given, however, that the purpose of netting legislation is to provide a high level of legal certainty as to the enforceability of close-out netting, sections 4(b) to 4(h) deal with insolvency-related laws and rules that have, in the past in some jurisdictions, raised doubts regarding the ability of a non-insolvent party fully and effectively to enforce close-out netting under a netting agreement. Accordingly, these provisions put those issues expressly beyond doubt, but without prejudice to the generality of section 4(a).

(b) Limitation on obligation to make payment or delivery

7.18 Section 4(b) clarifies that after commencement of insolvency proceedings in relation to a party, the only obligation of either party is to pay the amount due after the operation of close-out netting under the relevant netting agreement. This reinforces the general rule in section 4(a).

⁵³ This situation has arisen in the past in countries where there was netting legislation, but a new type of insolvency procedure was introduced (often within a very short timeframe to address the sudden insolvency of an important local entity) that was not within the scope of the netting legislation. In each case, the jurisdiction briefly became a Non-Netting Jurisdiction until the local legislature was able to amend the netting legislation to cover the new insolvency procedure. The definition of "insolvency proceedings" in section 1 of Part I of the 2018 MNA is deliberately broad and open-ended in order to minimize or avoid this potential difficulty.

(c) *Limitation on right to receive payment or delivery*

7.19 Section 4(c) is the counterpart to section 4(b) and also reinforces the general rule in section 4(a). The combined effect of sections 4(b) and 4(c) is that there is a single amount due post-insolvency. If it is due from the insolvent party, then it is subject to the ordinary rules that apply to debts owed by the insolvent party. This will in turn depend on whether the net amount due has been collateralised or is unsecured. Any stay on enforcement that applies under the law of the insolvency proceedings applicable to the insolvent party will apply to enforcement of the net claim due from the insolvent party. If the net amount is due to the insolvent party, then it is an asset of the insolvent estate, and the insolvency practitioner will seek to collect it from the non-insolvent party for the benefit of the other creditors, subject, however, to any right of set-off that the non-insolvent party may have.⁵⁴

(d) *Limitation on powers of the insolvency practitioner*

7.20 Section 4(d) makes it explicit that an insolvency practitioner may not exercise any “cherry-picking” power in a manner that disrupts close-out netting. Once the close-out netting provision has operated and produced a net amount, that amount is either a debt due by the insolvent party, which is then dealt with under the ordinary rules applicable to debts owed by the insolvent party, as discussed in paragraph 7.19 above, or it is a debt due to the insolvent party, in which case it will be collected by the insolvency practitioner as an asset of the insolvent estate, but subject to any right of set-off that the non-solvent party may have.

(e) *Limitation of insolvency laws prohibiting set-off*

7.21 Many jurisdictions limit the right of a creditor to exercise a right of set-off or similar right to offset or net obligations once insolvency proceedings have commenced. Section 4(e) is intended to put beyond doubt that any such limitations do not apply to limit netting under a netting agreement falling within the scope of legislation based on the 2018 MNA. This reinforces the general rule in section 4(a).

(f) *Preferences and fraudulent transfers*

7.22 Section 4(f) is not intended to be a blanket exemption of a netting agreement, a related collateral arrangement or any qualified financial contract entered into under the netting agreement from the ordinary insolvency rules applicable to preferences and fraudulent transfers. It is intended to clarify simply that the mere fact that a transfer occurred or an obligation was incurred during a relevant suspect period should not affect the enforceability of close-out netting. Something more must be present, namely, an actual intent to “hinder, delay or defraud” any creditor or creditors.

7.23 To give an example: if (a) an ISDA Master Agreement were put in place and a number of transactions were entered into between two parties prior to a relevant suspect period in relation to a party that became insolvent and then (b) a Credit Support Annex were put in place during the relevant suspect period, then the Credit Support Annex could, potentially, be a preference or

⁵⁴ We are referring here to any form of set-off that may apply after the operation of the close-out netting provision, e.g. a contractual right of set-off in the netting agreement itself, as discussed in para 3.22, or a right of set-off available on some other basis, e.g. legal or independent set-off, equitable or transactional set-off, statutory set-off and so on.

fraudulent transfer, although only if there is clear and convincing evidence that the intention of the insolvent party in agreeing to enter into the Credit Support Annex was, in effect, to defraud other creditors of the insolvent party.

7.24 The general principle is that if the relevant netting agreement and any related collateral arrangement were entered into prior to a suspect period, then the mere fact that transfers occur or obligations arise during the suspect period under the normal operation of the netting agreement or collateral arrangement should not engage the rules relating to preferences and fraudulent transfers. It is part of the nature of netting agreements and related collateral arrangements that there are on-going transfers and obligations, and this will continue to be true in the period immediately before a party enters insolvency proceedings. Only negligent or fraudulent or otherwise unfair transfers or obligations should be caught by the rules for preferences and fraudulent transfers. This is, of course, often quite a technical area of insolvency law, and the language proposed in section 4(f) may need to be adjusted in a particular jurisdiction to achieve the policy goal outlined in this paragraph.

(g) *No stay or moratorium*

7.25 Section 4(g) clarifies that any stay, moratorium or other order having a similar effect shall not apply to limit or delay the operation of close-out netting under a netting agreement. This is, however, without prejudice to section 4(j) where the insolvent party is a financial institution subject to resolution proceedings (whether due to its insolvency or any other reason for resolution under the relevant legislation providing for resolution). This provision reflects the fact that the inability to close out promptly following an event of default can lead to unacceptable levels of market risk and credit risk, potentially giving rise to a “contagion effect” where the insolvent party is systemically important and therefore potentially threatening the stability of the financial system.⁵⁵

(h) *Realization and liquidation of collateral*

7.26 Section 4(h) reinforces the general rule specifically in relation to enforcement of collateral. The value of financial collateral is by its nature volatile. It is important that following the early termination of transactions under a netting agreement, any related collateral arrangement may be enforced promptly in order to crystallize the position and prevent further losses for either party due, for example, to the deterioration of collateral values.

(i) *Scope of this provision*

7.27 Section 4(i) deals principally with the issue discussed in footnote 35, sometimes referred to as “bad apple” risk. Sub-clause (i) deals with it in the context of a netting agreement and sub-clause (ii) deals with it in the context of a collateral arrangement. The basic principle is that the netting agreement or collateral arrangement should continue to apply in relation to any qualified financial contracts, even if other types of “agreements, contracts or transactions” that are not qualified financial contracts have been included within the contractual arrangements.

⁵⁵ This was acknowledged by the FSB in the *FSB Key Attributes* and reflected in the rule that any temporary stay of early termination rights under a resolution regime should be limited to two business days, as noted in para 1.9 of this Guide.

- 7.28 Sub-clause (iii) of section 4(i) reinforces the single agreement nature of a netting agreement, which is often set out expressly in the netting agreement, and to that extent reinforces the general rule in section 4(a) and the anti-“cherry-picking” rule 4(d).
- 7.29 Sub-clause (iv) of section 4(i) deals with multibranch netting and should only be included if legislation based on Optional Part II is being enacted.
- (j) *Financial institution in resolution proceedings*
- 7.30 Section 4(j) gives effect to the necessary, but limited, override of early termination rights under a netting agreement that is contemplated in the *FSB Key Attributes* and implemented under the various resolution regimes that have been put in place or amended and updated in recent years in light of the *FSB Key Attributes*. It is necessary to include precise references to the relevant provisions of the resolution legislation. It is important that those references are carefully drafted and limited as described in italics in section 4(j) of the 2018 MNA.

Optional Part II (Multibranch Netting): section 1 (Additional Definitions)

- 7.31 Section 1 of Optional Part II sets out definitions that are used exclusively in Optional Part II. These are in addition to the definitions set out in section 1 of Part I, which apply to both parts of the 2018 MNA. As noted in part 5 of this Guide, the provisions of Optional Part II are based on provisions successfully enacted in the US in the State of New York, where New York banking law in relation to the New York branch of a foreign bank is subject to ring-fencing of local assets for the benefit of creditors of the New York branch.
- 7.32 Optional Part II deals with a situation where the insolvent party is a local branch or agency of a foreign multibranch party. It applies where the local branch is subject to local insolvency proceedings, even if the foreign party as a whole is not subject to insolvency proceedings in its home jurisdiction or elsewhere. This is reflected in the definition of “insolvent local branch”.
- 7.33 Key definitions include “global net payment obligation”, “local net payment obligation”, “global net payment right” and “local net payment right”:
- (a) The *global net payment obligation* is the net amount due under the multibranch netting agreement viewed as a whole in a case where the foreign multibranch party is out-of-the-money on a net basis. This would normally be payable by the foreign multibranch party to the non-insolvent party. It is an obligation arising under the close-out netting provisions of the multibranch netting agreement and would not normally be specifically allocated as a liability to any branch, including the insolvent local branch. Instead, it would be an obligation of the foreign multibranch party as a whole, and by implication principally payable, once close-out has occurred, by the head office of the foreign multibranch party. Whether that is true in a particular case will depend on the proper interpretation of the multibranch netting agreement.
 - (b) The *local net payment obligation* is the amount the foreign multibranch party would have owed to the non-insolvent party if the only transactions between the foreign multibranch party and the non-insolvent party were those entered into through the

insolvent local branch. This is normally a theoretical amount,⁵⁶ but it is necessary to determine it in order to operate the provisions of section 2(a).

- (c) The *global net payment right* is the net amount due under the multibranch netting agreement viewed as a whole in a case where the non-insolvent party is out-of-the-money on a net basis. This would normally be payable by the non-insolvent party to the foreign multibranch party or, if it is in insolvency proceedings in its home jurisdiction, to the home jurisdiction insolvency practitioner. It is a right of the foreign multibranch party arising under the close-out netting provisions of the multibranch netting agreement and would not normally be specifically allocated as a right to any branch, including the insolvent local branch. Instead, it would be a right of the foreign multibranch party as a whole, and by implication principally payable, once close-out has occurred, to the head office of the foreign multibranch party or its home jurisdiction insolvency practitioner. Whether that is true in a particular case will depend on the proper interpretation of the multibranch netting agreement.
- (d) The *local net payment right* is the amount the non-insolvent party would have owed to the foreign multibranch party if the only transactions between the foreign multibranch party and the non-insolvent party were those entered into through the insolvent local branch. As in the case of a local net payment obligation, this is normally a theoretical amount,⁵⁷ but it is necessary to determine it in order to operate the provisions section 2(b).

7.34 In each of sections 2(a) and 2(b) the value of any collateral applied to discharge a global net payment obligation or global net payment right, as the case may be, is also brought into account, and an appropriate adjustment is made to the amount deemed⁵⁸ to be owed by or to the insolvent local branch.

Optional Part II (Multibranch Netting): section 2 (Enforceability of a Multibranch Netting Agreement against an Insolvent Local Branch)

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

7.35 Section 2(a)(i) limits the liability of the insolvent local branch in circumstances where the foreign multibranch party owes a global net payment obligation after the operation of the close-out netting provisions of the multibranch netting agreement. The liability of the insolvent local branch is deemed to be the lesser of the global net payment obligation and the local net payment obligation (the “**capped local branch liability**”).⁵⁹

⁵⁶ It would be theoretical unless the only transactions between the parties are those between the non-insolvent party and the insolvent local branch. Even if that is the case, however, it would normally be an amount owed by the non-insolvent party to the foreign multibranch party as a whole, rather than specifically to the insolvent local branch, although that will again depend on the proper interpretation of the multibranch netting agreement.

⁵⁷ See n 56.

⁵⁸ It is “deemed to be owed” because, as a general rule, as already noted, once a close-out has occurred, the fact that transactions were booked in individual branches of the foreign multibranch party ceases to be relevant. The net close-out amount is owed, as a contractual matter, by or to the foreign multibranch party as a whole, and therefore, by implication, by or to its head office. Once again, though, this depends on the proper interpretation of the multibranch netting agreement.

⁵⁹ The liability is “deemed to be” because, as previously noted, it would normally be the case that under the multibranch netting agreement the liability would not specifically be allocated to the branch. It would be a liability of the foreign multibranch party as a whole. However, in a jurisdiction that imposes ring-fencing, it is possible that, regardless of the strict contractual position, the capped local branch liability would be considered a liability of the insolvent local branch.

- 7.36 The amount limited by section 2(a)(i) is then further reduced under section 2(a)(ii) to take account of:
- (a) any payment made to the non-insolvent party in respect of the global net payment obligation, but only in circumstances where that payment is enough to cover the capped local branch liability; and
 - (b) the application of collateral under any related collateral arrangement.
- 7.37 In relation to (a) in paragraph 7.36 above, the payment made to the insolvent party is taken into account by adding the amount of such payment (A) to the capped local branch liability (B) and then comparing the sum of A and B with the global net payment obligation (C). If A plus B is greater than C, then the capped local liability is reduced by the difference. If A plus B is equal to or less than C, then no reduction is made.
- (b) *Limitation on the foreign multibranch party's rights to receive payment.*
- 7.38 Section 2(b)(i) limits the liability of the non-insolvent party in circumstances where it owes a global net payment right after the operation of the close-out netting provisions of the multibranch netting agreement. The liability of the non-insolvent party is limited to the lesser of the global net payment right and the local net payment right (the “**capped local branch payment right**”). The purpose of this provision is to protect the non-insolvent party from the unfairness that would ensue if it were required to pay more than the global net payment right in circumstances where the local net payment right exceeds the global net payment right.
- 7.39 The capped local branch payment right is then further reduced under section 2(a)(ii) to take account of:
- (a) any payment made by the non-insolvent party in respect of the global net payment obligation to the foreign multibranch party or any insolvency practitioner for the foreign multibranch party, in the local jurisdiction, the home jurisdiction or elsewhere, but only in circumstances where that payment is enough to cover the capped local branch payment right; and
 - (b) the application of collateral under any related collateral arrangement.
- 7.40 In relation to (a) in paragraph 7.39 above, the payment made by the insolvent party is taken into account by adding the amount of such payment (A) to the capped local branch payment right (B) and then comparing the sum of A and B with the global net payment right (C). If A plus B is greater than C, then the capped local payment right is reduced by the difference. If A plus B is equal to or less than C, then no reduction is made.

Optional Part II (Multibranch Netting): section 3 (Collateral for a Multibranch Netting Agreement)

- 7.41 Section 3 of Optional Part II of the 2018 MNA sets out an important protection for the non-insolvent party, providing legal certainty that it will not be required to disgorge any collateral held to secure the obligations of the foreign multibranch party until it has had the

opportunity to operate the close-out netting provisions of the multibranch netting agreement and then apply the collateral to discharge the global net payment obligation of the foreign multibranch party. Section 3 makes it clear that the non-insolvent party must promptly return any excess collateral, although that would normally apply in any event both under the contractual terms governing the collateral arrangement and under the substantive law that applies to the collateral arrangement.

2018 MODEL NETTING ACT

[Part I: Netting]⁶⁰1. **Definitions**

For the purposes of this Act the following definitions apply:

“Authority” means the *[insert name of the central bank or other relevant financial authority for the 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:

- (a) cash in any currency;
- (b) securities of any kind, including, without limitation, debt and equity securities; sukuk and fund interests;
- (c) guarantees, letters of credit and obligations to reimburse; and
- (d) any asset commonly used as collateral in *[insert name of 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 to which a netting agreement applies, including, without limitation:

- (a) a pledge or any other form of security interest in collateral, whether possessory or non-possessory;
- (b) a title transfer collateral arrangement; and
- (c) 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; or a netting agreement;

“insolvency practitioner” 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 name of jurisdiction]*;

“insolvency proceedings” means any collective proceedings, other than resolution proceedings, under the laws of *[insert name of jurisdiction]* affecting the claims of creditors of an insolvent party

⁶⁰ This Part heading should be deleted if not also enacting Part II (Multibranch Netting).

including liquidation, winding up, reorganisation, rehabilitation, administration, receivership, conservatorship or other similar form of collective proceedings;⁶¹

“insolvent party” is the party in relation to which insolvency proceedings under the laws of [insert name of jurisdiction] have been instituted;

“netting” means the operation of a set of provisions in an agreement between two persons that:

- (a) may be commenced by notice given by one person to the other person upon the occurrence of an event of default with respect to the other party or other termination event or that may, in certain circumstances, occur automatically as specified in the agreement; and
- (b) has the following effect:
 - (i) the termination, liquidation and/or acceleration of any present or future payment or delivery rights or obligations arising under or in connection with one or more qualified financial contracts to which a netting agreement applies;
 - (ii) the calculation or estimation of a close-out value, market value, liquidation value or replacement value in respect of each right and obligation or group of rights and obligations terminated, liquidated and/or accelerated under (i) and the conversion of each such value into a single currency; and
 - (iii) the determination of the net balance of the values calculated under (ii), whether by operation of set-off or otherwise, giving rise to the obligation of one person to pay an amount equal to the net balance to the other person;

“netting agreement” means an agreement between two persons that provides for netting, including, without limitation:

- (a) an agreement that provides for the netting of amounts due under two or more netting agreements; and
- (b) a collateral arrangement relating to or forming part of a netting agreement;

“non-insolvent party” is the party that is not the insolvent party;

“party” means a person that is a party to a netting agreement;

“person” includes an [individual], [partnership], [corporation], [regulated entity such as a bank, investment firm, securities or commodities dealer, insurance company or investment manager], [or any other body corporate whether organized under the laws of [insert name of 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];

⁶¹ This provisions should ideally be adapted to refer to the specific types of insolvency proceedings available under local law. It should be drafted broadly enough to cover all possible forms of insolvency proceeding that could potentially apply to an insolvent party organized in the jurisdiction.

“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, under 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, including, without limitation:

- (a) a currency, cross-currency or interest rate swap or profit 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, including a derivative on physical transmission rights, financial transmission rights or transmission capacity;
- (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, fund interest, weather, bonds and other debt instruments, sukuk, 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);
- (z) an instrument, agreement or transaction that is or effects the economic equivalent of one of the instruments, agreements or transactions referred to in paragraphs (a) to (y) through use of a murabaha, musawama or wa'ad or any other structure commonly used for the purpose of effecting Shari'a compliant instruments, agreements or transactions; and
- (aa) any agreement, contract or transaction designated as a qualified financial contract by the Authority under this Act;

“resolution proceedings” means a statutory regime for the recovery and resolution of a financial institution following a significant deterioration in its financial position, including any preventive measures taken or powers exercised by a competent public authority in relation to the financial institution under the statutory regime prior to a financial institution’s formal entry into resolution and including, without limitation, any insolvency proceedings in relation to the financial institution, or the whole or part of its business, following its formal entry into resolution;

“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 Authority.** The Authority 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) **Gaming and wagering laws.** A qualified financial contract shall not be and shall be deemed never to have been void or unenforceable by reason of [*insert reference to the applicable law*] relating to games, gaming, gambling, wagering or lotteries.

(b) **Qualified financial contract considered Shari’a compliant at its inception.** If, at the time a person enters into a qualified financial contract (or any agreement relating to such qualified financial contract), the person represents or otherwise indicates to the other party to the qualified financial contract that it is satisfied that the qualified financial contract is Shari’a compliant, the person may not subsequently disaffirm, disclaim, repudiate or reject, in whole or in part, its obligations under the qualified financial contract on the basis that the qualified financial contract has ceased to be Shari’a compliant due to a change of interpretation of any relevant rule or principle of the Shari’a or for any other reason.

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 collateral or security for any obligation of the insolvent party and may not be stayed, avoided or otherwise limited by any action taken or power exercised by the insolvency practitioner or by any other provision of law applicable to the insolvent party by virtue of its being subject to insolvency proceedings.

(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 in respect of all rights and obligations terminated, liquidated or accelerated pursuant to the application of netting under that netting agreement shall be its obligation to pay a net amount to the other party as determined in accordance with the terms of the 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 in respect of all rights and obligations terminated, liquidated or accelerated pursuant to the application of netting under that agreement shall be equal to its right to receive a net amount from the other party as determined in accordance with the terms of the netting agreement.

(d) **Limitation on powers of the insolvency practitioner.** Any powers of the insolvency practitioner to assume or repudiate individual contracts or transactions will not prevent the termination, liquidation and/or acceleration of all payment or delivery obligations or rights under one or more qualified financial contracts to which a netting agreement applies, 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 that 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 and/or delivery obligations or rights under one or more qualified financial contracts to which a netting agreement applies 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 insolvency practitioner 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 insolvent party made such transfer, substitution or exchange or 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 such transfer was made or such obligation was incurred.

(g) Pre-emption. No stay, injunction, avoidance, moratorium, or similar proceeding or order, whether issued or granted by a court, administrative agency, insolvency practitioner 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 the realization, appropriation and/or liquidation of collateral to be conducted in a commercially reasonable manner.

(i) Scope of this provision. For the purposes of this section:

(i) 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 section 1 of [this Part of]⁶² 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 section 1 of [this Part of]⁶³ this Act.

(ii) 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 a qualified financial contract entered into under a netting agreement in terms of section 1 of [this Part of]⁶⁴ 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” in section 1 of [this Part of]⁶⁵ this Act.

(iii) A netting agreement and all qualified financial contracts to which a netting agreement applies shall constitute a single agreement.

[(iv) 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 name of jurisdiction*] the enforceability of the provisions of the multibranch netting agreement shall be determined in accordance with Part II of this Act.]⁶⁶

(j) Financial institution in resolution proceedings. In a case where the insolvent party is a financial institution subject to resolution proceedings under [*insert reference to relevant legislation providing for resolution*] (whether due to its insolvency or any other reason for resolution under [*insert reference to relevant legislation providing for resolution*]), the provisions of this Act are without prejudice to the operation of [*insert reference to relevant statutory provisions (i) providing that a party may not terminate transactions with the financial institution in resolution by reason only of its entry into resolution or the exercise by the relevant resolution authority of a resolution measure or power and (ii) providing for a temporary stay of no more than 48 hours in accordance with the FSB Key Attributes*], subject always to the safeguards for netting agreements and collateral arrangements set out in [*insert reference to relevant statutory provisions providing safeguards for close-out netting and collateral arrangements in the relevant resolution legislation*].

⁶² Delete if not enacting optional Part II of this Act.

⁶³ Delete if not enacting optional Part II of this Act.

⁶⁴ Delete if not enacting optional Part II of this Act.

⁶⁵ Delete if not enacting optional Part II of this Act.

⁶⁶ Delete if not enacting optional Part II of this Act.

Optional:⁶⁷

Part II : Multibranch Netting

1. **Additional Definitions**

For the purposes of this Part II of this Act, in addition to the definitions in section 1 of Part I of this Act, the following definitions apply:

“foreign insolvency practitioner” means an insolvency practitioner for a foreign multibranch party under insolvency proceedings in the country in which it is organized or incorporated or in any other country;

“foreign multibranch party” is a person that is not organized or incorporated in [*insert name of jurisdiction*] and that has entered into one or more qualified financial contracts under a netting agreement through its branch or agency in [*insert name of jurisdiction*] and one or more qualified financial contracts through its head or home office in the country in which it is organized or incorporated;

“global net payment obligation” means the amount, if any, owed by the foreign multibranch 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;

“global net payment right” means the amount, if any, owed by the non-insolvent party to the foreign multibranch 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;

“insolvent local branch” means a branch or agency in [*insert name of jurisdiction*] of a foreign multibranch party that is subject to insolvency proceedings in [*insert name of jurisdiction*], regardless of whether the foreign multibranch party is subject to insolvency proceedings in the country in which it is organized or incorporated or in any other country;

“local insolvency practitioner” means an insolvency practitioner for the insolvent local branch under insolvency proceedings in [*insert name of jurisdiction*];

“local net payment obligation” means the amount, if any, that would have been owed by the foreign multibranch party to the non-insolvent party after netting only those qualified financial contracts entered into by the non-insolvent party with the insolvent local branch under a multibranch netting agreement;

“local net payment right” means the amount, if any, that would have been owed by the non-insolvent party to the foreign multibranch party after netting only those qualified financial contracts entered into by the non-insolvent party with the insolvent local branch under a multibranch netting agreement.

⁶⁷ Part II of the Model Netting Act is optional. See part 5 of this Guide and, in particular, para 5.4.

“multibranch netting agreement” means a netting agreement between two persons under which at least one person is a foreign multibranch party with a branch or agency in [*insert name of jurisdiction*];

“party” means, for purposes of this Part II of this Act, a person that is a party to a multibranch netting agreement.

2. **Enforceability of a Multibranch Netting Agreement against an Insolvent Local Branch.**

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

(i) The liability of an insolvent local branch to a non-insolvent party 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:

- (A) the global net payment obligation; and
- (B) the local net payment obligation.

(ii) The liability of the insolvent local branch under sub-clause (i) shall be reduced, but not below zero, by:

- (A) any amount otherwise paid to or received by the non-insolvent party in respect of the global net payment obligation under the multibranch netting agreement which, if added to the liability of the insolvent local branch under clause (i), would exceed the global net payment obligation; and
- (B) the fair market value of, or the amount of any proceeds of, collateral that secures or supports the obligations of the foreign multibranch party under the multibranch netting agreement and has been applied by the non-insolvent party to satisfy the obligations of the foreign multibranch party under the multibranch netting agreement.

(b) Limitation on the foreign multibranch party’s right to receive payment.

(i) The liability of a non-insolvent party to an insolvent local branch under a multibranch netting agreement shall be calculated as of the date of termination of the qualified financial contracts enter into under such multibranch netting agreement in accordance with its terms and shall be limited to the lesser of:

- (A) the global net payment right; and
- (B) the local net payment right.

(ii) The liability of the non-insolvent party under sub-clause (i) shall be reduced, but not below zero, by:

(A) any amount otherwise paid to or received by:

- (1) the local insolvency practitioner on behalf of the insolvent local branch; and/or
- (2) any foreign insolvency practitioner on behalf of the foreign multibranch party

in respect of the global net payment right under the multibranch netting agreement which, if added to the liability of the non-insolvent party under sub-clause (i), would exceed the global net payment right; and

(B) 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 under the multibranch netting agreement and has been applied by the foreign multibranch party or any insolvency practitioner acting on its behalf to satisfy the obligations of the non-insolvent party under the multibranch netting agreement to the foreign multibranch party.

3. **Collateral for a Multibranch Netting Agreement.** If the non-insolvent party to a multibranch netting agreement has taken collateral under a collateral arrangement that secures or supports the obligations of the foreign multibranch party under the multibranch netting agreement, the non-insolvent party may retain such collateral and apply it in satisfaction of the obligation of the foreign multibranch party in respect of the global net payment obligation. The non-insolvent party must promptly, after such application, return any excess collateral to the foreign multibranch party.

**2013 UNIDROIT PRINCIPLES ON THE OPERATION OF
CLOSE-OUT NETTING PROVISIONS**

The complete text of the 2013 UNIDROIT Principles on the Operation of Close-Out Netting Provisions is composed of both black-letter rules (reproduced below with the kind permission of UNIDROIT) and accompanying Comments. The full text is available on UNIDROIT's website at:

<https://www.unidroit.org/english/principles/netting/netting-principles2013-e.pdf>

PRINCIPLE 1

Scope of the Principles

- (1) These Principles deal with the operation of close-out netting provisions that are entered into by eligible parties in respect of eligible obligations.
- (2) Except as otherwise expressly indicated in these Principles, the term 'operation' encompasses the creation, validity, enforceability, effectiveness against third parties and admissibility in evidence of a close-out netting provision.

PRINCIPLE 2

Definition of 'close-out netting provision'

'Close-out netting provision' means a contractual provision on the basis of which, upon the occurrence of an event predefined in the provision in relation to a party to the contract, the obligations owed by the parties to each other that are covered by the provision, whether or not they are at that time due and payable, are automatically or at the election of one of the parties reduced to or replaced by a single net obligation, whether by way of novation, termination or otherwise, representing the aggregate value of the combined obligations, which is thereupon due and payable by one party to the other.

PRINCIPLE 3

Definition of 'eligible party' and related notions

- (1) 'Eligible party' means any person or entity, other than a natural person who is acting primarily for personal, family or household purposes, and includes a partnership, unincorporated association or other body of persons.
- (2) 'Qualifying financial market participant' means any of the following:
 - (a) a bank, investment firm, professional market maker in financial instruments or other financial institution which (in each case) is subject to regulation or prudential supervision;

- (b) an insurance or reinsurance company;
 - (c) an undertaking for collective investment or an investment fund;
 - (d) a central counterparty or a payment, clearing or settlement system, or the operator of such a system which (in each case) is subject to regulation, oversight or prudential supervision;
 - (e) a corporation or other entity that, according to criteria determined by the implementing State, is authorized or supervised as an important participant in the implementing State's markets in contracts giving rise to eligible obligations.
- (3) 'Public authority' means any of the following:
- (a) a governmental or other public entity;
 - (b) a central bank;
 - (c) the Bank for International Settlements, a multilateral development bank, the International Monetary Fund or any similar entity.

PRINCIPLE 4

Definition of 'eligible obligation'

- (1) 'Eligible obligation' means:
- (a) an obligation arising under a contract of any of the following kinds between eligible parties at least one of which is a public authority or a qualifying financial market participant:
 - (i) Derivative instruments, that is to say, options, forwards, futures, swaps, contracts for differences and any other transaction in respect of an underlying or reference asset or a reference value that is, or in future becomes, the subject of recurrent contracts in the derivatives markets;
 - (ii) Repurchase agreements, securities lending agreements and any other securities financing transaction, in each case in respect of securities, money market instruments or units in an undertaking for collective investment or an investment fund;
 - (iii) Title transfer collateral arrangements related to eligible obligations;
 - (iv) Contracts for the sale, purchase or delivery of:
 - a. securities;
 - b. money market instruments;
 - c. units in an undertaking for collective investment or an investment fund;
 - d. currency of any country, territory or monetary union;

e. gold, silver, platinum, palladium or other precious metals;

(b) an obligation of an eligible party (whether by way of surety or as principal debtor) to perform an obligation of another person which is an eligible obligation under sub-paragraph (a);

(c) a single net obligation determined under a close-out netting provision entered into by the same parties in respect of obligations under subparagraph (a) or (b).

(2) An implementing State may elect to broaden the scope of paragraph (1)(a) in one or both of the following ways:

(a) by providing that it is to extend to obligations arising under contracts between parties neither of whom is a public authority or a qualifying financial market participant;

(b) by providing that it is to extend to obligations not limited to those listed in paragraph (1);

subject, in either case, to such limitations or exceptions as the implementing State may specify.

PRINCIPLE 5

Formal acts and reporting requirements

(1) The law of the implementing State should not make the operation of a close-out netting provision dependent on:

(a) the performance of any formal act other than a requirement that a close-out netting provision be evidenced in writing or any legally equivalent form;

(b) the use of standardized terms of specific trade associations.

(2) The law of the implementing State should not make the operation of a close-out netting provision and the obligations covered by the provision dependent on the compliance with any requirement to report data relating to those obligations to a trade repository or similar organization for regulatory purposes.

PRINCIPLE 6

Operation of close-out netting provisions in general

(1) The law of the implementing State should ensure that a close-out netting provision is enforceable in accordance with its terms. In particular, the law of the implementing State:

(a) should not impose enforcement requirements beyond those specified in the close-out netting provision itself;

(b) should ensure that, where one or more of the obligations covered by the close-out netting provision are, and remain, invalid, unenforceable or ineligible, the operation of the close-out

netting provision is not affected in relation to those covered obligations which are valid, enforceable and eligible.

(2) These Principles do not render enforceable a close-out netting provision or an eligible obligation that would otherwise be unenforceable in whole or in part on grounds of fraud or conflict with other requirements of general application affecting the validity or enforceability of contracts.

PRINCIPLE 7

Operation of close-out netting provisions in insolvency and resolution

(1) Subject to Principle 8 and in addition to Principle 6, the law of the implementing State should ensure that upon the commencement of an insolvency proceeding or in the context of a resolution regime in relation to a party to a close-out netting provision:

(a) the operation of the close-out netting provision is not stayed;

(b) the insolvency administrator, court or resolution authority should not be allowed to demand from the other party performance of any of the obligations covered by the close-out netting provision while rejecting the performance of any obligation owed to the other party that is covered by the close-out netting provision;

(c) the mere entering into and operation of the close-out netting provision as such should not constitute grounds for the avoidance of the close-out netting provision on the basis that it is deemed inconsistent with the principle of equal treatment of creditors;

(d) the operation of the close-out netting provision, and the inclusion of any obligation in the calculation of the single net obligation under the close-out netting provision, should not be restricted merely because the close-out netting provision was entered into, an obligation covered by the provision arose or the single net obligation under the close-out netting provision became due and payable during a prescribed period before, or on the day of but before, the commencement of the proceeding.

(2) These Principles do not affect a partial or total restriction of the operation of a close-out netting provision under the insolvency law of the implementing State on grounds which include factors other than, or additional to, those referred to in sub-paragraphs (c) and (d) above, such as knowledge of a pending insolvency proceeding at the time the close-out netting provision was entered into or the obligation arose, the ranking of categories of claims, or the avoidance of a transaction as a fraud of creditors.

PRINCIPLE 8

Resolution of financial institutions

These Principles are without prejudice to a stay or any other measure which the law of the implementing State, subject to appropriate safeguards, may provide for in the context of resolution regimes for financial institutions.

ISDA NETTING AND COLLATERAL OPINIONS

The following lists the netting and collateral opinions that ISDA has obtained from counsel in the jurisdictions listed below, as at 25 September 2018. For an up-to-date listing of ISDA's full opinions library, see the ISDA website at www.isda.org.⁶⁸

Jurisdiction	Netting	Collateral
	<i>Date of Latest Opinion</i>	<i>Date of Latest Opinion</i>
Anguilla	6 March 2018	6 March 2018
Australia	28 February 2017	8 August 2017
Austria	3 May 2017	20 April 2018
Bahamas	12 December 2016	3 April 2017
Barbados	10 June 2016	10 June 2016
Belgium	13 May 2016	28 February 2017
Bermuda	8 July 2016	12 June 2018
Brazil	23 October 2017	23 October 2017
British Virgin Islands	6 March 2018	6 March 2018
Canada ⁶⁹	21 December 2017	23 December 2017, ⁷⁰ 1 January 2017 ⁷¹
Cayman Islands	29 June 2017	29 June 2017
Chile	14 July 2017	14 July 2017
Colombia	14 December 2017	14 December 2017
Curaçao, Aruba, St Maarten	12 December 2016	<i>Pending</i>
Cyprus	6 August 2018	29 May 2017

⁶⁸ This is a list of the netting and collateral opinions. The full ISDA opinions library includes clearing-related and other opinions that are not included in this table. The up-to-date listing is available on the ISDA website at the following link: <https://www.isda.org/2017/10/02/opinions-overview/>. Note that access to the opinions is limited to ISDA members.

⁶⁹ Federal jurisdiction, Ontario, Alberta, British Columbia and Quebec.

⁷⁰ Federal jurisdiction, Ontario, Alberta and British Columbia.

⁷¹ Quebec.

Jurisdiction	Netting	Collateral
	<i>Date of Latest Opinion</i>	<i>Date of Latest Opinion</i>
Czech Republic	31 January 2017	1 March 2017
Denmark	6 December 2017	6 December 2017
England and Wales	23 June 2017	10 October 2017
Finland	11 April 2017	7 December 2017
France	28 June 2018	13 July 2017
Germany	1 September 2017	1 September 2017
Greece	22 February 2018	27 March 2018
Guernsey	7 December 2017	26 July 2018
Hong Kong	6 July 2017	6 July 2017
Hungary	6 July 2018	28 May 2018
Iceland	5 April 2017	29 August 2017
India	12 February 2016	15 September 2016
Indonesia	9 July 2013	9 July 2013
Ireland	28 June 2018	10 April 2017
Israel	15 May 2018	13 June 2016
Italy	18 January 2018	18 January 2018
Japan	16 October 2017	1 September 2017
Jersey	20 October 2017	7 March 2018
Liechtenstein	28 September 2017	--
Lithuania	8 May 2018	--
Luxembourg	9 March 2017	14 May 2018
Malaysia	7 August 2018	7 August 2018
Malta	27 July 2017	30 August 2017

Jurisdiction	Netting	Collateral
	<i>Date of Latest Opinion</i>	<i>Date of Latest Opinion</i>
Mauritius	25 February 2016	--
Mexico	3 November 2017	3 November 2017
Netherlands	13 June 2017	17 May 2018
New Zealand	19 January 2017	4 July 2017
Norway	22 June 2017	22 August 2017
Peru	17 August 2016	29 September 2016
Philippines	28 March 2016	28 March 2016
Poland	17 July 2017	17 July 2017
Portugal	14 June 2017	13 November 2017
Qatar ⁷²	8 July 2018	--
Romania	18 July 2018	31 July 2018
Russia	17 July 2018	--
Scotland	18 April 2017	5 March 2018
Singapore	7 August 2017	7 August 2017
Slovakia	24 July 2018	--
Slovenia	9 August 2018	<i>Pending</i>
South Africa	9 February 2017	21 June 2018
South Korea	28 November 2017	28 November 2017
Spain	8 June 2017	15 February 2018
Sweden	3 May 2017	30 August 2017
Switzerland	31 May 2017	12 April 2018
Taiwan	18 September 2017	18 September 2017

⁷² Qatar Financial Centre only.

Jurisdiction	Netting	Collateral
	<i>Date of Latest Opinion</i>	<i>Date of Latest Opinion</i>
Thailand	12 December 2017	12 December 2017
Turkey	4 December 2017	4 December 2017
UAE	18 September 2017, ⁷³ 5 October 2016 ⁷⁴	--
USA ⁷⁵	1 March 2018	1 March 2018

⁷³ Abu Dhabi Global Markets (ADGM) free zone.

⁷⁴ Dubai International Financial Centre (DIFC) free zone.

⁷⁵ New York and US federal law, excluding US insurance companies. See ISDA website for information regarding netting opinions in relation to US insurance companies, in relation to which insolvency proceedings are governed by state law rather than US federal law.

STATUS OF NETTING LEGISLATION

Introductory note:

In the table below, we set out ISDA's understanding of the current status of netting legislation in each of the jurisdictions listed in the table, based on information available to ISDA as at the date of publication of this Guide.⁷⁶

In all cases, the information set out in the table is accurate as far as ISDA is aware, but it is set out for general guidance only and is not to be relied. Instead reference should be made to an appropriate source in the relevant country, for example, a governmental source or an appropriately qualified legal or other professional adviser.

What constitutes netting legislation varies from country to country, as discussed elsewhere in this Guide. In some countries, it is a self-standing statute or a distinct chapter of a larger statute or code. In other countries, it is a set of amendments to different existing statutes or code provisions dealing with distinct issues. It is also important to bear in mind that the scope and quality of netting legislation varies from jurisdiction to jurisdiction. The fact that a country has netting legislation usually means, but does not necessarily mean, that close-out netting is enforceable against a local counterparty to the high standard of legal certainty required for recognition of close-out netting as risk-reducing for purposes of capital adequacy rules. In each case, it is necessary to consult with local counsel to confirm the scope and strength of the enforceability of close-out netting against a local counterparty, typically in the form of a fully reasoned legal opinion.⁷⁷

Where the name of a statute is available to ISDA in the (or an) official language of the relevant jurisdiction, we have included it, together, where available, with an English translation. The translation is unofficial, unless otherwise indicated. If there is no current netting legislation in a country but the local legal framework is, at least to some extent, favourable to netting, that is noted in the table together with brief relevant information.⁷⁸ References below to statutes are to such statutes as amended from time to time and as currently in effect, based on information available to ISDA as at the date of publication of this Guide.

⁷⁶ See inside front cover for the date of publication of this Guide. Where ISDA has obtained a netting opinion from local counsel in a particular country (see Appendix C), the description is drawn from the netting opinion. For a number of other countries in relation to which ISDA has not yet commissioned a netting opinion, ISDA has obtained an informal country update from local counsel regarding a number of legal issues relevant to the trading of derivatives, including the enforceability of close-out netting. For some countries, therefore, the description of the netting legislation is drawn from the relevant informal country update. In the case of other countries for which there is no opinion and no informal country update, ISDA has obtained information regarding local netting legislation from one or more appropriate sources in the country.

⁷⁷ See, in this regard, Appendix C.

⁷⁸ Note that in some countries, close-out netting under a netting agreement is fully enforceable to a high degree of legal certainty on the basis of general principles without the need for special legislation. That was historically the case, for example, in England and Wales and in Scotland. The introduction by the Banking Act 2009 of a special resolution regime for banks and building societies meant that limited netting legislation was needed to protect the enforceability of close-out netting against a bank or other financial institution subject to resolution. Against most, if not all, other legal entity types, close-out netting remains enforceable under English and Welsh law and under Scots law without the need for netting legislation. Other jurisdictions where close-out netting is generally enforceable without the need for netting legislation include Hong Kong, the Netherlands and Turkey.

Country	Status of netting legislation
Andorra	<i>Llei 8/2013, del 9 de maig, sobre els requisits organitzatius i les condicions de funcionament de les entitats operatives del sistema financer, la protecció de l'inversor, l'abús de mercat i els acords de garantia financera</i> (Law 8/2013, of May 9 regulating the organizational requirements and functioning conditions of the operative entities of the financial system, investor protection, market abuse and contractual netting agreements, financial collateral arrangements and financial guarantees).
Anguilla	Netting Act (Act 15/2006), Revised Statutes of Anguilla, Chapter N3, in force 19 October 2006, revised 15 December 2006.
Armenia	<p>Netting legislation in Armenia takes the form of amendments to:</p> <ul style="list-style-type: none"> (i) the Law on Bankruptcy (Law N 20-51-Ն of the Republic of Armenia on Bankruptcy dated 25 December 2006, amended as of 27 October 2016) to provide for the enforceability of netting arrangements arising out of financial transactions and collateral arrangements notwithstanding statutory moratoria and the power of a liquidator to unwind transactions post-bankruptcy; and (ii) the Law on Bankruptcy of Financial Institutions (Law N 20-262 of the Republic of Armenia on Bankruptcy of Banks, Credit Organisations, Investment Companies, Investment Fund Managers and Insurance Companies dated 25 December 2006, amended as of 27 October 2016) to provide for the enforceability of netting arrangements notwithstanding the opening of bankruptcy proceedings in relation to a financial institution. <p>Notwithstanding these measures, unwinding of netting and collateral arrangements and/or derivative financial transactions post-bankruptcy remains possible in limited cases.</p>
Argentina	Sections 188-194 of Law No 27,440 (the “Productive Financing Law”), which entered into effect on 19 May 2018.
Australia	Part 4 of the Payment Systems and Netting Act 1998, No. 83, 1998, as amended and in force on 1 June 2016.
Austria	<ul style="list-style-type: none"> (i) <i>Bundesgesetz über das Insolvenzverfahren (Insolvenzordnung) (the Insolvency Code) RGBl. Nr. 337/1914, as amended and in force on 31 July 2017;</i> (ii) <i>Bundesgesetz über das Bankwesen (Bankwesengesetz) (the Banking Act) BGBl. Nr. 532/1993, as amended and in force on 24 April 2018;</i> (iii) <i>Abschnitt 9 des Bundesgesetz über Sicherheiten auf den Finanzmärkten (Finanzsicherheiten-Gesetz) (Section 9 of the Act on Financial Collateral Arrangements), as amended and in force on 20 February 2015</i> (iv) <i>Abschnitt 91 des Bundesgesetz über Investmentfonds (Investmentfondsgesetz 2011) (the Investment Funds Act 2011), as amended and in force on 14 June 2018; and</i> (v) <i>Bundesgesetz über die Sanierung und Abwicklung von Banken (Sanierungs- und Abwicklungsgesetz) (the Act on Banking Recovery and Resolution), BGBl. I Nr. 98/2014, as amended and in force on 14 June 2018.</i>

Country	Status of netting legislation
Bahamas	Close-out netting is enforceable in the Bahamas under general principles without the need for specific legislation. ⁷⁹ Close-out netting is, nonetheless, reinforced in the Bahamas by a specific legislative provision: section 236 of the Companies Act, 1992 as incorporated into the International Business Companies Act, 2000 by section 2 of the International Business Companies (Winding Up Amendment) Act, 2011.
Bahrain	لائحة المفاسدة بموجب عقد السوق (Regulation in respect of Close-Out Netting under a Market Contract), which entered into force on 19 December 2014.
Barbados	Section 35 of the Bankruptcy and Insolvency Act [CAP.303].
Belgium	<p>(i) <i>Articles 4 et 14-16 de la Loi du 15 décembre 2004 relative aux sûretés financières et portant des dispositions fiscales diverses en matière de conventions constitutives de sûreté réelle et de prêts portant sur des instruments financiers</i> (Sections 4 and 14-16 of the Act of 15th December 2004 on financial collateral and on various tax provisions relating to security agreements and loans relating to financial instruments, the “Financial Collateral Act”), which entered into force on 1 February 2005; and</p> <p>(ii) <i>Article 286 de la Loi du 25 avril 2014 relative au statut et au contrôle des établissements de crédit</i> (Article 286 of the Act of 25th April 2014 on the status and control of credit institutions, the “Credit Institutions Act”), which entered into force on 7 May 2014.</p>
Bermuda	Close-out netting is enforceable in Bermuda under general principles without the need for specific legislation. ⁸⁰
Brazil	<i>Artigo 119º e 122º de Lei Nº 11.101, de 9 de Fevereiro de 2005</i> (Articles 119 and 122 of Law No 11.101, of 9 February 2005, the "Bankruptcy Law").
British Virgin Islands	Part XVII of the Insolvency Act 2003.
Bulgaria	There is currently no netting legislation in Bulgaria, but Bulgaria has implemented the EU Financial Collateral Directive. ⁸¹
Canada	<p>(i) Section 65 of the Bankruptcy and Insolvency Act 1992;</p> <p>(ii) Section 22 of the Winding-up and Restructuring Act 1985;</p> <p>(iii) Section 39.15 of the Canada Deposit Insurance Corporation Act 1985;</p> <p>(iv) Section 34 of the Companies’ Creditors Arrangement Act 1985; and</p> <p>(v) Section 13 of the Payment Clearing and Settlement Act 1996.</p>
Cayman Islands	Close-out netting is enforceable in the Cayman Islands under general principles without the need for specific legislation. ⁸²

⁷⁹ See n 78.

⁸⁰ See n 78.

⁸¹ Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements [2002] OJ L168/43.

Country	Status of netting legislation
Channel Islands – Guernsey	Close-out netting is enforceable in Guernsey under general principles without the need for specific legislation. ⁸³
Channel Islands – Jersey	Bankruptcy (Netting, Contractual Subordination and Non-Petition Provisions) (Jersey) Law 2005, as amended and in force on 1 January 2006.
Chile	<i>Capítulo III.D.2 del Compendio de Normas Financieras del Banco denominado Reconocimiento y regulación de convenios marco de contratación de derivados para efectos que indica</i> (Chapter III.D.2 of the Financial Regulations Compendium called the Recognition and regulation of framework agreements for derivatives contracts for effects indicated), which entered into force on 9 April 2018.
Colombia	(i) Artículo 74 de Ley 1328 de 2009 (Article 74 of Law 1328 of 2009), which entered into force on 15 July 2009; and (ii) Decreto Reglamentario 4765 de 2011 (Decree 4765 of 2011), which entered into force on 14 December 2011.
Croatia	(i) <i>Zakon o ništetnosti ugovora o kreditu s međunarodnim obilježnjima sklopljenim u Republici Hrvatskoj</i> (Act on the Nullity of Loan Agreements), which entered into force on 29 July 2017; (ii) <i>Članak 8. Zakona o financijskom osiguranju</i> (Article 8 of the Financial Collateral Act), which entered into force on 1 January 2008; (iii) <i>Stečajni zakon</i> (Bankruptcy Law), which entered into force 1 September 2015; (iv) <i>Zakon o sanaciji kreditnih institucija i investicijskih društava</i> (Act on Recovery of Credit Institutions and Investment Firms), which entered into force on 28 February 2015.
Cyprus	(i) <i>Ο περί Πτώχευσης Νόμος</i> (the Bankruptcy Law), Chapter 5 of the Laws, as amended and in force on 13 July 2018; (ii) <i>Ο περί Εταιρειών Νόμος</i> (the Companies Law), Chapter 113 of the Laws, as amended and in force on 13 July 2018; (iii) <i>Ο περί Εξυγίανσης Πιστωτικών Ιδρυμάτων και Επενδυτικών Εταιρειών Νόμος του 2016</i> (the Resolution of Credit and Other Institutions Law of 2016), N.22(I)/2016, as amended and in force on 18 March 2016; and (iv) <i>Ο Περί των Συμφωνιών Παροχής Χρηματοοικονομικής Εξασφάλισης Νόμος του 2004</i> (Financial Collateral Arrangements Law of 2004), N.43(I)/2004, as amended and in force on 20 October 2017.

⁸² See n 78.

⁸³ See n 78.

Country	Status of netting legislation
Czech Republic	<ul style="list-style-type: none"> (i) § 193 Zákon č. 256/2004 Sb., o podnikání na kapitálovém trhu (Section 193 of Act No. 256/2004 Coll., on Conducting of Business on the Capital Market), as amended and in force on 3 January 2018; (ii) § 2(a) a 6 Zákon č. 408/2010 Sb., o finančním zajištění (Sections 2(a) and 6 of Act, No. 408/2010 Coll., on Financial Collateral), as amended and in force on 3 January 2018; (iii) § 366(2) Zákon č. 182/2006 Sb., o úpadku a způsobech jeho řešení (insolvenční zákon), (Section 366(2) of the Act No. 182/2006 Coll., on Insolvency and Manners of its Resolution), as amended and in force on 1 December 2017; and (iv) Zákon č. 374/2015 Sb., o ozdravných postupech a řešení krize na finančním trhu (Act No. 374/2015 Coll., on Framework for the Recovery and Crisis Resolution on the Financial Market, as amended and in force on 1 January 2017.
Denmark	<ul style="list-style-type: none"> (i) Lov om kapitalmarkeder (the Capital Markets Act), Act. No. 650 of 8 June 2017, which entered into force on 3 January 2018; (ii) Lov om restrukturering og afvikling af visse finansielle virksomheder (Act on Recovery and Resolution of Credit Institutions), Act No. 333 of 31 March 2015, which entered into force on 1 June 2015; and (iii) Bekendtgørelse af lov om finansiel virksomhed (the Financial Business Act), Consolidation Act No. 1140 of 26 September 2017, which entered into force on 1 July 2007.
Estonia	<ul style="list-style-type: none"> (i) Pankrotiseadus (the Bankruptcy Act), which entered into force on 1 January 2004; (ii) Krediidiastutuste seadus (the Credit Institutions Act), which entered into force on 1 July 1999; and (iii) Kindlustustegevuse seadus (the Insurance Activities Act), which entered into force on 1 January 2016.
Finland	<ul style="list-style-type: none"> (i) Laki eräistä arvopaperi- ja valuuttakaupan sekä selvitysjärjestelmän ehdoista (Act on Certain Terms of Securities and Foreign Exchange Transactions and Settlements (1084/1999)), as amended and in force on 31 May 2018; and (ii) 4 §, 13 luku, Laki luottolaitosten ja sijoituspalveluyritysten kriisinratkaisusta (Section 4, Chapter 13 of the Act on Procedure for the Resolution of Credit Institutions and Investment Firms (1194/2014)), as amended and in force on 31 May 2018.
France	Articles L.211-36, L.211-36-I, L.211-40 et L.613-57-1, Code monétaire et financier (Articles L.211-36, L.211-36-1, L.211-40 and L.613-57-1 of the Monetary and Financial Code).
Georgia	Netting legislation is currently under consideration in Georgia, but has not yet been enacted.

Country	Status of netting legislation
Germany	(i) <i>Abschnitt 104 des Insolvenzordnung</i> (Section 104 of the Insolvency Code); and (ii) <i>Abschnitt 110 des Gesetz zur Sanierung und Abwicklung von Instituten und Finanzgruppen (Sanierungs- und Abwicklungsgesetz)</i> (Section 110 of the Act on Recovery and Resolution of Institutions and Financial Groups (Recovery and Resolution Act)).
Ghana	Netting legislation is currently under consideration in Ghana, but has not yet been enacted.
Greece	(i) <i>Άρθρο 16, Νόμος 3156/2003 Ομολογιακά Δανεια, Τιτλοποίηση Απαιτήσεων Και Απαιτήσεων Απο Ακίνητα Και Άλλες Διαταξεις</i> (Article 16 of Law 3156/2003 on bond loans); (ii) <i>Άρθρο 7, Νόμος 3301/2004 Συμφωνίες Παροχής Χρηματοοικονομικής Ασφαλείας Εφαρμογή Των Διεθνών Λογιστικών Προτύπων Και Άλλες Διαταξεις</i> (Article 7 of Law 3301/2004 on financial collateral arrangements); and (iii) <i>Άρθρο 76, Νόμος 4335/2015 Επείγοντα Μέτρα Εφαρμογής Του Ν. 4334/2015 (Α' 80)</i> (Article 76 of Law 4335/2015 on urgent measures for the implementation of Law 4334/2015 (80 A)).
Hong Kong	Close-out netting is enforceable in Hong Kong under general principles without the need for specific legislation. ⁸⁴
Hungary	(i) <i>2001. évi CXX. törvény a tőkepiacról</i> (Act CXX of 2001 on the Capital Markets), as amended and in force on 3 January 2018; (ii) <i>40(4) §, 1991. évi XLIX. Törvény a csődeljárásról és a felszámolási eljárásról</i> (Section 40(4) of Act XLIX of 1991 on Bankruptcy and Liquidation Proceedings), as amended and in force on 18 June 2018; and (iii) <i>2014. évi XXXVII. törvény a pénzügyi közvetítőrendszer egyes szereplőinek biztonságát erősítő intézményrendszer továbbfejlesztéséről</i> (Act XXXVII of 2014 on the improvement of the framework strengthening the resilience of certain institutions of the financial intermediary system), as amended and in force on 1 January 2018.
Iceland	<i>Lög um verðbréfavíðskipti 2007 nr. 108 26. Júní, 2 gr, V kafli, 39 gr – 41 gr</i> (Act on Securities Transactions No 108/2007 of 26 June 2007), Article 2 and Chapter V, Articles 39-41.
India	Close-out netting is enforceable in India under general principles without the need for specific legislation. ⁸⁵
Indonesia	Close-out netting is enforceable in Indonesia under general principles without the need for specific legislation. ⁸⁶ ISDA's netting opinion counsel acknowledges, however, that there is a relatively large degree of uncertainty with respect to the material content of the relevant legal rules, including their scope and enforceability.

⁸⁴ See n 78.

⁸⁵ See n 78.

⁸⁶ See n 78.

Country	Status of netting legislation
Ireland	<ul style="list-style-type: none"> (i) Netting of Financial Contracts Act 1995; (ii) Regulation 30 of the European Communities (Reorganisation and Winding-up of Credit Institutions) Regulations 2011; (iii) European Communities (Financial Collateral Arrangements) Regulations 2010; and (iv) Sections 45(5) and 104(1), Central Bank and Credit Institutions (Resolution) Act 2011.
Israel	<p>חוק ו-2006 "התשס"ו פיננסיים בנכסים הסכמים חוק (Financial Assets Agreements Law, 5766-2006), as amended and in force on 15 January 2018.</p>
Italy	<ul style="list-style-type: none"> (i) <i>Decreto Legislativo 24 febbraio 1998, n. 58</i> (Legislative Decree no. 58 of 24 February 1998), as amended and in force on 28 February 2018; (ii) <i>Decreto Legislativo 21 maggio 2004, n. 170</i> (Legislative Decree no. 170 of 21 May 2004), as amended and in force on 6 May 2011; (ii) <i>Regio Decreto 16 marzo 1942, n. 267</i> (Royal Decree no. 267 of 16 March 1942), as amended and in force on 17 June 2006; (iii) <i>Decreto Legislativo 1 settembre 1993, n. 385</i> (Legislative Decree no. 385 of 1 September 1993), as amended and in force on 13 January 2018; (iv) <i>Decreto Legislativo 16 novembre 2015, n. 180</i> (Legislative Decree no. 180 of 16 November 2015), as amended and in force on 9 March 2016; and (v) <i>Legge 4 agosto 2017, n. 124</i> (Law no. 124 of 4 August 2017), as amended and in force on 1 January 2018.
Jamaica	<p>Section 53(8) of the Insolvency Act, 2014.</p>
Japan	<ul style="list-style-type: none"> (i) <i>kin'yu kikan tou ga okonau tokutei kin'yu torihiki no ikkatsu seisan ni kansuru houritsu</i> (The Act on Collective Liquidation of Specified Financial Transactions conducted by Financial Institutions), Law No. 108 of 1998, which entered into force on 1 December 1998; and (ii) <i>hasan hou</i> (The Bankruptcy Act), Law No. 154 of 2002, which entered into force on 1 January 2002.
Latvia	<p>Netting legislation is currently under consideration in Latvia, but has not yet been enacted. Latvia has enacted the EU Financial Collateral Directive.⁸⁷</p>

⁸⁷ See n 17.

Country	Status of netting legislation
Liechtenstein	<ul style="list-style-type: none"> (i) <i>Artikel 33(4) des Gesetz über das Konkursverfahren (Konkursordnung)</i> (Article 33(4) of the Law on Insolvency), as amended and in force on 1 January 2017; (ii) <i>Artikel 392 und 398 des Sachenrecht</i> (Articles 392 and 398 of the Law on Property), as amended and in force on 1 January 2017; (iii) <i>Artikel 9b des Gesetz betreffend den Nachlassvertrag</i> (Article 9(b) of the Law on Composition Agreement), as amended and in force on 1 January 2017; (iv) <i>Artikel 16 des Gesetz über die Wirksamkeit von Abrechnungen in Zahlungs- sowie Wertpapierliefer- und -abrechnungssystemen (Finalitätsgesetz)</i> (Article 16 of the Law on the Effectiveness of Settlement in Payment and Securities Settlement Systems (Finality Act)), as amended and in force on 3 January 2018; and (v) <i>Gesetz zur Sanierung und Abwicklung von Banken und Wertpapierfirmen, SAG</i> (the Law on Recovery and Resolution of Banks and Investment firms), which entered into force on 1 January 2017.
Lithuania	<ul style="list-style-type: none"> (i) <i>Lietuvos Respublikos finansinio užtikrinimo susitarimų įstatymas Lietuvos Respublikos finansinio</i> (Law on Financial Collateral Arrangements of the Republic of Lithuania), No IX-2127 as amended and in force on 3 December 2015; and (ii) <i>91 ir 92 straipsniai, Lietuvos Respublikos finansinio tvarumo įstatymas</i> (Articles 91 and 92 of the Law on Financial Sustainability of the Republic of Lithuania), No XI-393, as amended and in force on 1 January 2016.
Luxembourg	<ul style="list-style-type: none"> (i) <i>Loi du 5 août 2005 sur les contrats de garantie financière</i> (Law of 5 August 2005 on financial collateral arrangements), Mémorial A n° 128 de 2005, which entered into force on 28 December 2015; (ii) <i>Art. 61-24, Loi du 5 avril 1993 relative au secteur financier</i> (Article 61-24, Law of 5 April 1993 on the financial sector), Mémorial A n° 27 de 1993; (iii) <i>Loi du 18 décembre 2015 relative aux mesures de résolution, d'assainissement et de liquidation des établissements de crédit et de certaines entreprises d'investissement ainsi qu'aux systèmes de garantie des dépôts et d'indemnisation des investisseurs</i> (Law of 18 December 2015 on the recovery, resolution and liquidation of credit institutions and certain investment firms, as well as deposit guarantee and investor compensation schemes), Mémorial A n° 246 de 2015.
Malaysia	Netting of Financial Arrangements Act 2015, which entered into force on 30 March 2015.

Country	Status of netting legislation
Malta	(i) <i>Att dwar Tpaċija u Netting f'każ ta' Insolvenza</i> (the Set-off and Netting on Insolvency Act, Chapter 459), which entered into force on 1 June 2003; (ii) <i>Regolamenti dwar Istituzzjonijiet ta' Kreditu (Organizzazzjoni mill-Ġdid u Stralċ) - Att dwar il-Kummerċ Bankarju</i> (Credit Institutions (Reorganisation and Winding Up) Regulations - the Banking Act), Chapter 371.12, which entered into force on 1 May 2004; and (iii) <i>Regolamenti dwar Ditti ta' Investment (Organizzazzjoni mill-Ġdid u Stralċ) - Att dwar Servizzi ta' Investment</i> (Investment Firms (Reorganisation and Winding Up) Regulations - the Investment Services Act), Chapter 370.30, which entered into force on 18 September 2015.
Marshall Islands	Close-out netting is enforceable in the Marshall Islands under general principles without the need for specific legislation. ⁸⁸
Mauritius	Part V of the Insolvency Act 2009, which entered into force on 1 June 2009.
Mexico	(i) Artículo 176 de Ley de Instituciones de Credito (Article 176 of the Banking Law), which entered into force on 18 July 1990; and (ii) Artículos 102, 104 y 105 de Ley de Concursos Mercantiles (Articles 102, 104 and 105 of the Commercial Insolvency Law), which entered into force on 12 May 2000.
Morocco	Netting legislation is currently under consideration in Morocco, but has not yet been enacted.
Netherlands	Close-out netting is enforceable in the Netherlands under general principles without the need for specific legislation. ⁸⁹
Netherlands – Aruba, Curaçao, St Maarten	Close-out netting is enforceable in the Netherlands territories of Aruba, Curaçao and Sint Maarten under general principles without the need for specific legislation. ⁹⁰
New Zealand	(i) Companies Amendment Act 1999, No 19, which entered into force on 26 April 1999; (ii) Corporations (Investigation and Management) Amendment Act 1999, No 20, which entered into force on 26 April 1999; (iii) Reserve Bank of New Zealand Amendment Act 1999, No 22, which entered into force on 26 April 1999; and (iv) Companies Amendment Act 2006, No 56, which entered into force on 7 November 2006.

⁸⁸ See n 78.

⁸⁹ See n 78.

⁹⁰ See n 78.

Country	Status of netting legislation
Norway	(i) <i>Lov om verdipapirhandel (verdipapirhandelloven)</i> (the Securities Trading Act), 29 June 2007 No 75, which entered into force on 1 November 2007; and (ii) <i>Lov om finansiell sikkerhetsstillelse</i> (the Financial Collateral Arrangements Act) 26 March 2004 No 17, which entered into force on 1 July 2004.
Pakistan	Netting legislation is currently under consideration in Pakistan, but has not yet been enacted.
Panama	Netting legislation is currently under consideration in Panama, but has not yet been enacted.
Peru	<i>Artículo 116 de Ley General del Sistema Financiero y Sistema de Seguros y Orgánica de la Superintendencia de Banca y Seguros</i> , (Article 116 of the Banking Law), Law 26702.
Philippines	Close-out netting is enforceable in the Philippines under general principles without the need for specific legislation. ⁹¹ Netting opinion counsel notes, however, that relevant provisions of the Civil Code may affect the range of transactions capable of being safely conducted with Philippines counterparties if entered into with the intention of cash-settling or if not entered into for hedging or other legitimate business purposes.
Poland	(i) <i>Ustawa z dnia 28 lutego 2003 r.- Prawo upadłościowe</i> (Act of 28 February 2003 - Bankruptcy Law), J.L. 2016, item 2171, which entered into force on 1 October 2003; (ii) <i>Ustawa z dnia 15 maja 2015 r. - Prawo restrukturyzacyjne</i> (Act of 15 May 2015 - Restructuring Law), J.L. 2016, item 1574, which entered into force on 1 January 2016; and (iii) <i>Ustawa z dnia 10 czerwca 2016 r. o Bankowym Funduszu Gwarancyjnym, systemie gwarantowania depozytów oraz przymusowej restrukturyzacji</i> (Act of 10 June 2016 on the Banking Guarantee Fund, deposits guarantee scheme and compulsory restructuring), J.L. 2016, item 996, which entered into force on 9 October 2016.
Portugal	(i) <i>Decreto-Lei n.º 70/97 de 3 de Abril 1997</i> (Decree Law no. 70/97 of 3 April, 1997), Diário da República n.º 78/1997, Série I-A de 1997-04-03; (ii) <i>Decreto-Lei n.º 298/92 de 31 de Dezembro 1992, Regime Geral das Instituições de Crédito e Sociedades Financeiras</i> (Decree Law no. 298/92 of 31 December, 1992, General Regime of Credit Institutions and Financial Companies), Diário da República n.º 301/1992, 6º Suplemento, Série I-A de 1992-12-31; (iii) <i>Decreto-Lei n.º 53/2004 de 18 de Março 2004, Código da Insolvência e da Recuperação de Empresas</i> (Decree Law no. 53/2004 of 18 March, 2004, Insolvency and Business Recovery Code), Diário da República n.º 66/2004, Série I-A de 2004-03-18; and (iv) <i>Decreto-Lei n.º 157/2014 de 24 de Outubro 2014</i> (Decree Law no. 157/2014 of 24 October, 2014), Diário da República n.º 206/2014, Série I de 2014-10-24.

⁹¹ See n 78.

Country	Status of netting legislation
Qatar	Netting legislation in Qatar is limited to the Qatar Financial Centre regime. The relevant legislation in this regard is the Qatar Financial Centre Netting Regulations, Regulation No 20 of 2017.
Romania	<p>(i) <i>Lege nr. 85 din 25 iunie 2014 privind procedurile de prevenire a insolvenței și de insolvență</i> (Law no. 85 of 25 June 2014 on pre-insolvency and insolvency proceedings); and</p> <p>(ii) <i>Lege nr. 312 din 4 decembrie 2015 privind redresarea și rezoluția instituțiilor de credit și a firmelor de investiții, precum și pentru modificarea și completarea unor acte normative în domeniul financiar</i> (Law no. 312 of 4 December 2015 on the recovery and resolution of credit institutions and investment firms).</p>
Russia	<i>Статья 4.1 от Федерального закон О несостоятельности (банкротстве)</i> (Article 4.1 of the Federal Law On Insolvency (Bankruptcy), No. 127-FZ, dated 26 October 2002).
San Marino	<i>Decreto Delegato 31 Agosto 2018 N.113 (Disposizioni in Materia di Contratti di Garanzia Finanziaria in Recepimento della Direttiva 2002/47/CE).</i>
Saudi Arabia	Netting legislation is currently under consideration in Saudi Arabia, but has not yet been enacted.
Serbia	Netting legislation is not yet in force in Serbia, but will enter into force on 1 January 2019. The relevant legislation is: <i>Zakon o finansijskom obezbeđenju</i> (the Financial Collateral Act).
Seychelles	Netting legislation is currently under consideration in the Seychelles, but has not yet been enacted.
Singapore	Close-out netting is enforceable in Singapore under general principles without the need for specific legislation. ⁹²
Slovakia	<p>(i) <i>Zákon o konkurze a reštrukturalizácii a o zmene a doplnení niektorých zákonov</i> (Act on bankruptcy and restructuring), Act No. 7/2005 Coll., as amended and in force on 30 September 2015; and</p> <p>(ii) <i>Zákon o riešení krízových situácií na finančnom trhu a o zmene a doplnení niektorých zákonov</i> (Act on resolution of crisis situations in financial markets), Act No. 371/2014 Coll., as amended and in force on 14 October 2015.</p>

⁹² See n 78.

Country	Status of netting legislation
Slovenia	<ul style="list-style-type: none"> (i) <i>Zakon o finančnem poslovanju, postopkih zaradi insolventnosti in prisilnem prenehanju</i> (the Financial Operations, Insolvency Proceedings and Compulsory Dissolution Act), Official Gazette of the Republic of Slovenia, No. 126/2007; (ii) <i>Zakon o reševanju in prisilnem prenehanju bank</i> (the Resolution and Compulsory Dissolution of Credit Institutions Act), Official Gazette of the Republic of Slovenia, No. 44/2016; and (iii) <i>Zakon o bančništvu</i> (the Banking Act), Official Gazette of the Republic of Slovenia, No. 25/2015.
South Africa	<ul style="list-style-type: none"> (i) Sections 35B and 46 of the Insolvency Act, 1936, which entered into force on 31 March 2005; and (ii) Section 69(6)(b) of the Banks Act, 1990, which entered into force on 1 November 1996.
South Korea	<ul style="list-style-type: none"> (i) Article 120, Paragraph 3 and Article 336 of the Debtor Rehabilitation and Bankruptcy Law, which entered into force on 1 April 2006; (ii) The Corporate Restructuring Promotion Law, which entered into force on 18 March 2016; and (iii) Ruling of the Financial Services Commission of Korea on the scope of financial claims under the Corporate Restructuring Promotion Law.
Spain	<ul style="list-style-type: none"> (i) <i>Capítulo II, Real Decreto-ley 5/2005, de 11 de marzo, de reformas urgentes para el impulso a la productividad y para la mejora de la contratación pública</i> (Chapter II, Royal Decree Law 5/2005, of 11 March on urgent reforms to boost productivity and improve public procurement), which entered into force on 15 March 2005; (ii) <i>Ley 6/2005, de 22 de abril, sobre saneamiento y liquidación de las entidades de crédito</i> (Law 6/2005, of 22 April on the reorganization and liquidation of credit institutions), which entered into force on 24 April 2005; and (iii) <i>Ley 11/2015, de 18 de junio, de recuperación y resolución de entidades de crédito y empresas de servicios de inversión</i> (Law 11/2015, of 18 June on the recovery and resolution of credit institutions and investment service companies), which entered into force on 20 June 2015.
Sweden	<ul style="list-style-type: none"> (i) <i>Avsnitt 5(1), Sw: Lag 1991:980 om handel med finansiella instrument</i> (Section 5(1) of the Financial Instruments Trading Act); and (ii) <i>Sw: Lag 2015:106 om resolution</i> (the Resolution Act).
Switzerland	<ul style="list-style-type: none"> (i) <i>Artikel 211 para 2bis des Bundesgesetz über Schuldbetreibung und Konkurs (SchKG) / Loi fédérale sur la poursuite pour dettes et la faillite (LP)</i> (Article 211 para 2^{bis} of the Swiss Federal Act on Debt Enforcement and Bankruptcy), SR 281.1, as amended and in force on 3 October 2003. (ii) <i>Artikel 27 para 1 des Bundesgesetz über die Banken und Sparkassen (BankG) / Loi fédérale sur les banques et les caisses d'épargne (LB)</i> (Article 27 para 1 of the Swiss

Country	Status of netting legislation
	Federal Act on Banks and Savings Banks), SR 952.0, as amended and in force on 22 April 1999.
Taiwan	Close-out netting is enforceable in Taiwan under general principles without the need for specific legislation. ⁹³
Thailand	Close-out netting is enforceable in Thailand under general principles without the need for specific legislation. ⁹⁴
Trinidad and Tobago	Section 49 of the Bankruptcy and Insolvency Act, Chap. 9:70.
Turkey	Close-out netting is enforceable in Turkey under general principles without the need for specific legislation. ⁹⁵
Ukraine	Netting legislation is currently under consideration in the Ukraine, but has not yet been enacted.
United Arab Emirates	<p>Netting legislation in the UAE is limited to the Dubai International Financial Centre (DIFC) and Abu Dhabi Global Market (ADGM) regimes:</p> <ul style="list-style-type: none"> (i) In relation to the ADGM: Part 7 (Financial Markets and Netting) of the ADGM Insolvency Regulations 2015; and (ii) in relation to the DIFC: <ul style="list-style-type: none"> (a) Netting Law, DIFC Law No 2 of 2014; and (b) Regulation 5.25 of the DIFC Insolvency Regulations 2009. <p>Netting legislation is currently under consideration at the federal level in the UAE, but has not yet been enacted.</p>
United Kingdom	<p>The UK is comprised of three separate legal jurisdictions, namely: (1) England and Wales, which form a single legal jurisdiction, (2) Scotland and (3) Northern Ireland. Close-out netting works on the basis of general principles in each of these three jurisdictions, subject only to the need for netting legislation to safeguard against the disruption of close-out netting by use of the partial property transfer power in case of the resolution of a bank or building society. The Banking Act 2009, under which the power of the resolution authority to make a partial property transfer order arises, applies separately to each of England and Wales, Scotland and Northern Ireland. The netting legislation is the Banking Act 2009 (Restriction of Partial Property Transfers) Order 2009 SI 2009/322.⁹⁶</p>

⁹³ See n 78.

⁹⁴ See n 78.

⁹⁵ See n 78.

⁹⁶ See n 78.

Country	Status of netting legislation
United States of America	<p>The USA (excluding its territories, such as Puerto Rico) is comprised of fifty-two legal jurisdictions, namely, each of the fifty US states, the District of Columbia and the federal jurisdiction, which applies throughout the USA. In relation to most corporate and bank counterparties,⁹⁷ bankruptcy (insolvency) is primarily governed by federal law. Netting legislation is therefore primarily federal legislation, the principal legislation being:</p> <ul style="list-style-type: none"> (i) United States Bankruptcy Code, 11 U.S.C. §101 et seq.; (ii) Federal Deposit Insurance Act, 12 U.S.C. §1811 et seq.; (iii) Orderly Liquidation Authority Statute, 12 U.S.C. § 5381 et seq.; (iv) Federal Deposit Insurance Corporation Improvement Act of 1991; and (v) Financial Netting Improvements Act of 2006. <p>In addition, in relation certain entities and proceedings in New York, the following New York netting legislation is relevant: New York Banking Law, N.Y. Banking Law §1 et seq.</p>
Zambia	The enforceability of close-out netting against a corporate entity is protected by relevant provisions of the Corporate Insolvency Act (Act No 41 of 2016).
Zimbabwe	Sections 35-36 of the Insolvency Act, 2018 (Cap. 6:07, No. 7/2018).

⁹⁷ But, notably, not US insurance companies.

**DIFFERENCES BETWEEN THE 2018 AND 2006 VERSIONS OF
THE MODEL NETTING ACT**

A number of changes have been made to the text of the 2018 MNA relative to the 2006 version of the Model Netting Act (the “2006 MNA”) to update and clarify the drafting. We summarise below only substantive differences between the 2018 and the 2006 versions. The reasons for the substantive changes are set out elsewhere in this Guide.

For the purpose of interpreting any existing legislation that is based in whole or in part on the 1997, 2002 or 2006 version of the Model Netting Act, no inference should be drawn from the fact that any difference between the text of the 2018 MNA and the text of any prior version of the Model Netting Act. Each version is a self-standing model set of provisions.

The substantive differences between the 2018 MNA and the 2006 MNA are as follows:

Part I: Netting

1. Section 1 (Definitions):
 - (a) The definition of “Bank” in the 2006 MNA has been amended to “Authority”.
 - (b) The definition of “liquidator” in the 2006 MNA has been amended to “insolvency practitioner”.
 - (c) A definition of “insolvency proceedings” has been added.
 - (d) The definition of “qualified financial contract” in the 2006 MNA has been amended to add a reference in sub-clause (l) to “physical transmission rights, etc.” and to add an additional sub-clause (designated “(z)” with the former sub-clause (z) re-designated as “(aa)”) referring to Shari’a compliant transactions.
 - (e) A definition of “resolution proceedings” has been added.
2. Section 3 (Enforceability of a Qualified Financial Contract):
 - (a) A new sub-clause (b) has been added (and the original text designated “(a)”) to address an issue relating to a qualified financial contract that is considered Shari’a compliant at inception, but where a party seeks to rely on a change of interpretation of relevant Shari’a rules or principles in order to repudiate the contract.
3. Section 4 (Enforceability of a Netting Agreement):
 - (a) A new sub-clause (j) has been added to address the case where the insolvent party is a financial institution subject to resolution proceedings (whether due to its insolvency or any other reason for resolution under the relevant legislation providing for resolution).

Optional Part II: Multibranch Netting

No substantive changes have been made, but more extensive changes have been made to clarify the drafting than is the case in relation to Part I. This was based on feedback received in relation to the 2006 MNA.

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