HENGELER MUELLER

MEMORANDUM OF LAW
FOR THE
INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC.

Collateral Provider Insolvency -
The Validity and Enforcement of Collateral Arrangements
Under the ISDA Credit Support Documents
in German Law

September 1, 2017

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A.
INTRODUCTION

You have requested this Memorandum of Law with respect to the validity and enforceability under the laws of the Federal Republic of Germany ("**Germany**") of margin or collateral arrangements entered into in connection with one of the master agreements (each, a "**Master Agreement**")[1] published by the International Swaps and Derivatives Association, Inc. ("**ISDA**") under one of the following documents published by ISDA:

(i) the 1994 Credit Support Annex governed by the laws of the State of New York ("**New York law**") (the "**1994 NY Annex**");

(ii) the 2016 Credit Support Annex for Variation Margin (VM) governed by New York law (the "**VM NY Annex**") and the Amendments for Independent Amounts to be included in Paragraph 13 of the New York law 2016 Credit Support Annex for Variation Margin (VM) (the "**VM NY Annex IA Amendments**");

(iii) the 2016 Phase One Credit Support Annex for Initial Margin (IM) governed by New York law (the "**IM NY Annex**") and the Recommended Amendment Provisions for the ISDA New York Law 2016 Phase One Credit Support Annex for Initial Margin (IM) with respect to Japanese Securities (the "**IM NY Annex Japanese Amendments**");

(iv) the 1995 Credit Support Deed governed by the laws of England and Wales ("**English law**") (the "**1995 Deed**");

(v) the 2016 Phase One IM Credit Support Deed governed by English law (the "**IM Deed**") and the Recommended Amendment Provisions for the ISDA English Law 2016 Phase One Credit Support Deed for Initial Margin (IM) with respect to Japanese Securities (the "**IM Deed Japanese Amendments**");

(vi) the 1995 Credit Support Annex governed by English law (the "**1995 Transfer Annex**");

(vii) the 2016 VM Credit Support Annex governed by English law (the "**VM Transfer Annex**") and the Amendments for Independent Amounts to be included in Paragraph 11 of the English law 2016 Credit Support Annex for Variation Margin (VM) (the "**VM Transfer Annex IA Amendments**");

(viii) the ISDA Euroclear Security Agreement (the "**Euroclear Security Agreement**") and the Recommended Amendment Provisions for the Euroclear Security Agreement with respect to Japanese Collateral (the "**Euroclear Security Agreement Japanese Amendments**");

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[1] The master agreements published by ISDA include (i) the 1987 Interest Rate Swap Agreement, (ii) the 1987 Interest Rate and Currency Exchange Agreement, (iii) the 1992 Master Agreement (Multicurrency - Cross Border), (iv) the 1992 Master Agreement (Local Currency - Single Jurisdiction) and (v) the 2002 ISDA Master Agreement.

(ix) the ISDA Euroclear Collateral Transfer Agreement (NY Law) (the "**Euroclear NY CTA**") and the Recommended Amendment Provisions for the Euroclear Collateral Transfer Agreements with respect to Japanese Collateral (the "**Euroclear CTA Japanese Amendments**"; and together with the Euroclear Security Agreement Japanese Amendments, the "**Euroclear Japanese Amendments**");

(x) the ISDA Euroclear Collateral Transfer Agreement (Multi-Regime) (the "**Euroclear Multi-Regime CTA**") and the Euroclear CTA Japanese Amendments;

(xi) the ISDA Clearstream 2016 Security Agreement (the "**Clearstream Security Agreement**") and the Novation Agreement (the "**Clearstream Security Agreements Japanese Amendments**");

(xii) the ISDA Clearstream 2016 Collateral Transfer Agreement (NY Law) (the "**Clearstream NY CTA**") and the CBL Services Novation Agreement (the "**Clearstream CTA Japanese Amendments**"; and together with the Clearstream Security Agreement Japanese Amendments, the "**Clearstream Japanese Amendments**"); or

(xiii) the ISDA Clearstream 2016 Collateral Transfer Agreement (Multi-Regime) (the "**Clearstream Multi-Regime CTA**").

For the purposes of this letter:

(1) "**Annex**" means each of the 1994 NY Annex, the VM NY Annex and the IM NY Annex;

(2) "**Deed**" means each of the 1995 Deed and the IM Deed;

(3) "**Security Documents**" means the Annexes and the Deeds and, for purposes of question F.II.C below, securities documents and other agreements described in the assumption set out under F.I.(m);

(4) "**IM Security Documents**" means the IM NY Annex and the IM Deed and, for purposes of question F.II.C below, securities documents and other agreements described in the assumption set out under F.I.(m);

(5) "**Non-IM Security Documents**" means the 1994 NY Annex, the VM NY Annex and the 1995 Deed;

(6) "**Transfer Annex**" means each of the 1995 Transfer Annex and the VM Transfer Annex;

(7) "**Credit Support Documents**" means the Security Documents and the Transfer Annexes;

(8) "**Euroclear Documents**" means the Euroclear Security Agreement, the Euroclear NY CTA and the Euroclear Multi-Regime CTA; and

(9) "**Clearstream Documents**" means the Clearstream Security Agreement, the Clearstream NY CTA and the Clearstream Multi-Regime CTA.

Capitalized terms used, but not defined, herein have the meanings ascribed to them in the relevant Master Agreement or relevant Credit Support Document, as applicable.

In this Memorandum:

(a) in relation to the Security Documents, the term "**Security Collateral Provider**" refers to the Pledgor (under an Annex) or the Chargor (under a Deed), as the case may be;

(b) "**Collateral Provider**" means the Security Collateral Provider (under a Security Document) or the Transferor (under a Transfer Annex), as the case may be;

(c) "**Collateral Taker**" means the Secured Party (under a Security Document) or the Transferee (under a Transfer Annex), as the case may be; and

(d) "**Collateral**" refers (i) in the case of each Security Document to any assets in which a security interest is created by the Security Collateral Provider in favor of the Secured Party and (ii) in the case of each Transfer Annex to any securities transferred as credit support or cash deposited, in either case, by the Transferor to or with the Transferee, as credit support for the obligations of the Collateral Provider under the relevant Master Agreement.

This Memorandum supersedes and replaces our memorandum of law relating to the validity and enforcement of collateral arrangements under the ISDA Credit Support Documents in German law dated December 30, 2014.

This Memorandum and all conclusions expressed herein relate solely to matters of German law as in force at the date hereof and do not consider, except as expressly stated, the impact of any laws (including insolvency laws and conflict of laws rules) other than German law, even in the case where, under German law, any foreign law falls to be applied. Any description of, or other reference to, a legal position under any foreign law is based on information which we have received from you and which has not been verified by us. The accuracy of such information is assumed by us as a matter of fact. It is further assumed by us that all words and expressions in the Credit Support Documents are to be understood in accordance with their plain meaning and without regard of any import which they may have under New York or English law, as the case may be.

This Memorandum is directed to you solely for the benefit of your members. The purpose of this Memorandum is to provide an aid to your members in understanding generally issues which may be relevant from the viewpoint of German law when any of them want to enter into Credit Support Documents. We wish to emphasize, though, with your explicit approval, that the purpose of this Memorandum is not to provide a basis on which any of your members or any other person can rely with respect to, or in connection with, any transaction or act which any of them may undertake or omit to undertake. Accordingly, we assume no responsibility to any person in the context of this Memorandum.

This Memorandum constitutes a legal opinion for regulatory purposes and may be made available to the appropriate regulatory authorities. This Memorandum may also be made available to professional advisors of your members.

The specific questions which we have been asked to address and our answers thereto are set out under F.II and G.II below. Our analysis and conclusions presented in these answers are subject to the description of legal positions and the qualifications expressed in other parts of this Memorandum.

B.
COLLATERAL ARRANGEMENTS COVERED

1. Subject to B.2 below, this Memorandum considers the validity and enforceability of the Credit Support Documents in circumstances where the collateral arrangement entered into under a Credit Support Document qualifies as a financial collateral arrangement (*Finanzsicherheit* – "**Financial Collateral Arrangement**") within the meaning of § 1(17) of the German Banking Act (*Gesetz über das Kreditwesen* – the "**Banking Act**"). This provision has been included in the Banking Act in connection with the transformation into German law of Directive 2002/47/EC of the European Parliament and of the Council of June 6, 2002 on financial collateral arrangements[2], as amended (the "**EC Collateral Directive**"). A collateral arrangement entered into under a Credit Support Document qualifies as a Financial Collateral Arrangement if the requirements set out under (a) and (b) below are met:

   (a) The assets subject to a collateral arrangement are within one of the following categories set out in § 1(17), 1st sentence, of the Banking Act:

      (1) cash credited to a bank account ("**Cash**");

      (2) securities which term includes all types of transferable securities, with the exception of instruments of payment, including, in particular, (i) shares and other securities comparable to shares in companies, partnerships or other entities, and depositary receipts in respect of shares, (ii) debt instruments, in particular profit participating certificates, bearer bonds, registered bonds and certificates representing such debt instruments, (iii) any other securities giving the right to acquire or sell any securities specified under (i) and (ii) above or giving rise to a cash settlement determined by reference to securities, currencies, interest rates or other yields, commodities, indices or indicators and (iv) units in an investment fund (*Investmentvermögen*) within the meaning of § 1(1) of the Capital Investment Code (*Kapitalanlagegesetzbuch* – "**Capital Investment Code**");[3]

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2 Official Journal no. L 168 of June 27, 2002, pp. 43 *et seq*.

3 The definition of the term "securities" (*Wertpapiere*) as used in § 1(17), 1st sentence, of the Banking Act which was previously contained in the Banking Act has been deleted as of July 22, 2013. It seems to follow, however, from the definition of "financial instruments" (*Finanzinstrumente*) in § 1(11), 1st sentence, of the Banking Act that the above items should fall under such term. There is no available legal authority on this issue.

(3) money market instruments within the meaning of § 1(11), 2nd sentence, of the Banking Act ("**Money Market Instruments**");

The term "Money Market Instruments" comprises all types of claims that (i) are not securities as set out under (2) above, (ii) are customarily traded on the money market and (iii) are not instruments of payment; or

(4) credit claims, *i.e.*, pecuniary claims arising out of an agreement whereby a credit institution, as defined under B.1.(b)(i)(1) below, or an insurance company (*Versicherungsunternehmen*) within the meaning of § 7 no. 33 of the German Insurance Supervisory Act (*Gesetz über die Beaufsichtigung von Versicherungsunternehmen* - "**Insurance Supervisory Act**") grants credit in the form of a loan;

in each case including all rights and claims relating to such assets and in all cases irrespective of whether provided under a (i) security financial collateral arrangement ("**Security Financial Collateral Arrangement**")[4], (ii) a title transfer financial collateral arrangement ("**Title Transfer Financial Collateral Arrangement**") or (iii) in the case of Cash only, by way of payment of money from one account to another.[5]

(b) Each of the Collateral Provider and the Collateral Taker is either individually designated below or is within one of the following categories, provided that, where the Collateral Provider is not incorporated or organized in a Member State of the European Community ("**EC Member State**"), the Collateral Provider pursuant to § 1(17), 4th sentence, of the Banking Act must be substantially equivalent to any of the entities either designated below or falling within one of the categories set out below:[6]

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4 This term is not defined in § 1(17) of the Banking Act, but in Article 2(1)(c) of the EC Collateral Directive. According to this provision, the term "Security Financial Collateral Arrangement" means an arrangement under which a collateral provider provides financial collateral by way of security in favor of, or to, a collateral taker, and where the full ownership of the financial collateral remains with the collateral provider when the security right is established. *See* E.II.(D)(1) below.

5 Pursuant to Article 2(1)(b) of the EC Collateral Directive, the term "Title Transfer Financial Collateral Arrangement" means an arrangement, including repurchase agreements, under which a collateral provider transfers full ownership of financial collateral to a collateral taker for the purpose of securing or otherwise covering the performance of relevant financial obligations. *See* E.II.(D)(2) below.

6 We note that the persons and entities listed in Article 1(2) of the EC Collateral Directive as falling within the scope of application of the Directive are not limited to persons and entities established in an EC Member State (*cf.*, for example, letters (a) and (b) of said provision which expressly include entities not established in EC Member States). Apparently, the German legislature, when implementing the EC Collateral Directive, took a different view. It is, therefore, unclear whether the requirement set out in § 1(17), 5th sentence, of the Banking Act narrows the scope of application of the rules applicable to Financial Collateral Arrangements under German law as far as persons and entities are concerned which are not established in an EC Member State.

(i) financial institutions subject to prudential supervision, including:

(1) credit institutions, which means,

(A) in accordance with Article 4(1) No. 1 of the Regulation 575/2013/EC of the European Parliament and of the Council of June 26, 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012[7], as amended (the "**Banking Regulation**"), undertakings whose business is to take deposits or other repayable funds from the public and to grant credits for their own account; and

(B) each of the entities organized in EC Member States which are listed in Article 2(5) points (3) to (23) of the Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2206/49/EC, as amended;[8]

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7 Official Journal no. L 176 of June 27, 2013, pp. 1 et seq.

8 Official Journal no. L 176 of June 27, 2013, pp. 338 et seq. These entities comprise (i) post office giro institutions, (ii) with respect to *Austria*, undertakings recognized as housing associations in the public interest and the "Oesterreichische Kontrollbank AG", (iii) with respect to *Belgium*, the "Institut de Réescompte et de Garantie/Herdiscontering- en Waarborginstituut", (iv) with respect to Denmark, the " Eksport Kredit Fonden A/S", the "Danmarks Skibskredit A/S" and the "KommuneKredit", (v) with respect to *Estonia*, the "hoiu-laenuühistud", as cooperative undertakings that are recognised under the "hoiu-laenuühistu seadus", (vi) with respect to Finland, the "Teollisen yhteistyön rahasto Oy/Fonden för industriellt samarbete AB", and the "Finnvera Oyj/Finnvera Abp", (vii) with respect to *France*, the "Caisse des dépôts et consignations", (viii) with respect to *Germany*, the "Kreditanstalt für Wiederaufbau", undertakings which are recognized under the *Wohnungsgemeinnützigkeitsgesetz* as bodies of State housing policy and are not mainly engaged in banking transactions and undertakings recognised under that law as non-profit housing undertakings, (ix) with respect to Greece, the "Tamio Parakatathikon kai Danion", (x) with respect to *Hungary*, the "MFB Magyar Fejlesztési Bank Zártkörűen Működő Részvénytársaság" and the "Magyar Export-Import Bank Zártkörűen Működő Részvénytársaság", (xi) with respect to *Ireland*, credit unions and the friendly societies, (xii) with respect to *Italy*, the "Cassa depositi e prestiti", (xiii) with respect to *Latvia*, the "krājaizdevu sabiedrības", undertakings that are recognized under the "krājaizdevu sabiedrību likums" as cooperative undertakings rendering financial services solely to their members, (xiv) with respect to *Lithuania*, the "kredito unijos" other than the "Centrinė kredito unija", (xv) with respect to the *Netherlands*, the "Netherlandse Investeringsbank voor Ontwikkelingslanden NV", the "NV Noordelijke Ontwikkelingsmaatschappij", the "NV Industriebank Limburgs Instituut voor Ontwikkeling en Financiering" and the "Overijsselse Ontwikkelingsmaatschappij NV", (xvi) with respect to *Poland*, the "Spółdzielcze Kasy Oszczędnościowo - Kreditowe" and the "Bank Gospodarstwa Krajowego", (xvii) with respect to *Portugal*, "Caixas Económicas" existing on January 1, 1986 with the exception of those incorporated as limited companies and of the "Caixa Económica Montepio Geral", (xviii) with respect to Slovenia the „SID-Slovenska izvozna in razvojna banka, d.d. Ljubljana“, (xix) with respect to *Spain*, the "Instituto de Crédito Oficial", (xx) with respect to *Sweden*, the "Svenska Skeppshypotekskassan", and (xxi) with respect to the *United Kingdom*, the "National Savings Bank", the "Commonwealth Development Finance Company Ltd", the "Agricultural Mortgage Corporation Ltd", the "Scottish Agricultural Securities Corporation Ltd", the Crown Agents for overseas governments and administrations, credit unions and municipal banks.

(2) investment firms;[9]

(3) financial institutions;[10]

(4) insurance undertakings;[11]

(5) undertakings for collective investment in transferable securities ("**UCITS**");[12]

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9 Article 4(1) no. 1 of the Directive 2004/39/EC of the European Parliament and of the Council of April 21, 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (Official Journal no. L 145 of April 30, 2004, pp. 1 et seq.), as amended, defines an "investment firm" as any legal person whose regular occupation or business is the provision of one or more investment services to third parties and/or the performance of one or more investment activities on a professional basis. Pursuant to this provision, EC Member States may also include as investment firms undertakings which are not legal persons if (i) their legal status ensures a level of protection for third parties' interests equivalent to that afforded by legal persons, (ii) they are subject to equivalent prudential supervision appropriate to their legal form and (iii) certain further requirements set out therein are fulfilled.

10 Pursuant to Article 4(1) No. 26 of the Banking Regulation, a "financial institution" is an undertaking other than an institution, the principal activity of which is to acquire holdings or to carry on one or more of the following activities: (i) lending (including, inter alia, consumer credit, mortgage credit, factoring, with or without recourse, financing of commercial transactions (including forfeiting), (ii) financial leasing, (iii) payment services as defined in Article 4(3) of Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market, (iv) issuing and administering means of payment (e.g., credit cards, travellers' cheques and bankers' drafts) insofar as this activity is not covered by item (iv), (v) guarantees and commitments, (vi) trading for own account or for account of customers in (a) money market instruments (cheques, bills, certificates of deposit, etc.); (b) foreign exchange; (c) financial futures and options; (d) exchange and interest-rate instruments or (e) transferable securities, (vii) participation in securities issues and the provision of services related to such issues, (viii) advice to undertakings on capital structure, industrial strategy and related questions and advice as well as services relating to mergers and the purchase of undertakings, (ix) money broking, (x) portfolio management and advice, (xi) safekeeping and administration of securities and (xii) issuing electronic money.

11 Pursuant to Article 13(1) of the Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast) (Official Journal no. L 335 of December 17, 2009, pp. 1 et seq.), as amended, "insurance undertaking" means a direct life or non-life insurance undertaking which has received authorisation in accordance with Article 14 of this Directive .

12 "UCITS" means, pursuant to Article 1(2) of the Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (recast), as amended ("**UCITS Directive**"), undertakings (i) the sole object of which is the collective investment in transferable securities or in other liquid financial assets referred to in Article 50(1) of the UCITS Directive of capital raised from the public and which operate on the principle of risk-spreading, and (ii) the units of which are, at the request of holders, re-purchased or redeemed, directly or indirectly, out of those undertakings' assets. Pursuant to Article 3 of the UCITS Directive, the following undertakings are not considered as UCITS within the meaning of the Directive: (i) collective investment undertakings of the closed-ended type; (ii) collective investment undertakings which raise capital without promoting the sale of their units to the

(6) management companies;[13]

(ii) central counterparties;[14]

(iii) settlement agents;[15]

(iv) clearing houses;[16]

(v) persons, other than natural persons, who act in a trust or representative capacity on behalf of:

(1) any one or more persons that includes any bondholders or holders of other forms of securitized debt; or

(2) any institution as defined in items (i) to (iv) and (vi) to (viii);

(vi) central banks;

(vii) certain supranational banks or entities;[17]

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public within the EC or any part of it; (iii) collective investment undertakings the units of which, under the fund rules or the investment company's instruments of incorporation, may be sold only to the public in non-EC Member States; and (iv) categories of collective investment undertakings prescribed by the regulations of EC Member States in which such collective investment undertakings are established, for which the rules laid down in Chapter VII and Article 83 of the UCITS Directive are inappropriate in view of their investment and borrowing policies.

13 A "management company" is, according to Article 2(1)(b) of the UCITS Directive, any company, the regular business of which is the management of UCITS in the form of common funds or of investment companies (collective portfolio management of UCITS).

14 "Central counterparty" means, in accordance with Article 2(c) of the Directive 98/26/EC of the European Parliament and of the Council of May 19, 1998 on settlement finality in payment and securities settlement systems (Official Journal no. L 166 of June 11, 1998, pp. 45 *et seq*.), as amended, ("**Finality Directive**") an entity which is interposed between the institutions in a system and which acts as the exclusive counterparty of these institutions with regard to their transfer orders.

15 Pursuant to Article 2(d) of the Finality Directive, "settlement agent" means an entity providing to institutions and/or a central counterparty participating in systems, settlement accounts through which transfer orders within such systems are settled and, as the case may be, extending credit to those institutions and/or central counterparties for settlement purposes.

16 Article 2(e) of the Finality Directive defines a "clearing house" as an entity responsible for the calculation of the net positions of institutions, a possible central counterparty and/or a possible settlement agent.

17 These supranational banks or entities are the European Central Bank, the Bank for International Settlements, the International Monetary Fund, the European Investment Bank and multilateral development banks. The term "multilateral development banks" is defined in the EC Collateral Directive by reference to the Banking Regulation. Those banks are pursuant to Article 117: (i) the Asian Development Bank, (ii) the African Development Bank, (iii) the Black Sea Trade and Development Bank, (iv) the Caribbean Development Bank, (v) the Central American Bank for Economic Integration, (vi) the Council of Europe Development Bank, (vii) the European Bank for Reconstruction and Development, (viii) the European

(viii) public authorities (excluding publicly guaranteed undertakings unless they fall under items (i) to (vii) or (ix)) including:

(1) public sector bodies of EC Member States charged with or intervening in the management of public debt, and

(2) public sector bodies of EC Member States authorised to hold accounts for customers; or

(ix) any other persons (including unincorporated firms and partnerships) other than natural persons, provided that the counterparty to such party is an institution as defined in items (i) to (viii), and provided further that, if the person referred to in this item (ix) is the Collateral Provider, each of the following additional conditions pursuant to § 1(17), 2nd to 3rd sentence, of the Banking Act must be met:

(1) the Collateral secures obligations arising from contracts, or the brokerage of contracts, relating to:

(A) the purchase and sale of financial instruments (*Finanzinstrumente* - "**Financial Instruments**") within the meaning of § 1(11), 1st sentence, of the Banking Act;

The term "Financial Instruments" includes (i) shares and other securities comparable to shares in companies, partnerships or other entities, and depositary receipts in respect of shares, (ii) investments (*Vermögensanlagen*) within the meaning of § 1(2) of the Act on Investment Assets (*Vermögensanlagengesetz*), *i.e.*, (1) interests providing a participation in respect of the profit of an undertaking, (2) interests in a property that the issuer or a third party holds or manages in its own name and for the account of others, (3) interests in respect of other close-ended investment funds, (4) profit sharing rights (*Genußrechte*) and (5) registered bonds (*Namensschuldverschreibungen*), except for interests in a cooperative (*Genossenschaft*), (iii) debt instruments, bearer bonds, registered bonds and certificates representing such debt instruments, (iv) any other interest giving the right to acquire or sell any interest specified under (i) to (iii) above or giving rise to a cash settlement determined by reference to securities, currencies, interest rates or other

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Investment Bank, (ix) the European Investment Fund, (x) the Inter-American Development Bank, (xi) the International Bank for Reconstruction and Development, (xii) the International Finance Corporation, (xiii) the International Finance Facility for Immunisation, (xiv) the Islamic Development Bank, (xv) the Multilateral Investment Guarantee Agency, (xvi) the Nordic Investment Bank and (xvii) the CAF-Development Bank of Latin America.

yields, commodities, indices or indicators, (v) units in an investment fund (*Investmentvermögen*) within the meaning of § 1(1) of the Capital Investment Code, (vi) Money Market Instruments, (vii) currencies or units of account and (viii) derivatives;[18]

(B) repurchase, lending or similar transactions relating to Financial Instruments; or

(C) loans for financing the purchase of Financial Instruments; and

(2) at the time at which the Collateral is provided, such Collateral does not consist of own shares of the Collateral Provider or shares in affiliated enterprises within the meaning of § 290(2) of the Commercial Code (*Handelsgesetzbuch*).[19]

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18 Pursuant to § 1(11), 3rd sentence of the Banking Act, "derivatives" for the purposes of the term "Financial Instruments" as used in § 1(17), 2nd sentence, of the Banking Act are (i) firm transactions (*Festgeschäfte*) in the form of purchase transactions, swap transactions or other transactions or options, in each case having a deferred settlement time and having a price which directly or indirectly depends on the price or level of an underlying (forward transactions (*Termingeschäfte*)), in relation to one of the following underlyings: (a) Securities or Money Market Instruments, (b) foreign currency or units of account, (c) interest rates or other yield, (d) indices relating to the underlyings listed under (a), (b) or (c), other financial indices or financial indicators or (e) derivatives; (ii) forward transactions (*Termingeschäfte*) having commodities, freight rates, emissions allowances, climatic or other physical variables, inflation rates or other economic variables or other assets, indices or measures as underlying, to the extent they (a) must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event), (b) are traded on a regulated market or a multilateral trading facility or (c) meet in accordance with Article 38(1) of the Commission Regulation (EC) No 1287/2006 of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council as regards record-keeping obligations for investment firms, transaction reporting, market transparency, admission of financial instruments to trading, and defined terms for the purposes of that Directive ("**Commission Regulation (EC) No 1287/2006**") any criteria of other derivatives and do not serve commercial purposes, provided that the requirements of Article 38(4) of said Regulation are not fulfilled, and, in each case, such transactions are not spot contracts within the meaning of Article 38(2) of Commission Regulation (EC) No 1287/2006; (iii) contracts for difference; (iv) firm transactions (*Festgeschäfte*) in the form of purchase transactions, swap transactions or other transactions or options, in each case having a deferred settlement time and serving the transfer of credit risks (credit derivatives); and (v) forward transactions (*Termingeschäfte*) in relation to one or more of the underlyings mentioned in Article 39 of Commission Regulation (EC) No 1287/2006, to the extent they meet the requirements set out under (ii) above.

19 § 290(2) to (4) of the Commercial Code (*Handelsgesetzbuch*) read, in English translation:

"(2) Controlling influence of a parent always exists if:

1. it is has the majority of the shareholders' voting rights in another enterprise;

2. it has in respect of another enterprise the right to appoint or dismiss the majority of the members of the administrative, management or supervisory organ and is at the same time a shareholder;

3. it has the right to govern the financial and operating policies by reason of a control agreement concluded with another enterprise or by reason of a provision of such other enterprise's by-laws; or

2. This Memorandum does not consider the validity and enforceability of Credit Support Documents in circumstances where:

(a) the Collateral Provider is a capital management company (*Kapitalverwaltungsgesellschaft* – "**Capital Management Company**") within the meaning of § 17(1) of the Capital Investment Code managing segregated pools of assets (*Sondervermögen*) within the meaning of § 1(10) of the Capital Investment Code and acting for the account of such segregated pool of assets (*Sondervermögen*). Posting of collateral by a Capital Management Company in such circumstances is subject to regulatory restrictions under § 93(5) of the Capital Investment Code and may be invalid vis-à-vis the investors in such segregated pool of assets (*Sondervermögen*);

(b) the Collateral consists of assets which form part of:

(1) the cover (*Deckung*) for (i) mortgage bonds (*Hypothekenpfandbriefe*), (ii) public sector bonds (*Öffentliche Pfandbriefe*) or (iii) ship mortgage bonds (*Schiffspfandbriefe*) issued by credit institutions (*Kreditinstitute*) under the Mortgage Bond Act (*Pfandbriefgesetz*);

(2) the cover (*Deckung*) for covered bonds (*gedeckte Schuldverschreibungen*)

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4. when taking an economic view, it holds the majority of risks and opportunities of an enterprise which serves for reaching of a narrowly defined and exactly specified goal of the parent (special purpose entity). Special purpose entities may, apart from enterprises, also be other legal persons under private law or dependent special pools of assets (*unselbständige Sondervermögen*) organised under private law, except for special funds (*Spezial-Sondervermögen*) within the meaning of § 2(3) of the Investment Act (*Investmentgesetz*) or comparable foreign investment funds or open-ended domestic special AIF with fixed investment terms (*offene inländische Spezial-AIF mit festen Anlagebedingungen*) established as investment funds within the meaning of § 284 of the Capital Investment Code or comparable EU investment funds or foreign investment funds which are comparable to open-ended domestic special AIF with fixed investment terms (*offene inländische Spezial-AIF mit festen Anlagebedingungen*) established as investment funds within the meaning of § 284 of the Capital Investment Code.

(3) Rights that belong to a parent pursuant to Subsection 2 include the rights belonging to a subsidiary and the rights belonging to persons acting for the account of the parent or subsidiary. To the rights of a parent in another company will be added the rights which the parent or a subsidiary has at its disposal on the basis of an agreement with other shareholders of this enterprise. Rights shall be deducted that:

1. are connected with shares that are held by the parent or a subsidiary for the account of another person, or

2. are connected with shares that are held as security, to the extent that these rights are exercised according to instructions of the person providing the security or, if a credit institution holds the shares as security for a loan, in the interest of the person providing the security.

(4) For calculating the majority pursuant to Subsection 2 no. 1, the portion of voting rights belonging to an enterprise shall be determined by the proportion of the number of voting rights that it can exercise from the shares belonging to it to the total number of all voting rights. From the total number of all voting rights shall be deducted the voting rights from treasury shares that belong to the subsidiary itself, one of its subsidiaries or another person for the account of these enterprises."

issued by certain credit institutions;[20] or

(3) the pool of assets (*Sicherungsvermögen*) to be maintained by certain types of insurance companies pursuant to the Insurance Supervisory Act and securing fulfillment of relevant policies; or

(c) Collateral is provided in accordance with the rules or regulations of:

(1) a payment or securities settlement system within the meaning of Article 2(a) of the Finality Directive;[21]

(2) a non-EC based payment or securities settlement system which meets substantially the requirements set forth in Article 2(a) of the Finality Directive;

(3) a financial market within the meaning of Article 9 of the Council Regulation (EC) No 1346/2000 of May 29, 2000 on insolvency proceedings,[22] as amended (the "**2000 Insolvency Regulation**") or Article 12 of the Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast)[23], as amended, (the "**2015 Insolvency Regulation**" and, together with the 2000 Insolvency Regulation, the "**Insolvency Regulations**").; or

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20 The following credit institutions have the right to issue covered bonds (*gedeckte Schuldverschreibungen*): (i) DZ BANK AG Deutsche Zentral-Genossenschaftsbank (§ 9 of the Law on the Reorganisation of Deutsche Genossenschaftsbank (*Gesetz zur Umwandlung der Deutschen Genossenschaftsbank*) of August 13, 1998); (ii) Landwirtschaftliche Rentenbank, a credit institution established under public law (§§ 3(5), 13 of the Law on Landwirtschaftliche Rentenbank (*Gesetz über die Landwirtschaftliche Rentenbank*) of May 11, 1949, as amended), (iii) IKB Deutsche Industriebank AG (§ 1(1) of the Law on Industriekreditbank Aktiengesellschaft (*Gesetz betreffend die Industriekreditbank Aktiengesellschaft*) of July 15, 1951, as amended) and (iv) Deutsche Postbank AG (§ 7 and § 14 (2) of the Law on the Reorganisation of Deutsche Siedlungs- und Landesrentenbank into a Stock Corporation) (*Gesetz über die Umwandlung der Deutschen Siedlungs- und Landesrentenbank in eine Aktiengesellschaft*) of December 16, 1999.

21 Pursuant to this provision, "system" means a formal arrangement (i) between three or more participants, without counting a possible settlement agent, a possible central counterparty, a possible clearing house or a possible indirect participant, with common rules and standardized arrangements for the execution of transfer orders between the participants, (ii) governed by the law of an EC Member State chosen by the participants; the participants may, however, only choose the law of a Member State in which at least one of them has its head office and (iii) designated, without prejudice to other more stringent conditions of general application laid down by national law, as a system and notified to the EC Commission by the EC Member State whose law is applicable, after that EC Member State is satisfied as to the adequacy of the rules of the system.

22 Official Journal no. L 160 of June 30, 2000, pp. 1 *et seq*. The term "financial market" is not defined therein.

23 Official Journal no. L 141 of June 5, 2015, pp. 19 *et seq*.

(4) an organized market within the meaning of § 2(5) of the German Securities Trading Act (*Wertpapierhandelsgesetz*).[24]

C.
THE CREDIT SUPPORT DOCUMENTS

I.
GENERAL

The Credit Support Documents constitute form agreements. The Credit Support Documents provide for collateral arrangements in respect of the amount of the balance due upon close-out of the Transactions pursuant to Section 6(e) of the Master Agreement. All documents generally follow similar principles for determining the amount of credit support to be delivered or returned from time to time. The net mark-to-market value of the Transactions documented under the Master Agreement to which the Credit Support Document relates is determined at regular intervals specified by the parties (Valuation Dates) based on the amount that one party would be required to pay to the other if all outstanding Transactions between them were terminated as of the Valuation Date and a termination payment calculated in accordance with the close-out and netting provisions of Sections 5 and 6 of the Master Agreement.

II.
THE SECURITY DOCUMENTS

Under the 1994 NY Annex, the 1995 Deed and the 1995 Transfer Annex, the party that has the net exposure at each interval (the Collateral Taker) is entitled to hold Eligible Credit Support with a value equal to (x) its Exposure, plus (y) an add-on amount of Collateral, if applicable, in excess of the Exposure to account for potential volatility in future Exposure (determined in accordance with the Independent Amount applicable to each party), less (z) the Threshold amount, if applicable, representing the permitted unsecured risk applicable to that counterparty.

Under the VM NY Annex and the VM Transfer Annex, the party that has the net exposure at each interval (the Collateral Taker) is entitled to hold Eligible Credit Support with a value equal to its Exposure.

The secured party under the IM NY Annex and the IM Deed (the Collateral Taker) is entitled to hold, via a third-party custodian, Eligible Credit Support with a value equal to a certain amount of Collateral to account for potential future exposure (determined in accordance with the Delivery Amount (IM) applicable to the pledgor), less the Threshold amount, if applicable.

Collateral will either be transferred to the Collateral Taker (or a third-party custodian) to be held in an account in the name of the Collateral Provider and secured in favor of the Collateral Taker) or returned to the Collateral Provider depending on whether the amount of

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[24] Pursuant to this provision, the term "organized market" means a market which is regulated and supervised by state-approved bodies, is held on a regular basis and is directly or indirectly accessible to the public.

Collateral entitled to be held (the Credit Support Amount) is less than or greater than the Value of the Collateral transferred (subject to any applicable Minimum Transfer Amount and rounding provisions specified by the parties in the relevant Credit Support Document).

Under each Security Document, the Security Collateral Provider grants a security interest in the Collateral transferred to the Secured Party (or an account held with a third-party custodian). The precise nature of this security interest is determined by the applicable law.

III.
THE TRANSFER ANNEXES

Under each Transfer Annex, the Transferor transfers outright full ownership in securities Collateral to the Transferee, subject to a conditional obligation to return equivalent fungible securities in various circumstances or, on default, to account for the value of those securities as part of the close-out netting calculations under Section 6(e) of the Master Agreement. Note that this is not intended to be a fiduciary transfer by way of security but an outright transfer of ownership under English law. This approach is analogous to a securities repurchase (repo) agreement, although, unlike a typical repo, the consideration for the transfer of securities is the Transferee's agreement to perform under the Master Agreement; there is no cash consideration passing at the time of the delivery or redelivery of the securities.

Under each Transfer Annex, the Transferor may provide cash Collateral. The Transferee is obliged to repay this amount in various circumstances, either with or without interest as the parties may agree, or, on default, to account for such amount as part of the close-out netting calculations under Section 6(e) of the Master Agreement. Cash Collateral is referred to commercially as "title transfer collateral" when provided under either Transfer Annex, but operates by the simple creation of debt obligations by way of payment rather than by way of transfer of ownership to any non-cash asset.

D.
FACT PATTERNS

You have asked us, when responding to each question, to distinguish between the following three fact patterns:

I. The Location of the Collateral Provider is in Germany and the Location of the Collateral is outside Germany.

II. The Location of the Collateral Provider is in Germany and the Location of the Collateral is in Germany.

III. The Location of the Collateral Provider is outside Germany and the Location of the Collateral is in Germany.

For the foregoing purposes:

(a) the "**Location**" of the Collateral Provider is in Germany if it is incorporated or otherwise organized in Germany and/or if it has a branch or other place of business in Germany; and

(b) the "**Location**" of Collateral is the place where an asset of that type is located under the private international law rules of Germany.

"**Located**" when used below in relation to a Collateral Provider or any Collateral should be construed accordingly.

Although we do not expressly refer to each fact pattern in our answer to each question, we have taken the fact patterns into consideration in developing our analysis. It should generally be clear from the context which of the fact patterns is being discussed in each case.

E.
LEGAL BACKGROUND

I.
RELEVANT ASPECTS OF GERMAN PRIVATE INTERNATIONAL LAW

(A) Securities

German conflict of laws rules regarding the transfer of ownership and the creation of security interests in Securities, and the effects of such transfer or creation, are generally mandatory and consequently do not honor a choice of law in respect of these matters.[25]

(1) Relevant Conflict of Laws Rules

The relevant conflict rules regarding the transfer of ownership are set out below. These rules apply *mutatis mutandis* to the creation of security interests in Securities. The laws governing the transfer of ownership and the creation of security interests govern also the effects of such transfer of ownership and creation of security interests.

(a) Dematerialized Securities and Immobilized Securities

The conflict of laws rules applicable to:

- Securities which are not represented by any physical certificate but solely by a book entry in a register ("**Dematerialized Securities**"); and

- Securities which are either represented by a global certificate or a book entry for the benefit of a central securities depository ("**CSD**") or by definitive securities which are held with the relevant CSD on a fungible basis ("**Immobilized Securities**")

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25 *See* Oberlandesgericht Köln, Recht der Internationalen Wirtschaft 1994, 969; Bundesgerichtshof, Neue Juristische Wochenschrift 1997, 461, 462; Kegel/Schurig, Internationales Privatrecht, 9th ed., 2004, § 19 I; Wendehorste in Münchener Kommentar zum Bürgerlichen Gesetzbuch, 5th ed., 2010, Art. 43 EGBGB, note 205. Regarding an exception with respect to Securities which constitute claims, *see* footnote 46 below.

are set out in § 17a of the German Securities Custody Act (*Gesetz über die Verwahrung und Anschaffung von Wertpapieren (Depotgesetz)* - the "**Securities Custody Act**").[26] This provision implements Article 9(2) of the Finality Directive in the broadest possible sense.[27] It is the objective of § 17a of the Securities Custody Act to create a common conflicts regime for dispositions over Immobilized Securities and Dematerialized Securities which are transferable either by book entry in an account or by registration in a debt register, in each case with constitutive legal effect for the benefit of the transferee.[28]

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26 § 17a of the Securities Custody Act reads, in English translation:

"The disposition over securities, or interests in securities held in a central securities depository system, which are, with constitutive legal effects, entered into a register or booked in an account shall be governed by the laws of the country under whose supervision the register is kept in which such entry for the direct benefit of the transferee is made or in which the head office or branch of the custodian is located which makes the account entry with constitutive legal effect for the benefit of the transferee."

27 We note that Article 9 of the EC Collateral Directive addressing certain conflict of laws issues in relation to Financial Collateral Arrangements has not been implemented in Germany. Article 9 of the EC Collateral Directive reads:

"(1) Any question with respect to [financial collateral arrangements] arising in relation to book entry securities collateral shall be governed by the law of the country in which the relevant account is maintained. The reference to the law of a country is a reference to its domestic law, disregarding any rule under which, in deciding the relevant question, reference should be made to the law of another country.

(2) The matters referred to in paragraph 1 are:

(a) the legal nature and proprietary effects of book entry securities collateral;

(b) the requirements for perfecting a financial collateral arrangement relating to book entry securities collateral and the provision of book entry securities collateral under such an arrangement, and more generally the completion of the steps necessary to render such an arrangement and provision effective against third parties;

(c) whether a person's title to or interest in such book entry securities collateral is overridden by or subordinated to a competing title or interest, or a good faith acquisition has occurred;

(d) the steps required for the realization of book entry securities collateral following the occurrence of an enforcement event."

Article 2(g) of the EC Collateral Directive defines "book entry securities collateral" as "financial collateral provided under a financial collateral arrangement which consists of financial instruments, title to which is evidenced by entries in a register or account maintained by or on behalf of an intermediary." Pursuant to Article 2(h) of the EC Collateral Directive, "relevant account" means in relation to book entry securities collateral which is subject to a financial collateral arrangement, the register or account - which may be maintained by the collateral taker - in which the entries are made by which that book entry securities collateral is provided to the collateral taker.

28 While Article 9(2) of the Finality Directive relates to collateral provided to clearing systems or to central banks, § 17a is not limited to such arrangements, but creates a general conflicts regime and thus reflects the extensive approach Germany has taken in the implementation of Article 9(2) of the Finality Directive, *see* the Federal Government's report for the bill dated August 13, 1999, Bundesrat-Drucksache 456/99, pp. 33 *et seq.*; Keller, Wertpapier-Mitteilungen 2000, 1269, 1281; Schefold, Praxis des Internationalen Privat- und Verfahrensrechts 2000, 468, 474; Dittrich, in Scherer, Depotgesetz, 2012, § 17a note 2 *et seq*.

To this end, with respect to Immobilized Securities[29] transferable by book entry in an account with constitutive legal effect for the benefit of the transferee § 17a of the Securities Custody Act provides that the law governing dispositions over such Securities is determined by reference to the location of the principal or branch office of the custodian bank making the account entry in favor of the transferee. In the case of Dematerialized Securities directly transferred or charged by entries in the register with constitutive legal effect for the benefit of the transferee, any disposition is subject to the laws of the jurisdiction under whose supervision the register is maintained. The location (*situs*) of the Immobilized Securities or Dematerialized Securities themselves is irrelevant in both cases and thus § 17a of the Securities Custody Act parts with the *lex cartae sitae* rule which used to govern all dispositions over bearer Securities, registered Securities bearing a blank indorsement or other certificated Securities which may be transferred, under their governing laws, by delivery alone of the certificate.

Certain questions relating to this provision remain unresolved, and no court precedent or developed rule under German law appears to exist in respect of the interpretation of § 17a of the Securities Custody Act.[30] In particular, it is uncertain whether this rule applies universally to the transfer of all types of Immobilized Securities or Dematerialized Securities including those governed by foreign law.[31]

In general, the Securities Custody Act addresses dispositions over Immobilized Securities governed by German law which fall under the statutory definition for securities under § 1(1) of the Securities Custody Act.[32] Such German law Immobilized Securities include bearer securities

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29 Dematerialized Securities transferred or charged through book entries on custody accounts are treated like Immobilized Securities.

30 For example, there is a question what the reference to the "legally effective" (*rechtsbegründend*) account or register entry means. Under the prevailing interpretation of the Securities Custody Act, the account entry is normally not constitutive for the right of the beneficiary of the account credit because the beneficiary has received its right in respect of the Securities under general principles of civil law before the account entry is made, *see* Einsele, Wertpapier-Mitteilungen 2001, 7, 15. In this case, there would be no legally effective entry and thus no valid reference to the location of an account (*see* Einsele, in Münchener Kommentar zum Handelsgesetzbuch, vol. 6, 3rd ed. 2014, Depotgeschäft, note 198). However, the expression "legally effective" stems from Article 9(2) of the Finality Directive and is an (expanding) translation of "legally" in the English version of the Finality Directive. Its purpose in the Finality Directive was to distinguish the relevant account entry (the account entry directly for the benefit of the receiver of a collateral security) from other account entries made in a multi-level custody structure in connection with the same transaction, *see* Dittrich, Effektengiroverkehr mit Auslandsberührung, 2002, 109 *et seq.;* Dittrich, in Scherer, Depotgesetz, *loc.cit.*, § 17a note 51 *et seq.* If "legally effective" is interpreted in the same sense, there is no conflict with the traditional interpretation of the Securities Custody Act (*cf.* Kümpel, Bank- und Kapitalmarktrecht, 4th ed., 2011, notes 11.439 *et seq.*; Franz, Überregionale Effektentransaktionen und anwendbares Recht, 2005, pp. 93 *et. seq.*). In a decision by the Higher Court (*Oberlandesgericht*) in Dusseldorf (OLG Düsseldorf, I-11 U 3/03, 30 July 2003), the court appears to share the view that the application of § 17a of the Securities Custody Act requires legally effective entries. The securities in question were, however, share certificates in a Swiss stock corporation and these share certificates were definitive securities (*effektive Stücke*) and were not booked on a securities account nor transferred in book entry form. It is therefore questionable to what extent this decision would be of relevance for Dematerialised Securities and Immaterialised Securities.

31 When referring to the "law governing the security", we make reference to the law that is applicable to the relevant Security either by virtue of a valid choice of law or by operation of law.

32 § 1(1) of the Securities Custody Act reads, in English translation:

and securities in registered form bearing a blank indorsement which are held through Clearstream, Frankfurt and in relation to which the transfer of (co-) ownership vests a proprietary right *in rem* in the transferee.[33] German law Immobilized Securities also include Bunds.[34] Consequently, the transfer of (co-)ownership in respect of German law Immobilized Securities will be subject to the conflicts rule regarding Immobilized Securities under § 17a of the Securities Custody Act.

If Immobilized Securities or Dematerialized Securities governed by foreign law are similar in kind to the types of securities mentioned in § 1(1) of the Securities Custody Act and if, under the law governing such foreign Securities, the transferee may obtain not only a claim for delivery of such Securities but a proprietary position therein, it is likely that the conflicts provisions of § 17a of the Securities Custody Act will apply to dispositions over such Securities.[35] This should be the case, for example, for negotiable foreign law Securities which may be characterized as bearer Securities or Securities in registered form bearing a blank indorsement.[36] Likewise, in the case of foreign law Immobilized Securities or Dematerialized Securities held in custody by a foreign CSD which have been accepted for clearing by Clearstream, Frankfurt through the account link established with such foreign CSD pursuant to § 5(4) of the Securities Custody Act, if the transferee may obtain a legal position that is equivalent to a (co-)ownership interest in such Securities, it is likely that the conflicts provisions of § 17a of the Securities Custody Act will apply to dispositions over such Securities.[37]

"Securities within the meaning of this statute are shares, mining shares, intermediate certificates, share certificates in the *Reichsbank*, interest coupons, dividend coupons, talons, bearer bonds, bonds transferable by indorsement, further other securities if they are negotiable, excluding notes and paper money."

33 Those Securities exclude, *inter alia*, German law registered bonds (*Namensschuldverschreibungen*) which are non-negotiable, constitute a claim transferable by assignment and do not qualify for a *bona fide* acquisition of the claim.

34 Bunds are not represented by certificates. Any issue of Bunds is entered into the Federal Debt Register (*Bundesschuldbuch*) in the name of Clearstream, Frankfurt. The ownership in Bunds is at no time vested in Clearstream, Frankfurt, but in the bondholders who own a proportionate co-ownership interest (*Miteigentumsanteil*) in the pool of Securities of a given issue (§ 6 of the Securities Custody Act, § 6(2) of the Government Debt Act (*Bundesschuldenwesengesetz*). Pursuant to § 8(2), 1st sentence, of the Government Debt Act, Bunds held through Clearstream, Frankfurt are deemed to be bearer Securities for purposes of transfer of ownership, the creation of security interests therein and securities custody.

35 It is the view of the German legislature that § 17a of the Securities Custody Act applies to dispositions *in rem* over Securities and only, excluding dispositions over instruments that take the form of a claim (*schuldrechtliche Ansprüche*). *See* the Federal Government's report for the bill dated August 13, 1999, Bundesrat-Drucksache. 456/99, p. 35.

36 The cross-border clearing of Immobilized Securities held in non-German central depository systems is subject to the certain conditions, *see* Section 5(4) of the Securities Custody Act. Under Section 5(4) no. 2 of the Securities Custody Act, Clearstream, Frankfurt may only establish a reciprocal account link with a foreign CSD and entrust Securities to it for clearing if it is ensured that the depositor obtains a legal position with respect to such Securities which is equivalent to the (co-)ownership interest granted to a depositor under the Securities Custody Act in the case of Securities held in custody by Clearstream, Frankfurt.

37 Even where an account link between Clearstream, Frankfurt and the relevant foreign CSD exists, there appears to be no certainty that the legal position obtained by a transferee of foreign law Securities transferred through such link will be comparable to German law ownership.

However, with respect to dispositions over foreign law Securities which are incomparable to German law types of Securities or where the transferee will obtain only a claim against the custodian making the account entry for the delivery of such Securities (right *ad rem*) but no proprietary position therein, it is uncertain whether § 17a of the Securities Custody Act or the traditional conflict of laws rules will apply. We would expect that the governing law with respect to such dispositions should be determined pursuant to § 17a of the Securities Custody Act.[38]

(b) Bearer Securities

Where the law governing the Security provides that the transfer of ownership in the Security requires the delivery of a certificate, the transfer of ownership in bearer Securities other than Immobilized Securities or Dematerialized Securities is governed by the laws of the jurisdiction in which the certificate is physically located upon completion of delivery (*lex cartae sitae – see* Articles 43(1), 46 of the Introductory Act to the Civil Code (*Einführungsgesetz zum Bürgerlichen Gesetzbuche* – the "**Introductory Act to the Civil Code**")).[39]

(c) Registered Securities

It is necessary to distinguish between:

- negotiable registered Securities which are transferable by (i) indorsement, (ii) delivery and indorsement or (iii) mere delivery; and

- non-negotiable registered Securities which are transferable by assignment.

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38 It is the objective of § 17a of the Securities Custody Act to establish a universal conflicts regime for all Immobilized Securities or Dematerialized Securities held in a central securities depository system. The wording of the provision itself is not limited to certain types of Immobilized Securities. However, in the domestic context it is a principle of the Securities Custody Act that the transfer of (co-)ownership in respect of such Immobilized Securities vests a proprietary right *in rem* in the transferee for which German law contains specific substantive rules. If § 17a of the Securities Custody Act were to call for the application of German law in the case of a transfer of foreign law Immobilized Securities or Dematerialized Securities which do not allow for the creation of a right *in rem* therein under their governing laws, it is unclear which substantive rules of German law would govern such transfer. For unless the foreign law securities may be assimilated to a comparable type of German Securities, German law does not contain specific substantive rules in regard of the transfer of such Securities. By way of example, in the case of Dematerialized Securities which are generally unfamiliar to German law, with the exception of Bunds that are by statute treated as bearer Securities (*see* footnote 35 above), it may be argued that foreign Dematerialized Securities would have to be recharacterized as bearer Securities and the German rules on the transfer of bearer Securities would apply (cf. Dittrich, in Scherer, Depotgesetz, *loc.cit.*, § 17a note 44 *et seq*.). There is, however, no court precedent or developed rule in respect of this question.

39 Article 46 of the Introductory Act to the Civil Code provides that, if there is a substantially closer connection (*wesentlich engere Verbindung*) to the laws of another jurisdiction than to the laws of the jurisdiction governing pursuant to the rules set forth in Article 43 to 45 of the Introductory Act to the Civil Code, the laws of such other jurisdiction shall be applicable. There is no court precedent or developed rule in respect of this provision.

By way of example, German law registered bonds (*Namensschuldverschreibungen*) are non-negotiable, constitute a claim which is transferable by assignment, an effective assignment also resulting in the transfer of the certificate, and do not qualify for a *bona fide* acquisition of the claim.

Where the law governing the Security provides that the transfer of ownership in the Security requires an indorsement, the transfer of ownership in such Security is governed by the laws of the jurisdiction in which the indorsement is made.

Where the law governing the Security provides that the transfer of ownership in the Security requires delivery and indorsement at the point of the completion of delivery, the transfer of ownership in such Security is governed by the laws of the jurisdiction in which the certificate is physically located and the indorsement is made.

If a Security may, under its governing law, be transferred by delivery alone of the certificate, *e.g.* where a Security bears a blank indorsement, the transfer of ownership in such Security is governed by the laws of the jurisdiction in which the certificate is physically located upon completion of delivery.

If, as is the case with German law registered bonds, a Security is under its governing law considered to be a claim transferable by assignment, such assignment is governed by the law governing such Security.

(d) Other Securities

In the case of Securities other than those mentioned above, transfer of title therein is governed by the laws governing such Securities.

(2) Renvoi

In the event that the law governing the transfer of ownership or creation of a security interest, according to German conflict of laws principles, calls for the application of German law or the laws of another jurisdiction pursuant to the conflict of laws principles of such other jurisdiction, German law will generally recognize such remission or transmission to the law of a third jurisdiction.[40]

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40 Article 4(1), 1st sentence, of the Introductory Act to the Civil Code. If the applicable law under German conflict-of-laws principles calls for German law to be applied in the instance (*renvoi*), German substantive law will apply (Article 4(1), 2nd sentence of the Introductory Act to the Civil Code). The *renvoi* is excluded in the case of a valid express choice of law (Article 4(2) of the Introductory Act to the Civil Code) and in matters regarding the law of obligations (Article 20 of the Rome I Regulation). Further, if the *renvoi* is not appropriate, a court may decline to give effect to the remission or transmission ordered by the conflict rules of the law which is called to apply in the instance, Article 4(1), 1st sentence of the Introductory Act to the Civil Code. Instead, the substantive rules of such law will be applied in the instance. With respect to § 17a of the Securities Custody Act, however, it is not inconceivable that a *renvoi* should be excluded because, in the interest of a concentration of Securities transactions in specific accounts, the law governing dispositions over Immobilized Securities should be determined by reference to the location of the transferee's account in which the credit entry is made irrespective of whether the conflict-of-laws principles of the relevant jurisdiction recognize the rules contained in § 17a of the Securities Custody Act, *see* Keller, Wertpapier-Mitteilungen 2000, 1282. There appears, however, to exist no developed rule in respect of this issue under German law.

(3) Applicability of New York or English Law

As follows from all of the foregoing, the choice of New York or English law (as applicable) to govern the transfer of ownership or creation of a security interest in Securities pursuant to the Credit Support Documents will be recognized by German law in the following cases:

(a) Where, in the case of Securities in respect of which dispositions are booked in accounts with constitutive effect in favor of the transferee or beneficiary of the security interest, the account entry in respect of such transfer or creation is made with constitutive effect for such transferee or beneficiary by the principal or branch office of a custodian bank located in the State of New York or England and Wales (as applicable).

(b) Where, in the case of Securities in respect of which dispositions are entered into a register with constitutive effect in favor of the transferee or beneficiary of a security interest, the register is maintained under the supervision of the State of New York or England and Wales (as applicable).

(c) Where, in the case of Securities other than those mentioned under (a) or (b) above, the law governing the Security provides that the transfer of ownership requires the delivery of a certificate, such certificate is physically located in the State of New York or England and Wales (as applicable) upon completion of such transfer or creation.

(d) In the case of Securities other than those mentioned under (a) or (b) above,

(i) where the law governing the Security provides that the transfer of ownership requires an indorsement, such indorsement is made in the State of New York or England and Wales (as applicable),

(ii) where the law governing the Security provides that the transfer of ownership requires both delivery and indorsement, the certificate is physically located upon completion of such transfer, and the indorsement is made, in the State of New York or England and Wales (as applicable),

(iii) where a Security bears a blank indorsement and may, under the laws which govern such Security, in such event be transferred by delivery alone, the certificate is physically located in the State of New York or England and Wales (as applicable) upon completion of such transfer.

(e) In the case of Securities other than those mentioned under (a), (b), (c) or (d) above, such Securities are governed by New York or English law (as applicable).

If under German conflict rules the transfer of ownership or the creation of a security interest is subject to a law other than New York or English law (as applicable), German law should still recognize the choice of New York or English law, as the case may be, if such other law were to give effect to the choice of New York or English law. By way of illustration, under German conflict rules the transfer of ownership or creation of a security interest in Country X government bonds, assuming they were Immobilized Securities in bearer form under the law of

Country X and the account entry with constitutive effect for the benefit of the transferee is made by the principal or branch office of a custodian bank located in Country Y, would be governed by the laws of Country Y. If the laws of Country Y were to give effect to the choice of New York or English law, German law should recognize such choice of law.

(B) Cash

As will be explained below (under F.II.(A) (*Question 3 and Answer to Question 3*)), a pledge of Cash that has been transferred by or on behalf of the payor to a bank account maintained by the payee, as contemplated by the 1994 NY Annex and the 1995 Deed,[41] is inconceivable in German law. As will also be explained below (under G.II. (*Question 26 and Answer to Question 26*)) equally inconceivable is the transfer of ownership in Cash in these circumstances, as contemplated by the 1995 Transfer Annex.[42] Accordingly, there exist no conflict rules in Germany regarding such arrangements. We would expect, though, that a German court would refer to the substantive law of the jurisdiction in which the account of the recipient of the funds transferred is maintained.

In any event, with respect to a payee's claim against the bank maintaining the account of the payee to which the funds are being transferred, German conflict of laws principles refer to the law governing the account relationship between the bank and the payee. If the account is maintained with a bank in Germany, the claim of the accountholder against his bank for payment of money standing to the credit in the account, as well as all other rights of the accountholder arising from the account relationship, are governed by German law, unless otherwise agreed between the bank and the accountholder in respect of the account relationship.[43]

The assignment of a claim for the payment of money and the creation of a security interest in such claim, as well as the effects of such assignment or creation, are governed by the law which governs such claim.[44]

The afore-described conflicts principles constitute mandatory rules of law.

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41 *Cf.* Paragraphs 2 and 12 ("Transfer") of the 1994 NY Annex; Paragraphs 2(b) and 4(b)(i) of the 1995 Deed.

42 *See* Paragraphs 3(a) and 5(a) of the 1995 Transfer Annex.

43 Pursuant to German conflict of laws principles, the account relationship between a bank and a depositor of funds is subject to the law of the jurisdiction in which the bank is located, except as otherwise agreed, Articles 3(1), 4(1) and (2) of the Rome I Regulation. *See*, with respect to Articles 28(2), 27 of the Introductory Act to the Civil Code which have been replaced by said provisions of the Rome I Regulation, Bundesgerichtshof, Wertpapier-Mitteilungen 1983, 411; Martiny in Münchener Kommentar zum Bürgerlichen Gesetzbuch, 4th ed., 2006, Article 28, note 350; *contra* Soergel/von Hoffmann, Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen, 12th ed., 1996, Article 28, note 318 (law of the client).

44 Regarding a pledge *see* Soergel/von Hoffmann, *loc. cit.*, Article 33, note 16; von Bar, Internationales Privatrecht, vol. 2, 1991, note 572; regarding an assignment by way of security *cf.* Article 14 of the Rome I Regulation.

(C) Ineffective Choice of Law

If, pursuant to German conflict rules, a choice of law to govern the transfer of ownership or the creation of a security interest is invalid or does not comply with such conflict rules, such choice of law will generally be disregarded by German courts.[45] German courts will nevertheless uphold the transfer of ownership or the creation of a security interest if it is valid under the substantive law that falls to be applied pursuant to German conflict principles.

II.
RELEVANT ASPECTS OF COLLATERAL ARRANGEMENTS

(A) General

(1) The Obligation to Provide, and the Creation of, Security

German law does not distinguish between the creation of a security interest and its perfection, but distinguishes between the obligation to provide security and the creation (*Bestellung*) of the security interest. Creation as such results in effective security and constitutes fulfilment of the obligation to provide security.

Under German conflict of laws rules, the parties may freely choose the law governing the obligation to provide security (Article 3(1) of the Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) - the "**Rome I Regulation**"). However, the parties may not freely choose the law governing the creation of a security interest. The law governing the creation of a security interest is determined by mandatory rules (*see* above under E.I.).

In respect of the Security Documents, Paragraph 3 of the Annexes and the Deeds oblige the Pledgor to provide security. The choice by the parties of New York law or English law to govern the obligation to provide security is valid under German law.

(2) The Obligation to Transfer, and the Transfer of, Ownership

Similarly, under German conflict of laws rules, the parties may freely choose the law governing the obligation to transfer ownership (Article 3(1) of the Rome I Regulation), while the law governing the actual transfer of ownership is determined by mandatory rules (*see* above under E.I.).

In respect of the Transfer Annexes, Paragraph 2 establishes the obligation to transfer ownership. The choice by the parties of English law to govern such obligation is valid under German law.

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45 In the case of claims such as German law non-negotiable registered Securities, a choice of law made in respect of the transfer or creation of a security interest will be recognized if the debtor of the claim consents to such choice of law, *see* Bundesgerichtshof, BGHZ 108, 353 (362); Bundesgerichtshof, Praxis des Internationalen Privat- und Verfahrensrechts 1985, 221.

(B) Collateral Arrangements in Respect of Securities

German law provides for the following types of collateral arrangements in respect of ownership (or co-ownership) rights in negotiable Securities or claims arising from non-negotiable Securities (such as registered bonds under German law, *see* above under E.I.(A)(1)(b)):

(a) in relation both to ownership (or co-ownership) rights in negotiable Securities:

(i) the pledge (*Pfandrecht*) (*see* (1) below);

(ii) the transfer of such ownership (or co-ownership) rights for security purposes (*Sicherungsübereignung*) (*see* (2) below); and

(iii) the outright transfer of such ownership (or co-ownership) rights (*see* (4) below); and

(b) in relation to claims arising from non-negotiable Securities:

(i) the pledge (*Pfandrecht*) (*see* (1) below);

(ii) the assignment of such claims for security purposes (*Sicherungsabtretung*) (*see* (3) below); and

(iii) the outright assignment (*Abtretung*) of such claims (*see* (5) below).

(1) Pledge

(a) Statutory Framework

The pledge of the ownership (or co-ownership[46]) in bearer Securities is governed by the same rules that apply to the pledge of moveables[47] (§ 1293, §§ 1204 - 1258 of the Civil Code). Substantially the same rules which apply to bearer Securities apply to Securities payable to order (§§ 1273, 1292 of the Civil Code).

The pledge is *per se* a possessory security interest; subject to the discussion under (c) below, it will come into existence only if the pledgee obtains possession of the asset to be pledged. It is strictly accessory to the obligation which it is to secure; if such obligation does not validly arise, a pledge cannot be created; if such obligation ceases to exist, the pledge likewise ceases to exist; a substitution of such obligation for another obligation would result in the nullity of the pledge. If the obligation to be secured is or becomes subject to a permanent defense, the pledged asset must be returned to the pledgor (§ 1254 of the Civil Code). It is not necessary, though, that the obligation to be secured is for a fixed amount or for a fixed maximum amount.

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46 § 1258 of the Civil Code. With respect to Securities held in custody, *see* Soergel/Mühl, Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen, 13th ed., 2001, § 1258, note 2.

47 Wherever the term "moveables" is used herein, reference is made to tangible property other than real estate or ships.

Its accessory nature notwithstanding, a pledge may be created to secure future obligations as well as conditional obligations (§ 1204(2) of the Civil Code). The priority rights of the pledgee are solely determined by the time of creation, even when the pledge is created for a future or conditional obligation (§ 1209 of the Civil Code).

A pledge ceases to exist to the extent the collateral is returned to the pledgee or owner, even if the parties agree otherwise (§ 1253(1) of the Civil Code). Further new pledges may be made under a master pledge agreement, provided that the requirements for the creation of a pledge described in the first paragraph under (b) below are met, but they would constitute separate security interests.

The asset or assets to which the pledge(s) is (are) to extend must at all times be identifiable. Subject to such requirement, a pledge may effectively be created over a fluctuating pool of assets.[48]

The rules set out in the Civil Code provide that the pledgee must keep the collateral at all times in safe custody (§ 1215 of the Civil Code). The statutory rules do not provide for a right of the pledgee to use, sell, pledge or otherwise dispose of the collateral.[49] Only if specifically so agreed between pledgor and pledgee, the pledgee will be entitled to collect dividends, interest or other distributions in respect of the collateral (*Nutzungspfandrecht*) (*see* § 1213(1) of the Civil Code).

A pledge of a non-negotiable registered Security constitutes, in terms of law, a pledge of a claim and is governed as such by the special rules set out in §§ 1279 to 1290 of the Civil Code.

(b) Creation of a Pledge

The creation (*Bestellung*) of a pledge under German law requires (i) an agreement between the pledgor and the pledgee to establish a pledge over the collateral for the benefit of the pledgee and (ii) the transfer of possession of the collateral (§§ 1205, 1206 of the Civil Code).

In respect of the transfer of possession,[50] consideration need be given to the creation of a pledge in respect of such Securities the dispositions of which, pursuant to German conflict of laws rules (as described in E.I.(A), above), are governed by German law. Where such Securities are held in a CSD, any pledge over such Securities will be established in the co-ownership interest of the pledgor in a given issue of such Securities held in the CSD.[51] With respect to such

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48 The pledge consists, *stricto sensu*, of a series of security interests attached to each individual asset.

49 *See* the discussion under (c) below on whether the statutory rules allow for an agreement between the pledgor and the pledgee on a right of use in respect of the pledged assets.

50 In general, possession requires (direct or indirect) physical control and the intention to possess (*animus possidendi*) on the part of the transferee.

51 In our view, the scope of a pledge with respect to a portion of securities held in a CSD may be validly determined through a reference to the nominal amount of such pledged securities (Kümpel, Wertpapier-Mitteilungen 1980, 422, 428). Pursuant to a different view in the legal literature, a pledge over a portion of securities held in collective custody (*Sammelverwahrung*) may only be validly created if such portion is

Securities, the CSD maintains direct possession, while the bondholders maintain indirect possession either through the CSD directly (if they maintain a securities account with such CSD and the relevant Securities are credited to such account) or indirectly through an intermediary depositary (if the relevant Securities are credited to their securities accounts with an intermediary depositary (which may or may not be a CSD)). Subject to certain refinements, effective transfer of possession for purposes of creating a pledge in the co-ownership interest in such Securities takes place by debiting the account of the pledgor with the CSD or an intermediary depositary and crediting the account of the pledgee with the CSD or an intermediary depositary,[52] by which acts the pledgor loses (indirect) possession and the pledgee acquires (indirect) possession.[53]

If Securities in relation to which the creation of a pledge, according to German conflict rules, would be governed by German law are not held by the pledgor through an account with a CSD, but through an intermediary depositary or a chain of intermediary depositaries, it will be necessary for the effective creation of a pledge in the co-ownership interest of the pledgor that each such intermediary depositary (whether German or foreign) holds (indirect) possession of the relevant Securities for the benefit of its respective depositors. For all practical purposes, this will be the case if all intermediary depositaries are German banks authorized to engage in securities custody business. It will not be the case if the chain of intermediaries includes a (non-German) depositary (which may or may not be a CSD) which does not hold possession of the Securities for the benefit of its depositors, but merely purports to owe a contractual obligation to deliver the Securities to its depositors. In such event (indirect) possession would be wanting, and a pledge in the co-ownership interest of the pledgor in such Securities would not be validly created.

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sufficiently individualized, which, especially in circumstances where not all securities held on a deposit account belonging to the same kind but only a portion thereof are pledged, would require transfer of the relevant portion of the securities to a separate deposit sub-account (Merkel, in Schimansky/Bunte/Lwowski Bankrechts-Handbuch, 4th ed., 2011, § 93, note 91). There is no court precedent or developed rule in respect of this question.

52 The pledge characterization is generally recorded in the books of the pledgee.

53 This analysis is based on § 1205(1), 1st sentence, of the Civil Code. *See* Opitz, Depotgesetz, 2nd ed., 1955, §§ 6-8, note 34; Heinsius/Horn/Than, Depotgesetz, 1975, § 6, note 96; Staudinger/Wiegand Kommentar zum Bürgerlichen Gesetzbuch, 12th ed., 2009, § 1205, note 24; Klanten in Schimansky/Bunte/Lwowski, Bankrechts-Handbuch, 4th ed., 2011, § 72, note 118; Palandt/Bassenge, Bürgerliches Gesetzbuch, 73rd ed., 2014, § 1205, note 4; Bankrecht und Bankpraxis, 10.08 - 78th delivery, note 8/346. Cf. also Rögner, in Scherer, Depotgesetz, *loc.cit.*, § 6 note 6. According to other commentators, the pledgor's possession is deemed to be transferred to the pledgee (as described above) before the agreement on the creation of the pledge takes effect (§ 1205(1), 2nd sentence, of the Civil Code), *see* Kregel in Reichsgerichts-rätekommentar, 1996, § 1205, note 19; Soergel/Mühl, *loc. cit.*, § 1205, note 38. Yet other commentators consider the transfer of possession to be accomplished by an assignment pursuant to § 1205(2) of the Civil Code of the pledgor's claim against the CSD or an intermediary depositary to repossess the Securities, *see* Reichsgericht, RGZ 103, 153; Damrau in Münchener Kommentar, 6th ed., 2013, § 1205, note 18; Wolff/Wellenhofer, Sachenrecht, 29th ed., 2014, § 16, note 14; Planck/Flad, Bürgerliches Gesetzbuch, § 1205, note 2a. In the latter case, a notice in respect of such assignment to the pledgor's immediate depositary would be required for the pledge to be validly created. This requirement would in our view be fulfilled by the pledgor's instruction to the CSD or an intermediary depositary to transfer the relevant Securities from its account to the pledgee's account with the CSD or an intermediary depositary and to hold (until further notice) direct or indirect possession thereof for the benefit of the pledgee.

(c) Right of Use

As set out above (*see* E.II.(B)(1)(a)), the rules of the Civil Code require that the pledgee keeps collateral in the form of Securities at all times in safe custody. They do not provide for any right of the pledgee to use or dispose of such collateral prior to maturity of the secured obligation.

An agreement between the pledgor and the pledgee regarding the pledgee's right of use in respect of pledged Securities would contravene basic concepts of German law regarding pledges. Pursuant to §§ 1204 *et seq.* of the Civil Code a pledge of moveables essentially grants an *in rem* right to realize such collateral at maturity upon default of the debtor in order to discharge the secured obligation (§ 1228 of the Civil Code). As a general rule, the nature of, and the principal rights and obligations associated with, a pledge granted under §§ 1204 *et seq.* of the Civil Code may not be supplemented or amended by agreement between the pledgor and the pledgee.[54] The concepts and principles of German property law, *e.g.*, the rules on ownership (*Eigentum*), usufruct (*Nießbrauch*) or pledge (*Pfandrecht*), are defined in the Civil Code for reasons of clarity and legal certainty.[55] Moreover, the legislature considers the statutory rules to be a well-balanced framework adequately protecting the pledgor from exceedingly unfavorable agreements with the pledgee.

There exists certain special German legislation which recognizes in limited circumstances an appropriation right of the pledgee:

- Under §§ 17, 13(1) of the Securities Custody Act, the pledgee of securities may be specifically authorized to appropriate or dispose prior to maturity of the securities entrusted to it as custodian.[56] Under the Securities Custody Act such an irregular pledge (*pignus irregulare*) may only be created for the benefit of a German credit institution which has been authorized, under the Banking Act, to conduct securities custody business.

- Pursuant to § 19 no. 1 of the Act on the Deutsche Bundesbank (*Gesetz über die Deutsche Bundesbank*), the Bundesbank, when extending loans collateralized by pledges, is entitled to appropriate the asset pledged to it, in which case the claims of the Bundesbank under such Loan in the amount of the stock exchange or market price of such asset lapse.

In our view, these special provisions regarding the right of use or appropriation in respect of pledged securities in connection with (i) securities custody business carried on by German credit institutions and (ii) loans extended by the Bundesbank may not be expanded beyond their explicit scope of application. As exceptions to the general rules regarding pledges as perceived by the Civil Code, they are limited to the specific circumstances to which they explicitly apply.

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54 The prohibition to supplement or amend is based on the *numerus clausus* of rights *in rem* and the limitation of varieties (*Typenzwang*) in respect of each of these rights. Soergel/Mühl, *loc. cit.*, Introduction to § 1204, note 5; Staudinger/Seiler, *loc. cit.*, 2012, Introduction to Property Law, note 38 *et seq.*; Wiegand, Numerus clausus der dinglichen Rechte, Festschrift Kroeschell (1987), pp. 623 *et seq.*

55 From a third party's perspective, the attribution of rights *in rem* should be unambiguous.

56 *See* Heinsius/Horn/Than, *loc. cit.*, § 17, note 16, 22; Opitz, *loc. cit.*, § 17, note 5, Benzler, in Scherer, Depotgesetz, *loc.cit.*, § 17 note 4.

While German courts and legal commentators have recognized the existence of a non-statutory, irregular pledge of Cash[57] to which the concepts and principles of German property law as described above do not apply, no court precedent or developed rule of German law addresses the creation and effects of an irregular pledge over Securities.[58]

Article 5(1) of the EC Collateral Directive requires EC Member States, if and to the extent that the terms of a Security Financial Collateral Arrangement so provide, to ensure that the collateral taker is entitled to exercise a right of use in relation to the collateral provided under such collateral arrangement. A pledge over Securities may be the subject of a Security Financial Collateral Arrangement (*see* the discussion under E.II.(D)(1) below). When implementing the EC Collateral Directive, the German legislature was of the view that no changes need to be made to the existing statutory rules applicable to a pledge under the Civil Code because such rules would already permit agreements between a pledgor and a pledgee providing for the pledgee's right to use, and to dispose of, pledged Securities.[59]

As said before, this view is neither supported by any court precedent nor by the majority of views expressed in legal literature. Therefore, we believe that the concept and the rights and obligations under an irregular pledge in respect of Securities do not afford adequate certainty to determine the validity under German law of a right of use or appropriation agreed upon between a pledgor and a pledgee, except for circumstances where the afore-described special statutory provisions regarding such right of use or appropriation apply.

(d) Realization

The realization (enforcement) of the pledge may only be made if the claim which it secures has become due and payable (§ 1228(2) of the Civil Code). If such obligation is not an obligation for the payment of money, realization is permitted only once such obligation has become an obligation for the payment of money and has become due and payable (§ 1228(2)). Any realization prior to the due date of the secured obligation is expressed to be "illegal" and will be without legal effect (§ 1243(1) of the Civil Code). The Civil Code provides in § 1229 and §§ 1233 to 1239 for comprehensive rules regarding the manner of realization of the collateral, some of which are considered to be fundamental for the protection of the pledgor and are mandatory and not subject to the disposition of the parties.

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57 Bundesgerichtshof, BGHZ 127, 138, (140); Oberlandesgericht Bamberg, SeuffA 64, note 48; Soergel/Mühl, *loc. cit.*, § 1204, note 29; Staudinger/Wiegand, *loc. cit.*, § 1204, note 54 *et seq.*; Damrau in Münchener Kommentar zum Bürgerlichen Gesetzbuch, *loc. cit.*, § 1204, note 9; Erman/Schmidt, Bürgerliches Gesetzbuch, 14th ed., 2014, § 1204, note 4.

58 Although no examples are cited, this hypothetical is not excluded by Soergel/Mühl, *loc. cit.*, § 1204, note 29; Damrau in Münchener Kommentar zum Bürgerlichen Gesetzbuch, *loc. cit.*, § 1204, note 9.

59 Report of the Government submitting the Bill of the act implementing the EC Collateral Directive in German law (*Begründung des Gesetzesentwurfs der Bundesregierung)*, Bundestag-Drucksache 15/1853, p. 11 *et seq.*

As part of the implementation of the EC Collateral Directive in German law[60] a special rule has been introduced in § 1259 of the Civil Code on the realization of a pledge in circumstances where both the pledgor and the pledgee are:

(i) enterprises (*Unternehmer*) within the meaning of § 14(1) of the Civil Code which term comprises natural or legal persons as well as partnerships having legal capacity, in each case to the extent that any such person is acting in a business or self-employed professional capacity (*gewerbliche oder selbständige berufliche Tätigkeit*) with respect to the pledge;

(ii) public law entities; or

(iii) pools of assets governed by public law (*öffentlich-rechtliche Sondervermögen*).

If both the pledgor and the pledgee are within one of these categories, pursuant to § 1259 of the Civil Code the parties may agree[61] with respect to an asset having an exchange or market price[62] that (i) the pledgee may liquidate such asset by sale undertaken by himself or by a third party or (ii) ownership in such asset shall vest in the pledgee at the time at which the claim which it secures becomes due and payable in which case the claim shall be deemed to be fulfilled in an amount equal to the exchange or market price prevailing on the due date. Where the parties have so agreed, the statutory rules regarding the manner of realization of the pledge described above (§ 1229 and §§ 1233 to 1239 of the Civil Code) do not apply.

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60 § 1259 of the Civil Code which is discussed below implements Article 4 of the EC Collateral Directive according to which, *inter alia*, EC Member States shall ensure that on the occurrence of an enforcement event, the collateral taker shall be able to realize financial instruments provided under, and subject to the terms agreed in, a Security Financial Collateral Arrangement by sale or appropriation and by setting off their value against, or applying their value in discharge of, the relevant financial obligations. Article 4(4) of the EC Collateral Directive provides that the manners of realizing such Collateral shall, subject to the terms agreed in the Security Financial Collateral Arrangement, be without any requirement to the effect that (a) prior notice of the intention to realise must have been given, (b) the terms of the realization be approved by any court, public officer or other person, (c) the realization be conducted by public auction or in any other prescribed manner or (d) any additional time period must have elapsed.

61 § 1259, 1st sentence, of the Civil Code does not expressly provide whether the agreement regarding the realization of the pledge must be made at the time at which the pledge is created or may also be made at a later point in time. There is no authority on this issue available. The provision implements Article 4 of the EC Collateral Directive. Article 4(2)(a) of said Directive is ambiguous in this regard. While the English language version thereof provides that appropriation is possible only if "this has been agreed by the parties in the security financial collateral arrangement", the German language version thereof seems to indicate that the relevant agreement must have been made at the time at which the relevant security financial collateral arrangement has been agreed upon.

62 "Market price" means the average of the current prices at which transactions are effected on the day on which the collateral is liquidated in the place where the collateral is located (*e.g.*, where securities are deposited or registered), provided that the market or average price is determined on the basis of sufficient sales being effected on the relevant day, *see* Reichsgericht, Juristische Wochenschrift 1907, 6; Kregel in Reichsgerichtsrätekommentar, *loc. cit.*, § 1221, note 2; Damrau in Münchener Kommentar zum Bürgerlichen Gesetzbuch, *loc. cit.*, § 1221, note 1; Staudinger/Wiegand, *loc. cit.*, § 1221, note 2. Official or unofficial quotations provided by a screen service for the purpose of trading in the over-the-counter markets may be taken into account if the quoted prices meet the aforementioned requirements, *cf.* Staudinger/Olzen, *loc. cit.*, § 385, note 2; Soergel/Zeiss, *loc. cit.*, § 385, note 1.

(2) The Transfer of Ownership (Co-ownership) for Security Purposes

The rules regarding collateral arrangements in the form of a transfer of ownership (co-ownership) for purposes of security are not set forth in the Civil Code or any other German statute, but have been developed by court precedent and legal doctrine because of the need for a security interest which, contrary to the pledge, may be non-possessory. The arrangement involves a full transfer of ownership subject to fiduciary responsibilities of the transferee as a consequence of the limited, *i.e.* security, purpose of the transfer. Possession of the asset transferred may remain, and regularly remains, with the transferor, or may be transferred to the transferee. The details of the legal relationship between the transferor and the transferee may, as a matter of principle, be freely negotiated, including the rules applicable in the event of the realization (enforcement) of the asset transferred. Similarly as in the case of a pledge, the priority rights of the transferee are solely determined by the time of the transfer of ownership. Such transfer may also be made, as in the case of a pledge, to secure a future or conditional obligation.

(3) Assignment of a Claim for Security Purposes

This type of collateral arrangement is available when the asset to be assigned constitutes a claim, such as, in respect of Securities, the claims arising from a non-negotiable registered bond or, in a wider context, the claims arising under a cash or securities deposit for the payment or repayment of Cash or the delivery or redelivery of Securities. Similarly as in the case of a transfer for security purposes, an assignment for security purposes involves a full assignment, subject to certain responsibilities of the assignee arising from the limited purpose of the assignment.

(4) Outright Transfer

Collateral arrangements having the effect of an outright transfer of ownership as perceived by the Transfer Annexes, are recognized in German law. With respect to Financial Collateral Arrangements, § 1(17), 1st sentence, of the Banking Act specifically addresses such arrangements in the form of Title Transfer Financial Collateral Arrangements.

The transfer of ownership or a co-ownership interest under German law in respect of bearer Securities requires (i) an agreement between the transferor and the transferee to transfer ownership or a co-ownership interest in such Securities to the transferee and (ii) the transfer of possession of such Securities (§§ 929-931 of the Civil Code).[63]

Regarding the transfer of possession, consideration need here be given only to the transfer of ownership in such Securities the transfer of ownership of which is governed by German law according to German conflict of laws rules described in E.I.(A) above. Ownership in such Securities takes the form of co-ownership interests in a given issue of such Securities held in a CSD. As discussed in the case of the creation of a pledge (*see* E.II.(B)(1)(b) above),

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63 The transfer of possession may, *inter alia*, be effected by transfer of physical control (direct possession, § 929 of the Civil Code) or may be substituted by a custodial relationship in respect of the collateral between the transferee and the transferor (as custodian) who retains direct possession (§ 930 of the Civil Code).

while the relevant CSD maintains direct possession over the Securities, any bondholder maintains indirect possession either through the CSD directly (if the bondholder maintains an account with the CSD and the relevant Securities are credited to such account) or indirectly through an intermediary depositary (if the relevant Securities are credited to the bondholder's securities account with an intermediary depositary, including a CSD). Subject to certain refinements, effective transfer of possession in the co-ownership interest of such Securities occurs by debiting the account of the transferor with the CSD or an intermediary depositary for the Securities to be transferred and crediting such Securities to the account of the transferee with the CSD or an intermediary depositary, by which acts the transferor loses (indirect) possession and the transferee acquires (indirect) possession over the co-ownership interests to be transferred.[64]

No transfer of a co-ownership interest will occur, however, if the chain of intermediary depositaries through which the Securities are held includes a securities depositary which does not hold possession of the Securities for its depositors, but merely purports to owe a contractual claim to each of its depositors to deliver Securities standing to their credit. In such event (indirect) possession would be wanting and any transfer of a co-ownership interest of the transferor would not be effective. The position is similar as in the case of the creation of a pledge in the co-ownership interest in such Securities (*see* E.II.(B)(1)(b) above).

(5) Outright Assignment

This type of collateral arrangement is available when the assets to be assigned constitute claims arising from a non-negotiable Securities. As in the case of an outright transfer, collateral arrangements having the effect of an outright, *i.e.*, non-fiduciary, assignment (*Abtretung*) of such claims are recognized in German law and involve a full assignment of the relevant claims.

(C) Collateral Arrangements in Respect of Cash

German law provides for the following types of collateral arrangements in respect of Cash:

(i) the pledge (*Pfandrecht*) of the claim for the payment of money against the bank with which the account is held on which the Cash is credited;

(ii) the assignment of such claim for security purposes (*Sicherungsabtretung*); and

(iii) the outright assignment (*Abtretung*) of such claim.

A pledge of Cash which has been transferred by or on behalf of the payor to a bank account maintained by the payee as contemplated by Paragraph 12(i) ("Transfer") of the 1994 NY Annex and Paragraph 4(b)(i) of the 1995 Deed is inconceivable in German law. In the event of a funds transfer from one account to another, the payor initially has a claim against his bank arising under the account relationship in respect of the amount of money being transferred. This

64 Such a transfer of ownership is based on § 929, 1st sentence, of the Civil Code. *See* Bundesgerichtshof, Neue Juristische Wochenschrift 1959, 1536; Heinsius/Horn/Than, *loc. cit.*, § 6, notes 35, 84 *et seq.*, 92 *et seq.*; Klanten in Schimansky/Bunte/Lwowski, *loc. cit.*, § 72, note 104; Rögner, in Scherer, Depotgesetz, *loc.cit.*, § 6 note 6.

claim is discharged when such amount has been paid out. Upon receipt of the funds in the recipient's account, such recipient has a claim against his bank in respect of such amount. Any such payment claims may only be subject to one of the types of collateral arrangements mentioned under (i) to (iii) above.

(1) Pledge

As a rule, a pledge over a claim, including a claim for the payment of money, is created (i) by agreement between pledgor and pledgee to grant a pledge for the benefit of the pledgee and (ii) by giving notice thereof to the debtor of the claim (§§ 1274(1), 1280 of the Civil Code). No pledge may be made in respect of claims which cannot be disposed of as a matter of law (§ 1274(2) of the Civil Code). Also future or conditional claims may be subject to a pledge, provided, however, that such claims are identifiable at the time of the pledge. Pursuant to § 1256(1) of the Civil Code, the pledge will cease to operate as a matter of law if the pledgee holds or acquires title to the collateral.

To the extent that a claim has a stock exchange or market price, the rules set out above (*see* E.II.(B)(1)(d)) regarding the enforcement of a pledge of securities under § 1259 of the Civil Code apply *mutatis mutandis* to a pledge of such claim (§ 1279, 2nd sentence, of the Civil Code).

(2) Assignment

As a general rule, a claim may be assigned by agreement between the holder thereof and a third party. The giving of notice to the debtor is not required. A future or conditional claim may also be assigned, provided, however, that such claim is identified at the time of the assignment. If the holder of a claim assigns the claim to the debtor, the claim will be extinguished as a result of such assignment.[65]

If an assignment is made for security purposes, assignor and assignee may stipulate to what extent the assignee is authorized to reassign, pledge or otherwise dispose of the claim. However, as a matter of law, a reassignment or other form of disposal of the claim will be valid irrespective of whether or not the assignor has authorized the assignee to do so.

(D) Types of Financial Collateral Arrangements under German law

In relation to Financial Collateral Arrangements which are addressed in this Memorandum various, special provisions apply under German statutory rules. These special provisions have been inserted in the law in order to implement the EC Collateral Directive in Germany and aim at enhancing legal certainty in relation to Financial Collateral Arrangements.

Pursuant to § 1(17), 1st sentence, of the Banking Act (*see* B.1.(a) above), the term "Financial Collateral Arrangement" comprises:

65 Bundesgerichtshof, BGHZ 48, 219; Palandt/Grüneberg, *loc. cit.*, Introduction to § 362, note 4.

(i) Security Financial Collateral Arrangements which are defined in Article 2(1)(c) of the EC Collateral Directive[66] as arrangements under which a collateral provider provides financial collateral by way of security in favor of, or to, a collateral taker, and where the full ownership of the financial collateral remains with the collateral provider when the security right is established;

(ii) Title Transfer Financial Collateral Arrangements which are defined in Article 2(1)(b) of the EC Collateral Directive[67] as arrangements, including repurchase agreements, under which a collateral provider transfers full ownership of financial collateral to a collateral taker for the purpose of securing or otherwise covering the performance of relevant financial obligations; and

(iii) with respect to Cash only, arrangements under which a collateral provider provides financial collateral by way of payment of money from one account to another.

(1) Security Financial Collateral Arrangements

In respect of all collateral arrangements discussed under E.II.(B) and (C) above, only the pledge (*Pfandrecht*) (i) of ownership (or co-ownership) rights in negotiable Securities, (ii) of claims arising from non-negotiable Securities and (iii) of the claim for the payment of money against the bank with which the account is held on which Cash is credited qualifies as being the subject of a Security Financial Collateral Arrangement.

(2) Title Transfer Financial Collateral Arrangements

The outright transfer of ownership (or co-ownership) rights in negotiable Securities and the outright assignment (*Abtretung*) of claims arising from non-negotiable Securities qualify as being the subject of a Title Transfer Financial Collateral Arrangement.

It is not free from doubt whether (i) the transfer of ownership (or co-ownership) rights in negotiable Securities for security purposes (*Sicherungsübereignung*) and (ii) the assignment of claims arising from non-negotiable Securities for security purposes (*Sicherungsabtretung*) qualify for being entered into under a Title Transfer Financial Collateral Arrangement. Although the collateral provider transfers full ownership of the relevant Securities to the collateral taker, the collateral taker, as set out under E.II.(B)(2) above, is subject to fiduciary responsibilities as a consequence of the security purpose of the transfer according to which, *inter alia*, the collateral taker is obliged to return the very Securities transferred rather than equivalent Securities. Under the EC Collateral Directive only such collateral arrangements under which the collateral taker has a right to use over the Securities and no obligation to retransfer the same Securities that are

66 The term "Security Financial Collateral Arrangement" is not defined in § 1(17), 1st sentence, of the Banking Act. However, this provision has been introduced in the Banking Act in order to implement the EC Collateral Directive in German law (*see* B.1 above). Consequently, the term "Security Financial Collateral Arrangement" as used in § 1(17), 1st sentence, of the Banking Act may be interpreted in line with the definition provided in Article 2(1)(c) of the EC Collateral Directive.

67 What has been said in the preceding footnote, applies likewise to the interpretation of the term "Title Transfer Financial Collateral Arrangement".

transferred to him appear to qualify as Title Transfer Financial Collateral Arrangements (*cf.* Article 6(2) of said Directive).

However, according to the report of the Government submitting the Bill of the act implementing the EC Collateral Directive in German law (*Begründung des Gesetzesentwurfs der Bundesregierung)*[68] it appears that the legislature intended to include these types of collateral arrangements under German law into the scope of application of the rules on Title Transfer Financial Collateral Arrangements. Any precedent of a German court or any developed rule of German law does not exist in respect of this issue.

(3) Financial Collateral Arrangements in respect of Cash

It is uncertain whether or not German law allows for Title Transfer Financial Collateral Arrangements in respect of Cash. The definition of Title Transfer Financial Collateral Arrangements in Article 2(1)(b) of the EC Collateral Directive refers solely to arrangements where a collateral provider transfers full ownership of financial collateral to a collateral taker. In concepts of German law a sum of money placed or kept in an account with a bank does not convey ownership rights to the account holder, but merely a contractual claim of the account holder against his bank. Accordingly, an account holder originating a funds transfer has no "ownership" in the Cash standing to his credit in the account from which the transfer is made, but holds a contractual claim against the bank for payment of money. Similarly, the recipient of a funds transfer does not obtain "ownership" in the funds credited upon the transfer to his account, but holds a contractual claim against his bank for payment of money in amount equal to the sum that has been credited to his account. Accordingly, a transfer of ownership in Cash, as referred to in the definition of Title Transfer Financial Collateral Arrangements is inconceivable in German law.

To clarify this uncertainty § 1(17) of the Banking Act containing the definition of "Financial Collateral Arrangements" has been amended subsequently to the implementation of the EC Collateral Directive in Germany and now expressly states that the transfer of funds to an account held by the Collateral Taker falls within the scope of application of the rules on Financial Collateral Arrangements..

III.
VALIDITY AND ENFORCEMENT OF COLLATERAL ARRANGEMENTS IN INSOLVENCY PROCEEDINGS

The following outlines the principles of German insolvency laws with respect to the validity and enforcement of a collateral arrangement entered into under the Credit Support Documents in the case of insolvency proceedings instituted in Germany against an entity incorporated or otherwise organized in Germany (the "**German Party**").

68 Bundestag-Drucksache 15/1853, p. 12.

(A) General

(1) Applicable Law - Conflicts of Laws

Since 2002, German international insolvency laws have undergone fundamental changes. These changes have evolved in several steps.

Prior to May 31, 2002, German international insolvency laws consisted of some fragmentary insolvency conflict rules which were only set out in Article 102 of the Introductory Code to the Insolvency Code of October 5, 1994, as amended (*Einführungsgesetz zur Insolvenzordnung* - "**Introductory Code to the Insolvency Code**").

On May 31, 2002, the 2000 Insolvency Regulation came into force in all EC Member States except Denmark[69] (each such State, a "**Regulation State**").[70] The 2000 Insolvency Regulation contains conflict rules for insolvencies having a cross-border effect in a Regulation State. The 2000 Insolvency Regulation *ipso iure* forms part of the insolvency laws in all of the Regulation States, including Germany. Insofar as the 2000 Insolvency Regulation applies, it has replaced the conflict rules set out in Article 102 of the Introductory Code to the Insolvency Code. Thus, as from May 31, 2002, German international insolvency laws was governed by two separate bodies of law, one contained in Article 102 of the Introductory Code to the Insolvency Code, the other in the 2000 Insolvency Regulation.

After May 31, 2002, Germany was presented with two tasks: It had to facilitate the rule of the 2000 Insolvency Regulation, mainly by enacting provisions regarding the courts that were to have competence in matters governed by the 2000 Insolvency Regulation, and it had to transform into German law two EC directives, namely (i) Directive 2001/24/EC of the European Parliament and of the Council of April 4, 2001 on the reorganization and winding up of credit institutions[71], as amended, ("**Directive on the Winding up of Credit Institutions**") and (ii) Directive 2001/17/EC of the European Parliament and of the Council of March 19, 2001 on the reorganization and winding up of insurance undertakings[72], as amended, ("**Directive on the Winding up of Insurance Undertakings**"). In connection with the implementation of these directives, Germany resolved to enact more comprehensive conflict rules regarding insolvencies not covered by the 2000 Insolvency Regulation which were until then governed by the rules of Article 102 of the Introductory Code to the Insolvency Code. The Act on the Regulation of International Insolvency Laws (*Gesetz zur Neuregelung des Internationalen Insolvenzrechts*) which came into force on March 20, 2003 accomplishes all of these tasks. It provides the conflict rules regarding insolvencies not covered by the 2000 Insolvency Regulation in §§ 335 to 358 of the Insolvency Code.

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69 *Cf.* recital 33 of the 2000 Insolvency Regulation.

70 The 2000 Insolvency Regulation applies to Insolvency Proceedings opened after its entry into force (Article 43 of the 2000 Insolvency Regulation).

71 Official Journal no. L 125 of May 5, 2001, pp. 15 *et seq.*

72 Official Journal no. L 110 of April 20, 2001, pp. 28 *et seq.*

With effect as from June 26, 2017, the 2000 Insolvency Regulation has been repealed and replaced by the 2015 Insolvency Regulation. The 2015 Insolvency Regulation applies to insolvency proceedings opened after June 26, 2017 (Article 84(1), first sentence, of the 2015 Insolvency Regulation). The 2000 Insolvency Regulation continues to apply to insolvency proceedings which fall within the scope of the 2000 Insolvency Regulation and which have been opened before 26 June 2017 (Article 84(2) of the 2015 Insolvency Regulation).

As a result, the German international insolvency laws are currently contained in (i) the Insolvency Regulations and (ii) §§ 335 to 358 of the Insolvency Code. Accordingly, there exist now two distinct legal regimes of German international insolvency law, each of them applying to specified entities and with respect to different cross-border scenarios and containing varying conflict rules.

(a) The Insolvency Regulations

The Insolvency Regulations apply to Insolvency Proceedings (as defined under E.III.(A)(2) below)[73] opened against a Regulation Debtor (as defined below) insofar as they have a cross-border effect in a Regulation State. Insofar as such proceedings have a cross-border effect in a State which is not a Regulation State, the provisions on international insolvency law set out in §§ 335 to 358 of the Insolvency Code apply (*see* under E.III.(A)(1)(b) below).

(i) Regulation Debtor

The Insolvency Regulations apply to any debtor (hereinafter referred to as "**Regulation Debtor**"):

(i) which has the center of its main interests situated within the territory of a Regulation State[74] which, in the case of a company or legal person, is presumed to be the place of its registered office (Article 3(1), 2nd sentence, of the 2000 Insolvency Regulation and Article 3(1), third sentence, of the 2015 Insolvency Regulation[75]); and

(ii) which is not a Financial Institution.

"**Financial Institution**" means

(a) with respect to the 2000 Insolvency Regulation in accordance with Article 1(2) of the 2000 Insolvency Regulation and in circumstances where the 2000 Insolvency Regulation is applicable:

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73 Insolvency Proceedings under German law are listed in Annex A of the Regulation and, thus, qualify for application of the Regulation (Article 1(1), 2(a)).

74 *Cf.* Article 3(1), 1st sentence, of the 2000 Insolvency Regulation.

75 With respect to the 2015 Insolvency Regulation this presumption shall only apply if the registered office has not been moved to another EU Member State within the 3-month period prior to the request for the opening of insolvency proceedings (Article 3(1), fourth sentence, of the 2015 Insolvency Regulation).

(1) a *credit institution within* the meaning as described under B.1.(b)(i)(1) above;

(2) *an investment undertaking which provides services involving the holding of funds or securities for third parties* within the meaning as described under B.1.(b)(i)(2) above;

(3) a *collective investment undertaking* within the meaning as described under B.1.(b)(i)(6) above;[76] nor

(4) an *insurance undertaking* within the meaning of Article 13(1) of the Directive 2009/138/EC of the European Parliament and of the Council of 25 November 25, 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast), as amended, , *i.e.*, a direct life or non-life insurance undertaking which has received authorization in accordance Article 14 of said Directive ("**Insurance Undertaking**"); and

(b) with respect to the 2015 Insolvency Regulation in accordance with Article 1(2) of the 2015 Insolvency Regulation and in circumstances where the 2015 Insolvency Regulation is applicable:

(1) an insurance undertaking as referred to under (a)(2) above;

(2) a credit institution as referred to under (a)(1) above;

(3) an investment firm and other firm, institution and undertaking to the extent that it is covered by the Directive on the Winding up of Credit Institutions, *i.e.*,

(i) an investment firm as defined in Article 4(1) no. 2 of the EU Banking Regulation which is in accordance with Article 4(1) no. 1 of the Council Directive 2004/39/EC of April 21, 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC, as amended, any legal person the regular occupation or business of which is the provision of one or more investment services to third parties and/or the performance of one or more

76 It is the general view that, despite the term "collective investment undertaking" used in Article 1(1) and (2) of the 2000 Insolvency Regulation, the 2000 Insolvency Regulation refers by such term to undertakings for collective investment in transferable securities (*i.e.*, UCITS) within the meaning of Article 1(2) of the UCITS Directive. This issue is not relevant in the context of this Memorandum since we do not consider herein the validity and enforceability of Credit Support Documents in circumstances where the Collateral Provider is a Capital Management Company within the meaning of § 17(1) of the Capital Investment Code managing segregated pools of assets (*Sondervermögen*) within the meaning of § 1(10) of the Capital Investment Code and acting for the account of such segregated pool of assets (*Sondervermögen*), *see* B.2.a above.

investment activities, each as listed in Section A of Annex I relating to any of the instruments listed in Section C of Annex I of said Directive, on a professional basis, except for

(aa) a local firm, *i.e.*, a firm dealing for its own account on markets in financial futures or options or other derivatives and on cash markets for the sole purpose of hedging positions on derivatives markets, or dealing for the accounts of other members of those markets and being guaranteed by clearing members of the same markets, where responsibility for ensuring the performance of contracts entered into by such a firm is assumed by clearing members of the same markets; and

(bb) a firm which is not authorized to provide the safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash/collateral management, which provide only one or more of certain investment services and activities,[77] and which are not permitted to hold money or securities belonging to their clients and which for that reason may not at any time place themselves in debt with those clients; and

(ii) financial institutions, firms and parent undertakings falling within the scope of the EU Bank Recovery and Resolution Directive ("**BRRD**")[78] in the form of

(aa) financial institutions that are established in the European Union when the financial institution is a subsidiary of a credit institution or investment firm, or of a company referred to in points (ii) to (viii), and is covered by the supervision of the parent undertaking on a consolidated basis in accordance with Articles 6 to 17 of the EU Banking Regulation;

(bb) financial holding companies as defined in Article 4(1) no. 20 of the EU Banking Regulation;

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77 These investment services and activities are (1) the reception and transmission of orders in relation to one or more financial instruments; (2) the execution of orders on behalf of clients; (3) portfolio management; and (4) investment advice.

78 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 and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council, as amended.

(cc) mixed financial holding companies as defined in Article 4(1) no. 21 of the EU Banking Regulation;

(dd) mixed-activity holding companies that are established in the European Union as defined in Article 4(1) no. 22 of the EU Banking Regulation;

(ee) parent financial holding companies in a Member State as defined in Article 4(1) no. 30 of the EU Banking Regulation;

(ff) Union parent financial holding companies as defined in Article 4(1) no. 31 of the EU Banking Regulation;

(gg) parent mixed financial holding companies in a Member State as defined in Article 4(1) no. 32 of the EU Banking Regulation; or

(hh) Union parent mixed financial holding companies as defined in Article 4(1) no. 33 of the EU Banking Regulation; or

(4) a collective investment undertaking which term includes pursuant to Article 2(1) of the 2015 Insolvency Regulation (i) UCITS and (ii) alternative investment funds (AIFs) as defined in Article 4(1) item (a) of the Directive 2011/61/EU of the European Parliament and of the Council of June 8, 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010, as amended.

(ii) Cross-border Effect in a Regulation State

The Insolvency Regulations apply to Insolvency Proceedings opened against a Regulation Debtor insofar as such proceedings have a cross-border effect in a Regulation State.[79] This is the case if the Regulation Debtor has assets which are situated in the territory of at least one other Regulation State.[80] With respect to the *situs* of assets, Article 2(g) of the 2000 Insolvency Regulation and Article 2(9)(viii) of the 2015 Insolvency Regulation provide that:

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79 This is an implied requirement. However, it is reflected in various provisions of the 2000 Insolvency Regulation (*see*, for example, Articles 16(1) and 27(1)). *Cf.* Reinhart, in Münchener Kommentar zur Insolvenzordnung, 2003, Article 1 EUInsVO, notes 8 *et seq.*; Duursma-Kepplinger *et al.* (ed.), Europäische Insolvenzverordnung, 2002, Article 1, notes 2 *et seq.*; Smid, Deutsches und Europäisches Internationales Insolvenzrecht, 2004, p. 20. Only Huber, Zeitschrift für Zivilprozeß 114 (2001), 133, 138 takes the view that any cross-border effect shall be sufficient for the application of the 2000 Insolvency Regulation, irrespective of whether it takes place in a Regulation State.

80 It is not free from doubt whether a cross-border effect in a Regulation State may also be constituted through other links, *e.g.*, contracts governed by foreign law to which the insolvent debtor is a party (*cf.* Reinhart, in Münchener Kommentar zur Insolvenzordnung, *op. cit.*, notes 12 *et seq.*).

(i) tangible property shall be considered to be situated in the EC Member State within the territory of which the property is situated;

(ii) property and rights ownership of or entitlement to which must be entered in a public register shall be considered to be situated in the EC Member State under the authority of which the register is kept; and

(iii) claims shall be considered to be situated in the EC Member State within the territory of which the third party required to meet them has the centre of his main interests. In the case of a company or legal person, this is presumed to be the place of its registered office (Article 3(1), 2nd sentence, of the 2000 Insolvency Regulation and Article 3(1), third sentence, of the 2015 Insolvency Regulation.[81]).

The above rules do not provide guidance where Immobilized Securities or Dematerialized Securities are considered to be situated for the purposes of the Insolvency Regulations. Any court precedent or any developed rule of German law does not exist with respect to this issue.

(iii) Applicable Insolvency Conflict Rules

Under the Insolvency Regulations, the laws applicable to insolvency proceedings and their effects are those of the Regulation State within the territory of which such proceedings are opened (*lex fori concursus*) (Article 4(1) of the 2000 Insolvency Regulation and Article 7(1) of the 2015 Insolvency Regulation). Pursuant to Article 4(2), 2nd sentence, of the 2000 Insolvency Regulation and Article 7(2) of the 2015 Insolvency Regulation the *lex fori concursus* determines, *inter alia*, the assets which form part of the estate, the respective powers of the debtor and the liquidator, the effects of insolvency proceedings on current contracts to which the debtor is party, the claims which are to be lodged against the debtor's estate, the rules governing the lodging, verification and admission of claims, the rules governing the distribution of proceeds from the realization of assets, the ranking of claims and the rights of creditors who have obtained partial satisfaction after the opening of insolvency proceedings by virtue of a right *in rem* or through a set-off and the rules relating to the voidness, voidability or unenforceability of legal acts detrimental to all the creditors.

However, the general principle set out in Article 4(1) of the 2000 Insolvency Regulation and Article 7(1) of the 2015 Insolvency Regulation (as further detailed in Article 4(2) of the 2000 Insolvency Regulation and Article 7(2) of the 2015 Insolvency Regulation) is qualified by certain exceptions. Article 5(1) of the 2000 Insolvency Regulation and Article 8(1) of the 2015 Insolvency Regulation provide for an exception in respect of rights *in rem* of creditors and third parties. It sets forth that the opening of insolvency proceedings does not affect the rights *in rem* of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets belonging to the Regulation Debtor which are situated within the territory of another EC Member State at the time of the opening of such proceedings.

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81 With respect to the 2015 Insolvency Regulation this presumption shall only apply if the registered office has not been moved to another EU Member State within the 3-month period prior to the request for the opening of insolvency proceedings (Article 3(1), fourth sentence, of the 2015 Insolvency Regulation).

Rights *in rem* for the purposes of these provisions are pursuant to Article 5(2) of the 2000 Insolvency Regulation and Article 8(2) of the 2015 Insolvency Regulation in particular:

(i) the right to dispose of assets or have them disposed of and to obtain satisfaction from the proceeds of or income from those assets, in particular by virtue of a lien or a mortgage;

(ii) the exclusive right to have a claim met, in particular a right guaranteed by a lien in respect of the claim or by assignment of the claim by way of a guarantee; and

(iii) the right to demand the assets from, and/or to require restitution by, anyone having possession or use of them contrary to the wishes of the party so entitled.

It is disputed whether Article 5(1) of the 2000 Insolvency Regulation and Article 8(1) of the 2015 Insolvency Regulation refer to the law of the EC Member State where the assets belonging to the Regulation Debtor are situated (including the substantive insolvency law of such jurisdiction)[82] or whether it provides that assets belonging to the Regulation Debtor which are situated within the territory of another EC Member State at the time of the opening of insolvency proceedings shall not be affected by any substantive insolvency laws.[83]

(b) §§ 335 to 358 of the Insolvency Code

The provisions on international insolvency law set out in §§ 335 to 358 of the Insolvency Code apply to Insolvency Proceedings insofar as the Insolvency Regulations do not apply.[84]

Accordingly, these rules apply to Insolvency Proceedings:

(i) over the assets of a Financial Institution; or

(ii) over the assets of a Regulation Debtor, provided that the proceedings do not have a cross-border effect in any Regulation State, but in a State which is not a Regulation State.

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82 Fritz/Bähr, Deutsche Zeitschrift für Wirtschaftsrecht 2001, 228; Prütting, Zeitschrift für Wirtschaftsrecht 1996, 1277, 1287; Flessner, Praxis des Internationalen Privat- und Verfahrensrechts 1997, 1, 7 *et seq.*; Lehr, Zeitschrift für Konkurs-, Treuhand- und Schiedsgerichtswesen 2000, 577, 580; Paulus, Europäisches Wirtschafts- und Steuerrecht 2002, 497, 499 *et seq.*; von Bismarck/Schümann-Kleber, Neue Zeitschrift für das Recht der Insolvenz und Sanierung 2005, 147, 148 et seq.

83 Taupitz, Zeitschrift für Zivilprozeß 111 (1998), 315, 334; Leible/Staudinger, Zeitschrift für Konkurs-, Treuhand- und Schiedsgerichtswesen 2000, 551; Duursma-Kepplinger/Duursma/Chalupsky, *loc. cit.*, Art. 5 note 18 *et seq.*; Trunk, Internationales Insolvenzrecht, 1998, p. 429; Liersch, Neue Zeitschrift für das Recht der Insolvenz und Sanierung 2002, 15, 16.

84 This is not expressly provided in §§ 335 to 358 of the Insolvency Code. However, pursuant to Article 288(2) of the Treaty on the Functioning of the European Union, an EU regulation shall have general application and shall be binding in its entirety and directly applicable in all Member States. Any such regulation that conflicts with a provision of German law takes priority over such provision, even if such provision was enacted later than such regulation (Nettesheim in Grabitz/Hilf, Das Recht der Europäischen Union, Volume III, Article 288, notes 47 *et seq.*).

(i) Cross-border Effect in a Regulation State

As discussed above (VII.(B)(2)(b)), Insolvency Proceedings have a cross-border effect in a Regulation State if the counterparty to the German Party has the center of its main interests situated within the territory of a Regulation State other than Germany. Therefore, the conflict rules set out in §§ 335 to 358 of the Insolvency Code apply if the counterparty to the German Party has the center of its main interests situated in a State which is not a Regulation State.

The conflict rules of §§ 335 to 358 of the Insolvency Code make no express provision of whether or not these rules only apply where Insolvency Proceedings over the assets of the German Party have an international (or cross-border) nexus and, if so, which factual elements would constitute such an international nexus. Arguably, an international (or cross-border) nexus for the purposes of these rules does already exist where a contract to which the insolvent debtor is a party is governed by foreign law.[85] Any precedent of a German court or any developed rule of German law does not exist in this regard.

(ii) Applicable Insolvency Conflict Rules

Where the conflict rules of §§ 335 to 358 of the Insolvency Code apply, § 335 of the Insolvency Code contains substantially the same general principle as Article 4(1) of the 2000 Insolvency Regulation and Article 7(1) of the 2015 Insolvency Regulation according to which the laws applicable to insolvency proceedings and their effects are those of the State within the territory of which such proceedings are instituted (*lex fori concursus*).

However, the conflict rules of §§ 335 to 358 of the Insolvency Code do not contain a general exception in respect of rights *in rem* of creditors and third parties comparable to the exception provided for in Article 5(1) of the 2000 Insolvency Regulation and Article 8(1) of the 2015 Insolvency Regulation.[86] Solely with respect to foreign insolvency proceedings, § 351(1) of the Insolvency Code provides that the rights of a third party in respect of assets forming part of the insolvent debtor's estate which are situated within Germany at the time of the opening of such foreign insolvency proceedings and which entitle such third party to segregation (*Aussonderung*) or separate liquidation (*Absonderung*) shall not be affected by the opening of the foreign insolvency proceedings.

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85 Stephan, in Heidelberger Kommentar zur Insolvenzordnung, 7th ed., 2014, before §§ 335 *et seqq.* note 2; Reinhart, in Münchener Kommentar zur Insolvenzordnung, *op. cit.*, introduction to Article 102 EGInsO, notes 1 and 3.

86 Article 21(1) of the Directive on the Winding up of Credit Institutions and Article 20(1) of the Directive on the Winding up of Insurance Undertakings provide that that opening of reorganization measures or winding-up proceedings in respect of credit institutions and insurance undertakings (each as defined in said Directives) shall not affect the rights *in rem* of creditors or third parties in respect of tangible or intangible, movable or immovable assets - both specific assets and collections of indefinite assets as a whole which change from time to time - belonging to such credit institutions or insurance undertakings which are situated within the territory of another EC Member State at the time of the opening of such measures or proceedings. These provisions have not been implemented in Germany.

(2) Institution of Insolvency Proceedings in Germany

Insolvency Proceedings (*Insolvenzverfahren* - "**Insolvency Proceedings**") in Germany may take the form of: (i) winding up proceedings, which result in the complete liquidation of the insolvent entity and the realization of its assets; (ii) composition proceedings (*Insolvenzplanverfahren*) which serve to reduce the insolvent's liabilities in order to allow the insolvent to remain in business and rehabilitate its economic potential; and (iii) proceedings of self-management (*Eigenverwaltung*) which are not administered by a receiver, but by the insolvent debtor under the supervision of a trustee acting on behalf of the creditors.[87]

Insolvency Proceedings may be instituted[88] in Germany as main proceedings or as secondary proceedings affecting only the assets of a debtor which are situated in Germany.[89]

(a) Main Insolvency Proceedings

Insolvency Proceedings may be instituted in Germany as main proceedings affecting all assets of a German party subject to secondary insolvency proceedings in other jurisdictions:

(i) in the case of a German party where the proceedings have a cross-border effect in another Regulation State, over the assets of an entity having the center of its main interests situated within Germany (§ 3(1) of the Insolvency Regulations)[90]; or

(ii) in the case of (i) a German Financial Institution or (ii) a German party where the proceedings do not have a cross-border effect in another Regulation State, over the assets of any entity which has its principal office (*i.e.*, the center of its business activity (*Hauptniederlassung*)) or, in the absence of a principal office, its registered office (*Sitz*) in Germany (§ 3(1) of the Insolvency Code in connection with §§ 12 *et seq.* of the Civil Procedure Act (*Zivilprozeßordnung* - "**Civil Procedure Act**")).

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87 What will be said below in respect of the receiver applies *mutatis mutandis* to the insolvent debtor in the case of proceedings of self-management.

88 The term "to institute" or "institution" as used in this Memorandum with respect to Insolvency Proceedings means the granting by the competent court of a petition for such proceedings. The term "to open" or "opening" as used in this Memorandum with respect to matters governed by, and consistent with, the Insolvency Regulations has with respect to Insolvency Proceedings under German law the same meaning as the term "to institute" or "institution" as used herein.

89 The terms "main insolvency proceedings" and "secondary insolvency proceedings" used in this paragraph are the terms used in the Insolvency Regulations (*cf.* Article 3(3), first sentence and Article 27, first sentence, of the 2000 Insolvency Regulation and Article 3(3) and (4) of the 2015 Insolvency Regulation). However, these terms designate different types of proceedings having different prerequisites depending on whether the Insolvency Regulations or the conflict rules contained in the Insolvency Code apply.

90 Pursuant to Article 3(1), 2nd sentence, of the 2000 Insolvency Regulation and Article 3(1), third sentence, of the 2015 Insolvency Regulation, in the case of a company or legal person, the place of the registered office shall be presumed to be the center of its main interests in the absence of proof to the contrary. With respect to the 2015 Insolvency Regulation this presumption shall only apply if the registered office has not been moved to another EU Member State within the 3-month period prior to the request for the opening of insolvency proceedings (Article 3(1), fourth sentence, of the 2015 Insolvency Regulation).

(b) Secondary Insolvency Proceedings

Subject as set out below, secondary insolvency proceedings may be instituted in Germany:

(i) in the case of a non-German party where the proceedings have a cross-border effect in another Regulation State, over the assets situated in Germany of an entity having the center of its main interests situated in a Regulation State other than Germany, provided that such entity possesses an establishment (that is any place of operations where such entity carries out a non-transitory economic activity with human means and assets[91]) within Germany (Article 3(2) of the Insolvency Regulations); and

(ii) in the case of (i) a non-German Financial Institution or (ii) a non-German party where the proceedings do not have a cross-border effect in a Regulation State, over the assets of any entity which has neither its principal office (*i.e.*, the center of its business activity (*Hauptniederlassung*)) nor, in the absence of a principal office, its registered office (*Sitz*) in Germany and whose assets are situated in Germany (§§ 354(1), 356(1) of the Insolvency Code).

An exception applies to certain types of credit institutions[92] and insurance companies[93] having their registered office within the territory of (i) an EC Member State or (ii) another contracting state of the Agreement on the European Economic Area in respect of which no secondary insolvency proceedings may be instituted in Germany.

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91 Article 2(h) of the 2000 Insolvency Regulation and Article 2(10) of the 2015 Insolvency Regulation.

92 Credit institutions exempted pursuant to § 46e(2) of the Banking Act are CRR credit institutions (*CRR-Kreditinstitute*) having their registered office within the territory of either an EC Member State or another contracting state of the Agreement on the European Economic Area other than Germany. CRR credit institutions are defined, pursuant to § 1(3d), 1st sentence, of the Banking Act, as credit institutions within the meaning of Article 4(1) No. 1 of the EC Banking Regulation, *i.e.*, undertakings whose business is to receive deposits or other repayable funds from the public and to grant credits for their own account.

93 Insurance companies are, pursuant to § 312(3) of the Insurance Supervisory Act, exempted from secondary insolvency proceedings except for (i) branches of insurance companies which have their registered office in a Non-member State (as defined below) and which are required to have a licence to operate in accordance with § 67(1) of the Insurance Supervisory Act and (ii) insurance companies which have their registered office in another EC Member State or another contracting state of the Agreement on the European Economic Area which are not subject to the EC Directive 2009/138/EC and wish to conduct direct insurance business through a branch. For the purposes of (i) above, a "Non-member State" means each State (i) which is neither an EC Member State nor another contracting state of the Agreement on the European Economic Area or (ii) which is a quasi-state administrative entity with independent regulatory powers where the EC law provisions concerning the freedom of movement, of establishment and to provide services do not apply (§§ 7 no. 6, 22 of the Insurance Supervisory Act).

(3) Other Proceedings

(a) Moratorium Proceedings

Credit institutions (*Kreditinstitute*) within the meaning of § 1(1) of the Banking Act,[94] financial services institutions (*Finanzdienstleistungsinstitute*) within the meaning of § 1(1a) of the Banking Act[95] and German branches of entities established outside Germany which are

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94 Credit institutions are undertakings that carry on banking transactions on a commercial basis, or to an extent that necessitates a commercially organized business operation (§ 1(1) of the Banking Act). Banking transactions are: (1) the taking of moneys from others as deposits or other repayable funds of the public, provided that the claim for repayment is not evidenced by a bearer or order bond, irrespective of whether or not interest is paid (deposit business); (2) the business specified in § 1(1), 2nd sentence, of the Mortgage Bond Act (*Pfandbriefgesetz*) (mortgage bond business); (3) the granting of money loans and acceptance credits (credit business); (4) the purchase of bills of exchange and cheques (discount business); (5) the purchase and sale of financial instruments in its own name and for the account of others (financial commissions business); (6) the safe custody and administration of securities for others (safe custody business); (7) the incurring of obligations to acquire claims in respect of loans that have previously been sold prior to their maturity; (8) the granting of sureties, guarantees and other indemnities for others (guarantee business); (9) the processing of cashless cheque collection (cheque collection business) and bills of exchange collection (bills of exchange collection business) and the issuance of traveler cheques (traveler cheque business); (10) the acquisition of financial instruments for its own account for purposes of their placement or the issuance of equivalent guarantees (underwriting business) and (11) the activity as a central counterparty within the meaning of § 1(31) of the Banking Act). A credit institution is not limited in its activities to the above listed types of banking transactions. Under certain narrow circumstances, generally in respect of credit institutions of lesser significance from the viewpoint of prudential supervision, the Financial Services Supervisory Authority may determine that the special rules described under VII.(B)(2) regarding the institution of Insolvency Proceedings, including, *inter alia*, §§ 46 and 46b of the Banking Act, shall not apply.

95 Financial services institutions are undertakings that are not credit institutions, but provide financial services for third parties on a commercial basis, or to an extent that necessitates a commercially organized business operation (§ 1(1a) of the Banking Act). Financial services comprise: (1) the broking of transactions for the purchase and sale of financial instruments or their referral (investment brokerage); (2) the provision of personal recommendations to a client or its representative in respect of one or more transactions relating to specific financial instruments to the extent that the recommendation is based on a verification of the investor's personal circumstances or is presented as being suitable for him and is not exclusively published through information distribution channels or for the public (investment advice); (3) the operation of a multilateral trading facility which brings together multiple third-party buying and selling interests in financial instruments - within the system and in accordance with non-discretionary rules - in a way that results in a contract for purchase of such financial instruments (operating a multilateral trading facility); (4) placing of financial instruments without a firm commitment (placing business); (5) the purchase and sale of financial instruments in the name and for the account of third parties (securities brokerage); (6) the management of individual assets invested in financial instruments for the account of third parties by manager with freedom of judgement (financial portfolio management); (7) (a) the continuous offer of the purchase or sale of financial instruments at an organized market or in a multilateral trading facility at prices quoted by itself, (b) the frequent organized and systematic conduct of trading for its own account outside of an organized market or a multilateral trading facility by way of supplying a system accessible to third persons in order to effect transactions with those persons, (c) the purchase and sale of financial instruments for its own account as a service for third persons or (d) the purchase and sale of financial instruments for its own account as a direct or indirect participant of a national-organized market or a multilateral trading facility by means of a high-frequency algorithmic trading technique characterized by the use of infrastructure which aims for a minimization of latency by the decision of the system regarding the introduction, the production, the forwarding or the implementation of the order without any human intervention for individual transactions or orders as well as by a high undergrounded arise of notification in the form of orders, quotes or cancellations, even without services for third parties (proprietary trading); (8) the arranging of deposit transactions with undertakings having their registered office outside of the

engaged in banking transactions or financial services[96] may become subject in Germany to proceedings of the Federal Financial Services Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* - "**Financial Services Supervisory Authority**") under § 46 of the Banking Act. Essentially the same rules apply under § 42 of the Capital Investment Code of July 4, 2013 (*Kapitalanlagegesetzbuch* – "**Capital Investment Code**") with respect to capital management companies (*Kapitalverwaltungsgesellschaften*), which term comprises, *inter alia*, (i) capital management companies (*Kapitalverwaltungsgesellschaften*) managing segregated pools of assets (*Sondervermögen*) within the meaning of § 1(10) of the Capital Investment Code and (ii) investment stock corporations with variable capital (*Investmentaktiengesellschaft mit veränderlichem Kapital*) within the meaning of § 108 *et seq*. of the Capital Investment Code having no external management company[97].

European Economic Area (third country deposit brokerage); (9) the currency trading (currency exchange business); (10) the ongoing purchase of receivables based on master agreements with or without recourse (factoring); (11) the entry into finance leasing contracts as lessor and the management of property companies within the meaning of § 2(6), first sentence, no. 17 of the Banking Act outside the management of investment assets (*Investmentvermögen*) within the meaning of § 1(1) of the Capital Investment Code (finance leasing); (12) the purchase and sale of financial instruments outside the management of investment assets (*Investmentvermögen*) within the meaning of § 1(1) of the Capital Investment Code for a group of investors all of which are natural persons with freedom of judgement regarding the selection of relevant financial instruments to the extent this is a main feature of the offered product and is carried out with the intent that the investors participate in the performance of the purchased financial instruments (investment management); and (13) the deposit and the management of securities exclusively for alternative investment funds (AIF) within the meaning of § 1(3) of the Capital Investment Code (limited deposit-taking business). Financial services shall also include the purchase and sale of financial instruments for its own account which does not constitute a service for third parties (proprietary transaction); similarly to credit institutions, a financial services institution is not limited in its activities to the above listed types of financial services. Under certain narrow circumstances, generally in respect of financial services institutions of lesser significance from the viewpoint of prudential supervision, the Financial Services Supervisory Authority may determine that the special rules regarding the institution of Insolvency Proceedings described under VII.(B)(2) shall not apply.

96 Article 3(1) of the Directive on the Winding up of Credit Institutions and Article 4(1) of the Directive on the Winding up of Insurance Undertakings provide with respect to "reorganization measures" (which term includes "measures involving the possibility of a suspension of payments", Article 2, seventh indent, of the Directive on the Winding up of Credit Institutions and Article 2(c) of the Directive on the Winding up of Insurance Undertakings) that only the competent authorities of the home Member State of the relevant credit institution or insurance company, as applicable, shall be entitled to decide on such reorganization measures with respect to such institutions. Both directives provide for the same principle with respect to the opening of insolvency proceedings with respect to such institutions (cf. footnotes 93 and 94 above). Whilst the provisions of both directives concerning the opening of insolvency proceedings (Article 9(1) of the Directive on the Winding up of Credit Institutions and Article 8(1) of the Directive on the Winding up of Insurance Undertakings) have been implemented in Germany, the provisions of both directives concerning "reorganization measures", including a payment moratorium, have not been implemented in German law. Accordingly, the Financial Services Supervisory Authority may take measures described in this paragraph also with respect to German branches of those financial institutions which fall under both directives (see, footnotes 93 and 94 above).

97 Capital management companies (*Kapitalverwaltungsgesellschaften*) are undertakings engaged in the administration of domestic investment funds (*inländische Investmentvermögen*), EU investment funds (*EU-Investmentvermögen*) or non-German alternative investment funds (*ausländische AIF*). Domestic investment funds (*inländische Investmentvermögen*) may comprise segregated pools of assets (*Sondervermögen*). If a capital management company enters into derivative transactions for the account of one of the segregated pool of assets (*Sondervermögen*) it manages, it would seem to follow from the applicable statutory provisions that claims arising from such transactions do not qualify for being netted with claims arising from transactions into which the same capital management company enters into for the

Under § 46 of the Banking Act[98], the Financial Services Supervisory Authority may take appropriate action if the fulfilment of the obligations of a credit institution or a financial services institution towards its creditors, in particular if the security of the assets entrusted to such institution, is jeopardized. In particular, the Financial Services Supervisory Authority may: (i) issue directives concerning the management of the institution's operations; (ii) prohibit or restrict the acceptance of deposits and the extension of credits; (iii) prohibit or restrict the managers' administration of the institution; (iv) issue a temporarily order to the institution prohibiting disposals and payments and issue a payment moratorium (the "**Payment Moratorium**"); (v) order the closure of the institution for business with customers; and (vi) prohibit the acceptance of payments not made in satisfaction of debts owed to the institution, unless the competent deposit protection scheme or scheme for the indemnification of investors undertakes to satisfy those entitled in full.

If, prior to the commencement of Insolvency Proceedings, the appropriate insurance supervisory authority determines that an insurance company within the meaning of § 7 no. 33 of the Insurance Supervisory Act will be permanently unable to fulfil its obligations, it may, for purposes of avoiding Insolvency Proceedings, take any appropriate action under § 314 of the Insurance Supervisory Act, including the issuance of a Payment Moratorium.[99]

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account of any other of such segregated pool of assets (*Sondervermögen*) (*cf.* § 93 of the Capital Investment Code.

98 § 46(1) of the Banking Act provides as follows in the relevant part (in English translation):

"(1) If the performance by an institution of its obligations to its creditors, in particular the security of the assets entrusted to it, is jeopardized, or if there is reason to believe that effective supervision of the institution is not possible (§ 33(3) items 1 to 3), the Supervisory Authority may take provisional measures for the purpose of averting such jeopardy. In particular, it may

1. make orders concerning the conduct of the management of the institution's operations,

2. prohibit the acceptance of deposits or moneys or securities from customers and the extension of credits (§ 19(1)),

3. prohibit or limit the owners or managers in the exercise of their functions, and

4. issue a temporarily order to the institution prohibiting disposals and payments;

5. order the closure of the institution for business with customers; and

6. prohibit the acceptance of payments not made in satisfaction of debts owed to the institution, unless the competent deposit protection scheme or scheme for the indemnification of investors undertakes to satisfy those entitled in full.

Resolutions regarding the distribution of profits shall be void to the extent that they contravene action taken pursuant to sentences 1 or 2. With respect to institutions not organized as sole proprietorships, managers who have been prohibited from exercising their functions shall be excluded from the management and representation of the institution for the duration of such prohibition. ... Rights which enable a manager in his capacity as shareholder or partner or in any other manner to take part in decisions regarding management of the institution may not be exercised for the duration of such prohibition."

99 § 314(1) , 1st and 2nd sentence, of the Insurance Supervisory Act provides as follows in the relevant part (in English translation):

If the appropriate supervisory authority proceeds under § 46 of the Banking Act or § 89(1) of the Insurance Supervisory Act and issues a Payment Moratorium, such measure will lead to a temporary impediment to performance (*vorübergehendes Leistungshindernis*) with respect to any payment obligation that is or becomes due during the time of the Payment Moratorium.[100]

However, pursuant to § 46d(3), third sentence, of the Banking Act and § 314 of the Insurance Supervisory Act § 340(2) of the Insolvency Act shall apply *mutatis mutandis* with respect to reorganization measures. According to the application of this provision in the decision of the Federal Court of Justice (*Bundesgerichtshof*) of June 9, 2016,[101] the reference to this provision means that the effects of reorganization measures will be governed by the reorganization and insolvency laws of the State which governs the relevant Agreement, i.e., English or New York reorganization and insolvency laws. It is a matter of such laws whether or not our Memorandum of Law dated September 1, 2017 on the enforceability of close-out netting under the 1987 ISDA Master Agreements, the 1992 ISDA Master Agreements and the 2002 ISDA Master Agreement in German law, as updated from time to time (the "**Netting Memorandum**") close-out netting under the Agreements upon taking of reorganization measures by the competent supervisory authority may take effect in accordance with the relevant Agreement or will be affected by such measures.[102]

(b) Bank Resolution and Reorganization Proceedings

In addition to the proceedings discussed above, in a crisis situation credit institutions and certain other related entities may become subject to resolution or reorganization proceedings in relation to which complex sets of rules apply, each of which addresses different types of entities and different crisis scenarios.

"(1) If it follows from an audit of the business and the financial position of any [insurance company] that such [insurance company] is permanently unable to fulfill its obligations, but it appears that the avoidance of an insolvency proceeding is required in the best interest of the insured, then the supervisory authority may determine by order whatever is necessary to that end, and may in particular require the representatives of the [insurance company] to change the basis of the business or otherwise to cure the deficiencies within a set period of time. All kinds of payments may temporarily be prohibited, including payments under insurance policies to the insured, the distribution of profits, in the case of life insurances also the repurchasing or crediting of insurance policies as well as advances with respect thereto."

The words "insurance company" in the above-quoted text have been put in square brackets because the German text speaks in those places of "enterprises" (*Unternehmen*); such term, however, refers in this context to nothing but insurance companies.

100 *See* BGH WM 2013, 742.

101 BGH NJW 2016, 2328, 2331.

102 Assuming that German law would govern the Agreements and consequently apply to their construction and interpretation, it would be unlikely that a Payment Moratorium under § 46 of the Banking Act or § 89(1) of the Insurance Supervisory Act would constitute an insolvency-related event of default pursuant to Section 5(a)(vii); on the same assumption, however, failure to pay when due because of the imposition of the Payment Moratorium may constitute an event of default pursuant to Section 5(a)(i).

(i) Resolution Proceedings under the SRM Regulation

The EU Single Resolution Board as resolution authority for, in particular, significant EU credit institutions and credit institutions subject to the supervision by the European Central Bank, in cooperation with the German Federal Financial Stabilization Agency (*Bundesanstalt für Finanzmarktstabilisierung* – "**FMSA**"), may proceed in a crisis situation with various resolution measures in accordance with the Single Resolution Mechanism Regulation,[103] including by applying the sale of business tool, the bridge institution tool, the asset separation tool or the bail-in tool. In particular the application of the bail-in tool may have an adverse effect on unsecured creditors' rights. Further, resolution measures may interfere with various provisions of the Agreements

(ii) Resolution Proceedings under the SAG

Where the Single Resolution Mechanism Regulation does not apply, the FMSA may proceed in a crisis situation with various resolution measures in accordance with the German Act on Recovery and Resolution of Institutions and Financial Groups (Recovery and Resolution Act) (*Gesetz zur Sanierung und Abwicklung von Instituten und Finanzgruppen (Sanierungs- und Abwicklungsgesetz)* - "**SAG**") through which the EU Bank Recovery and Resolution Directive (BRRD)[104] has been implemented in Germany. Subject to the SAG are, in particular, certain types of credit institutions and investment firms and related group companies. Under the SAG essentially the same resolution measures as under the Single Resolution Mechanism Regulation may be applied. Accordingly, also such measures may affect creditors' rights and may interfere with various provisions of the Agreements.

(iii) Reorganization Proceedings

In circumstances where the stability of the financial system is endangered credit institutions may become the subject of reorganization proceedings (*Reorganisationsverfahren*) under Act on the Reorganization of Credit Institutions (*Kreditinstitute-Reorganisationsgesetz* - the "**Reorganization Act**").

Such reorganization proceedings may provide the basis to interfere with creditor's rights, in particular by reducing or postponing creditor's claims, as set out in a reorganization plan on which the relevant credit institution's creditors may decide by majority vote subject to court approval. § 13 of the Reorganization Act provides that (i) contractual arrangements with a credit institution which becomes the subject of such proceedings may not be terminated for a period

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103 Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010 (Official Journal no. L 225 of 30 July 2014, pp. 1 *et seq.*).

104 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 and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council.

beginning on the day on which the relevant credit institution institutes the proceedings by giving notice to the Financial Services Supervisory Authority in accordance with § 7 of the Reorganization Act until the end of the following business day and (ii) the occurrence of events of default or termination events are postponed until the end of this period. Where § 13 of the Reorganization Act applies to a German credit institution that is party to a 1992 ISDA Master Agreement or a 2002 ISDA Master Agreement, such application may prevent any automatic termination based on Section 5(a)(vii)(4) of the 1992 ISDA Master Agreements or on Section 5(a)(vii)(4) of the 2002 ISDA Master Agreement being effective until the end of the period described above. The same applies with respect to the designation of an Early Termination Date under an Agreement[105] It is, however, uncertain whether, and to which extent, § 13 of the Reorganization Act will affect contractual arrangements governed by a law other than German law. At present, there is no available legal authority on this issue. Given the legislative intent of § 13 of the Reorganization Act, we believe that this provision aims to interfere with all contractual arrangements of the relevant credit institution, irrespective of their governing law. However, it is for the law governing the relevant contractual arrangement (*i.e.*, in respect of a 1992 ISDA Master Agreement or a 2002 ISDA Master Agreement, English or New York law) to decide whether § 13 of the Reorganization Act will affect such contractual arrangement during reorganization proceedings (*Reorganisationsverfahren*) under the Reorganization Act.[106]

(B) Collateral Arrangements Governed by German Law

The following discussion relates solely to circumstances where, according to the analysis set out under E.III.(A)(1) above, German insolvency law is applicable under the conflict of laws rules of German international insolvency laws.

If Insolvency Proceedings are instituted in Germany with respect to a German Party, German insolvency law limits the rights of the secured creditors such as counterparties to the German Party under each of the Credit Support Documents irrespective whether created under German or foreign law. While the holder of a full ownership interest being in possession of the Collateral will not be affected by the institution of such proceedings with respect to the German Party, a holder of a security interest may not commence or continue to pursue individual enforcement proceedings against the debtor-in-insolvency in regard of his security interest after the filing of the insolvency petition (§ 89(1) of the Insolvency Code).

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105 It is uncertain whether or not this provision will apply in all circumstances. § 23 of the Reorganization Act provides that the rules contained in the Insolvency Code aiming at protecting financial collateral arrangements shall apply *mutatis mutandis*. Pursuant to Article 7(1)(a) of the EC Collateral Directive Member States shall ensure that a close-out netting provision can take effect in accordance with its terms notwithstanding the commencement reorganisation measures in respect of the collateral provider and/or the collateral taker. If the rules contained in the Insolvency Code aiming at protecting financial collateral arrangements were interpreted in conformity with this provision of the EC Collateral Directive, § 13 of the Reorganization Act should not apply where a financial collateral arrangement exists with respect to the relevant Master Agreement. Any legal authority on this issue is not available.

106 Although the matter is not free from doubt, this seems to follow from the reference in § 7(5), 2nd sentence, of the Reorganization Act to § 46d(3), 3rd sentence, of the Banking Act which in turn refers to § 340(2) of the Insolvency Code according to which the effects of reorganization proceedings shall be governed by the reorganization laws of the State which governs the relevant Agreement.

(1) Realization of the Collateral

Instead, realization of the Collateral is subject to mandatory rules of German insolvency laws. These rules are set out in §§ 50 *et seq.*, §§ 166 *et seq.* of the Insolvency Code. Pursuant to these rules, the holder of a security interest is entitled to realize the collateral by way of "separate liquidation" (*Absonderung*). This means that the secured creditor may seek preferential satisfaction out of the Collateral. The excess of the proceeds over the secured obligation is subject to the general distribution to the ordinary, unsecured creditors.

However, the rules on "separate liquidation" are to some extent different depending on whether the relevant collateral is to be characterized as a "moveable" (*bewegliche Sache*) or as a claim. There appear to exist no court precedent and there is no developed rule of law regarding the question whether Securities which are not bearer Securities qualify as "moveable" within the meaning of § 166(1) of the Insolvency Code. Although it is reasonable to expect that a German court would characterize Immobilized Securities as a "moveable" within such meaning, it is uncertain whether this can also be said with regard to non-negotiable registered Securities or Dematerialized Securities.

(a) Realization of Moveables

Where the relevant collateral qualifies as "moveable" within the meaning of § 166(1) of the Insolvency Code, the holder of a pledge (*Pfandrecht*) or fiduciary ownership transferred for security purposes (*Sicherungseigentum*) is entitled to realize the collateral in the following way:

(i) Possessory Security Interests

In the event of separate liquidation of a possessory security interest such as a pledge or a fiduciary ownership interest where possession of the Collateral is vested in the creditor, the secured creditor is entitled to liquidate the Collateral itself (§ 173(1) of the Insolvency Code) and to keep the proceeds to the extent necessary to cover its costs, interest and its open positions. Any balance must be transferred to the receiver. The secured party does not need to seek leave from the receiver or the court presiding over the insolvency proceedings in order to effect such separate liquidation. In the event, however, that the holder fails to liquidate during a period of time set by the court upon demand of the receiver, the receiver will have the exclusive right to liquidate the collateral and to pay the holder out of the proceeds.

(ii) Non-Possessory Security Interests

Pursuant to §§ 166 *et seq*. of the Insolvency Code, the general rule is that the receiver has the exclusive right to liquidate collateral in respect of which a non-possessory security interest exists, *e.g.*, where fiduciary ownership has been transferred for security purposes and the asset is in the possession of the insolvent debtor. In this case, the receiver is in possession of, and may use, the collateral (§ 172(1) of the Insolvency Code) prior to its liquidation. In addition, the receiver is under an obligation to report (upon demand) to the holder of the security interest on the status of such collateral (§ 167(1) of the Insolvency Code). Prior to liquidation, the holder of the security interest must be notified of the proposed method of liquidation and is entitled to suggest a less expensive way of liquidation (§ 168(1) of the Insolvency Code). In the event that the liquidation is accomplished by the receiver, a lump sum will be deducted from the proceeds prior to payment of the holder in order to cover the costs of ascertaining the holder's rights, the

liquidation costs and value-added tax, if applicable.[107] Currently, this deduction may amount to a charge of (generally) 28 per cent. of the proceeds (§§ 177(1), 171 Insolvency Code).[108]

If the receiver chooses not to liquidate himself, he may require the holder to repossess the collateral for purposes of liquidation. If the holder liquidates the collateral himself, he is required to pay to the estate the equivalent of the aforementioned lump sum in regard of costs (§ 170(2) Insolvency Code). To the extent that the open position of the secured party has not been covered by the proceeds of the collateral, such secured party will be considered an unsecured creditor with respect of the remainder of his claim and receive the proportionate share attributed to the class of unsecured, ordinary creditors (§ 52 Insolvency Code).

(iii) Rules Applicable to Financial Collateral Arrangements

In relation to Collateral provided under Financial Collateral Arrangements, the receiver, as an exception to the general rule set out above, has no right to liquidate Collateral in respect of which a non-possessory security interest exists (§ 166(3) no. 3 of the Insolvency Code). Accordingly, no lump sum will be deducted from the liquidation proceeds and the secured creditor is entitled to liquidate the Collateral itself in the same way as set out above in respect of a possessory security interest.

(b) Realization of a Claim Assigned for Security Purposes

Where the relevant Collateral qualifies not as a "moveable" but as a claim, the general rule is that the receiver has the exclusive right to liquidate such Collateral (§ 166(2) of the Insolvency Code). Again, this general rule does not apply in relation to Collateral provided under Financial Collateral Arrangements (§ 166(3) no. 3 of the Insolvency Code). Accordingly, the rules described above in relation to the liquidation of Collateral in respect of which a possessory security interest exists apply *mutatis mutandis* to the liquidation of Collateral provided under Financial Collateral Arrangements in the form of claims assigned for security purposes.

(2) Segregation from the Estate

Where a creditor has acquired full ownership (as opposed to a mere security interest) in respect of Collateral prior to the filing of the insolvency petition, it may enforce such ownership against the estate irrespective of the commencement of insolvency proceedings. Unlike the fiduciary owner who is not entitled to unconditionally use, sell and otherwise dispose of the Collateral and obliged to return the specific Collateral transferred to it in certain circumstances, the full owner has a right of segregation of the Collateral from the estate (*Aussonderung*) under § 47 Insolvency Code. Segregation from the estate means that the Collateral will not be considered part of the debtor's estate and its owner may exercise any rights arising from his ownership interest irrespective of the institution of insolvency proceedings. Where Collateral such as bearer Securities is in the (direct or indirect) possession of the debtor-in-insolvency, the

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107 As a general rule, no value-added tax will be deducted in the case of the liquidation of securities (*cf.* § 4 no. 8(e) of the German VAT Act (*Umsatzsteuergesetz*)).

108 The deduction may be at a higher amount in cases where the liquidation costs are substantially higher than 5 per cent. of the liquidation proceeds (§ 171(2), 2nd sentence, Insolvency Code).

owner may require that the receiver separate such property from the estate and return it to the owner.

(3) Voidable Preferences

(a) Conflict of Laws

Where Insolvency Proceedings over the assets of the German party do not have any cross-border effect, German insolvency law applies to the avoidance of transactions.

Where such Insolvency Proceedings have a cross-border effect, the following conflict rules apply:

In the case of Insolvency Proceedings against a German party which is not a Financial Institution where the counterparty is established in a Regulation State (*i.e.*, where the Insolvency Regulations apply), the general principle of Article 4(1) of the 2000 Insolvency Regulation and Article 7(1) of the 2015 Insolvency Regulation according to which the laws applicable to insolvency proceedings and their effects are those of the State within the territory of which such proceedings are instituted (*lex fori concursus*, *see* E.III. (A)(1)(a)(iii) above) applies also to the avoidance of transactions (Article 4(2)(m) of the 2000 Insolvency Regulation and Article 7(2)(m) of the 2015 Insolvency Regulation).[109] However, Article 13 of the 2000 Insolvency Regulation and Article 16 of the 2015 Insolvency Regulation contain an exception to this general principle. Pursuant to these provisions Article 4(2)(m) of the 2000 Insolvency Regulation and Article 7(2)(m) of the 2015 Insolvency Regulation, as applicable, do not apply where the person who benefited from an act detrimental to all the creditors provides proof that (i) the said act is subject to the law of a Regulation State other than that of the State of the opening of proceedings and (ii) that law does not allow any means of challenging that act in the relevant case.

In the case of Insolvency Proceedings instituted over the assets of (i) a German party which is a Financial Institution where the counterparty is established outside of Germany or (ii) a German party which is not a Financial Institution where the counterparty is established in a State which is not a Regulation State (*i.e.*, where the conflict rules contained in §§ 335 to 358 of the Insolvency Code apply), §§ 335, 339 of the Insolvency Code apply which contain the same rules as the Insolvency Regulations.

The following discussion relates solely to circumstances where German law is to be applied with respect to the avoidance of transactions because (i) the relevant Insolvency Proceedings do not have a cross-border effect or (ii) the person who benefited from an act detrimental to other creditors is unable to provide the proof described above.

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109 Pursuant to this provision the law of the State of the opening of Insolvency Proceedings determines also "the rules relating to the voidness, voidability or unenforceability of legal acts detrimental to all the creditors."

(b) German Insolvency Law Applicable

In the event of an insolvency proceeding over the assets of the German Party, any security interest of the counterparty to the German Party in Collateral and any outright transfer of Collateral to such counterparty pursuant to the Credit Support Documents would be deemed void if the creation of such security interest or transfer constitutes a voidable preference under fraudulent conveyances rules of the Insolvency Code.

Pursuant to § 129(1) Insolvency Code, the general rule is that the receiver may invalidate any transactions made prior to the institution of the insolvency proceedings which adversely affect the position of the other creditors. The fraudulent conveyances rules are set forth in §§ 130 to 147 of the Insolvency Code.[110]

As regards the creation of a pledge over securities, the transfer of ownership thereof for security purposes or the outright transfer of securities or the payment of cash to Party B under each of the Credit Support Documents, respectively, any such transaction may be avoided if:

(i) such transaction is effected subsequent to the filing of the insolvency petition and results in, or puts Party B in a position to obtain or seek, credit support (*Sicherung*) or satisfaction (*Befriedigung*), respectively, where Party B has knowledge of the insolvency or the insolvency petition or of the relevant facts supporting a compelling conclusion with respect to such insolvency or insolvency petition (§ 130(1) no. 2 of the Insolvency Code);

(ii) such transaction is effected during a period of three months prior to the filing of the insolvency petition and results in, or puts Party B in a position to obtain or seek, credit support or satisfaction, respectively, where Party A is insolvent at the time of the transaction and Party B has knowledge of such insolvency or of the relevant facts supporting a compelling conclusion with respect to such insolvency (§ 130(1) no. 1 of the Insolvency Code);

(iii) such transaction is effected during a period of one month prior to, or subsequent to, the filing of the insolvency petition and results in, or puts Party B in a position to obtain or seek, credit support or satisfaction, respectively, which the Secured Party is not entitled to[111] in such way or at such time or at all (§ 131(1) no. 1 of the Insolvency Code);

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110 With respect to the following discussion *see* Henckel, Insolvenzanfechtung, in Kölner Schrift zur Insolvenzordnung, 2nd ed., 2000, notes 7 *et seq.*; Obermüller, Insolvenzrecht in der Bankpraxis, 5th ed., 1997, notes 1.287 *et seq.*; Obermüller/Hess, Insolvenzordnung, 3rd ed., 1999, notes 298 *et seq.*; Hess/Pape, InsO und EGInsO, Grundzüge des neuen Insolvenzrechts, 1995, notes 721 *et seq.*; Haarmeyer/Wutzke/Förster, *loc. cit.*, notes 5/317 *et seq.*

111 Under similar provisions of the Bankruptcy Code of 1877 the interpretation of which we believe will also apply to the Insolvency Code, a creditor lacks an entitlement in this context if it does not have an enforceable claim to obtain satisfaction or security from the debtor. *See* Paulus in Kübler/Prütting, Insolvenzordnung, *loc. cit.*, § 131, note 6.

(iv) such transaction is effected during the second or third month prior to the filing of the insolvency petition and results in, or puts Party B in a position to obtain or seek, credit support or satisfaction, respectively, which the Secured Party is not entitled to in such way or at such time or at all, where Party A is insolvent at the time of such transaction (§ 131(1) no. 2 of the Insolvency Code) or Party B has knowledge at the time of such transaction that it has adverse effects[112] on the ordinary creditors (*Insolvenzgläubiger*) of Party A or has knowledge of the relevant facts supporting a compelling conclusion with respect to those adverse effects (§ 131(1) no. 3 of the Insolvency Code);

(v) such transaction is effected during a period of three months prior to the filing of the insolvency petition and results in immediate adverse effects on the position of the ordinary creditors of Party A where at the time of such transaction Party A is insolvent and Party B has knowledge of, or of the relevant facts supporting a compelling conclusion with respect to, such insolvency (§ 132(1) no. 1 of the Insolvency Code);

(vi) such transaction is effected subsequent to the filing of the insolvency petition and results in immediate adverse effects on the ordinary creditors of Party A where Party B has knowledge of, or of the relevant facts supporting a compelling conclusion with respect to, Party A's insolvency or the filing of the insolvency petition (§ 132(1) no. 2 of the Insolvency Code); or

(vii) such transaction is effected during a period of ten years prior to, or subsequent to, the filing of the insolvency petition where Party A has the intention to adversely affect the position of its creditors and the Secured Party has actual knowledge of such intention (§ 133(1) of the Insolvency Code) which knowledge is presumed to exist in the case where Party B has knowledge of the imminent insolvency of Party A and the adverse effects caused thereby to the position of Party A's creditors (§ 133(1), 2nd sentence, of the Insolvency Code). Pursuant to § 132(2) of the Insolvency Code, transactions accompanied by immediate adverse effects on the position of the ordinary creditors include, without limitation, transactions that result in the forfeiture or unenforceability of a right of Party A or in the preservation or enforceability of a liability of Party A.[113]

With respect to (i) and (ii) above, § 130(1), 2nd sentence, of the Insolvency Code provides that transactions may not be avoided if they are effected on the basis of a Financial Collateral Arrangement containing an obligation to provide collateral, substitute collateral or additional collateral in order to maintain the ratio between the value of the secured obligations and the value of the assets provided under the Financial Collateral Arrangement, as agreed upon in the

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112 Under similar provisions of the Bankruptcy Code of 1877, an "adverse effect" exists where the creditors cannot be satisfied out of the estate and the relevant transaction to be avoided, from an economic perspective, has prevented, made more difficult, endangered or delayed such satisfaction. *See e.g.*, Bundesgerichtshof, Zeitschrift für Wirtschaftsrecht 1996, 1516, 1518; Paulus, *loc. cit.*, § 129, note 22.

113 There are special rules governing gratuitous transactions or blocked loans (*kapitalersetzende Darlehen*).

relevant Financial Collateral Arrangement.[114] However, the special rule applicable to Financial Collateral Arrangements contained in § 130(1), 2nd sentence, of the Insolvency Code does not apply where a collateral arrangement provides that collateral, substitute collateral or additional collateral is to be posted upon the occurrence of other events, *e.g.*, the rating downgrading of the relevant counterparty.

If the receiver chooses to avoid a particular transaction (including substitutions under Paragraph 4(d) of an Annex, Paragraph 4(d) of the 1995 Deed or Paragraph 4(e) of the IM Deed, exchanges under Paragraph 3(c) of a Transfer Annex or the provision of additional credit support under Paragraph 3(a) of an Annex, Paragraph 3(a) of a Deed and Paragraph 2(a) of a Transfer Annex) under the aforementioned rules, the Collateral Taker must return to the receiver any securities previously delivered by the Collateral Provider to the Collateral Taker, and the Collateral Taker's claim to receive collateral will be reinstated and will participate as an unsecured claim in an insolvency proceeding. § 144(2) of the Insolvency Code provides that any consideration paid in connection with such transaction must be returned by the estate if it has not yet been commingled within the estate and still constitutes an asset of the estate.

(C) Collateral Arrangements Governed by Foreign Law

As mentioned above, Insolvency Proceedings instituted in Germany as main proceedings are deemed to have universal effects, subject to the restrictions applicable to rights *in rem* situated within the territory of another EC Member State in circumstances where the Insolvency Regulations apply (*see* E.III.(A)(1)(a)(iii) above). This means that all property of the insolvent located in Germany and abroad would be subject to such proceedings, provided that, in respect of property located in a foreign country, applicable foreign law recognizes and gives effect to the German claim of universality.

(1) Foreign Security Interests

German law recognizes a security interest if it has been validly created (and/or perfected) under the laws of a foreign jurisdiction.[115] For purposes of determining the effects and enforceability pursuant to German law (whether in the case of insolvency or in the absence of insolvency) of a foreign security interest, it is necessary that any such arrangement be assimilated ("trans-

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114 This provision aims at implementing Article 8 of the EC Collateral Directive. However, the German legislature implementing such Directive does not contain any provisions limiting the avoidance of transactions in the cases of (iii) and (iv) above where Collateral has been provided in the circumstances described above and the Secured Party is not entitled to such Collateral in such way or at such time or at all. The report of the Government submitting the Bill of the act implementing the EC Collateral Directive in German law (*Begründung des Gesetzesentwurfs der Bundesregierung)*, Bundestag-Drucksache 15/1853, p. 16) states that, if Collateral provided under a Financial Collateral arrangement were avoided, § 131 of the Insolvency Code would have to be interpreted in the light of the provision § 130(1), 2nd sentence, of the Insolvency Code. However, since such interpretation does not find a base in law applicable following the implementation of the EC Collateral Directive, it is uncertain whether a court would follow such interpretation and whether in fact Article 8 of the EC Collateral Directive has been implemented in German law.

115 This recognition is subject to the principles of German public policy (*ordre public*), Article 21 of the Rome I Regulation.

ported") to a comparable German type of security interest (*Transpositionslehre*),[116] irrespective whether or not the relevant assets are located in Germany at the time of the institution of insolvency proceedings.[117] Accordingly, a foreign security interest created (and perfected) under applicable foreign law will be recognized in Germany, if:

- the security interest constitutes a right *in rem*, *i.e.*, a right which does not have effects only between the parties, but also with respect to third parties;

- the security interest vests a priority right in the secured creditor with respect to other creditors of the debtor-in-insolvency or other third parties such as purchasers of the collateral; and

- the secured party must transfer any surplus to the debtor should the proceeds of liquidation exceed the secured obligation plus expenses (including legal costs) of repossession and sale and the like.

As a result of such "transposition", a foreign security interest is deemed to have the same effects either as a German law pledge (*Pfandrecht*) or fiduciary ownership (*Sicherungseigentum*), depending on the similarity of the positions obtained by the parties to each of those security interests.[118] Accordingly, the security interest created under foreign law may, if enforced in Germany, be enforced in accordance with the provisions applying to the equivalent German type of security interest.[119] For purposes of enforcement under German insolvency laws, both foreign security interests assimilated to a German pledge and those assimilated to a German

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116 Bundesgerichtshof, BGHZ 39, 173 (175-178); BGHZ 45, 95 (97, 101); Praxis des Internationalen Privat- und Verfahrensrechts 1993, 176, 177; Oberlandesgericht Frankfurt am Main, Die deutsche Rechtsprechung auf dem Gebiet des internationalen Privatrechts 1993, No. 50; Kreuzer, Praxis des Internationalen Privat- und Verfahrensrechts 1993, 157 *et seq.*; Gottwald/Arnold, Insolvenzrechts-Handbuch, 2nd ed., 2001, § 129, note 24; Favoccia, Vertragliche Mobiliarsicherheiten im internationalen Insolvenzrecht, 1991, 51-54; Wendehorst in Münchener Kommentar, *loc. cit.*, Article 43 EGBGB, notes 148 *et seq.*; Lüderitz, *loc. cit.*, notes 53, 60 *et seq.* If, for example, the creation of a security interest is subject to the *situs* rule and governed by the laws of a jurisdiction other than Germany, the security interest is as such not eligible for separate liquidation under the Insolvency Code.

117 Gottwald/Arnold, *loc. cit.*, § 129, notes 23, 24; Gottwald/Arnold, Nachtrag "Gesamtvollstreckungsordnung" zum Insolvenzrechts-Handbuch, 1993, XI A Note 5.

118 Lüderitz, *loc. cit.*, note 61; Wendehorst in Münchener Kommentar, *loc. cit.*, note 148.

119 For instance, the German rules pertaining to the enforcement of a pledge may, notwithstanding the possessory nature of the German pledge also be applied to non-possessory foreign security interests where the structure and content of such security interests is similar to the German pledge. The possessory nature of the pledge is not part of German public policy, *cf.* Bundesgerichtshof, BGHZ 39, 173, 174 *et seq.*; Wendehorst in Münchener Kommentar, *loc. cit.*, note 150 *in fine*; Hübner, Internationalprivatrechtliche Anerkennungs- und Substitutionsprobleme bei besitzlosen Mobiliarsicherheiten, Zeitschrift für Wirtschaftsrecht 1980, 825, 829 *et seq.*; Erman/Hohloch, Bürgerliches Gesetzbuch, *loc. cit.*, Article 43, note 22; Palandt/Thorn, *loc. cit.*, Article 43, note 5. It should be noted, though, that security interests (such as English law floating charges) in regard of an aggregate of collateral (*Sachgesamtheiten*) as opposed to individual items will not be recognized as such under German law, *see* von Bar, Internationales Privatrecht, *loc. cit.*, note 761; Lüderitz, *loc. cit.*, note 99.

fiduciary ownership interest will enjoy the benefit of separate liquidation as described under E.III.(B)(1) above.[120]

German courts have been generous in recognizing foreign collateral arrangements accordingly. However, the transposition of a foreign security interest may be refused if such security interest "is not compatible with the principles of German property law."[121] Until today, no case has been reported where a court has avoided a foreign collateral arrangement on these grounds.

(2) Ownership Transferred Pursuant to Foreign Law

In the event that a creditor has acquired from the debtor-in-insolvency full, non-fiduciary ownership in securities pursuant to applicable foreign law prior to the filing of the insolvency petition, such ownership will be recognized by German law.[122]

(3) Voidable Preferences

Any collateral arrangement created under foreign law may be subject to German fraudulent conveyances rules.[123] Reference is made to the discussion under E.III.(B) above.

(D) Effects of a Payment Moratorium on Collateral Arrangements

As set out above under E.III.(A)(3), credit institutions (*Kreditinstitute*) within the meaning of § 1(1) of the Banking Act, financial services institutions (*Finanzdienstleistungsinstitute*) within the meaning of § 1(1a) of the Banking Act and German branches of entities established outside Germany which are engaged in banking transactions or financial services may become subject to a Payment Moratorium issued by the Financial Services Supervisory Authority pursuant to § 46 of the Banking Act. Essentially the same rules apply under § 42 of the Capital Investment Code with respect to capital management companies (*Kapitalverwaltungsgesellschaften*). Likewise insurance companies within the meaning of § 7 no. 33 Insurance Supervisory Act may become subject to a Payment Moratorium issued by the Financial Services Supervisory Authority pursuant to § 314(1) of the Insurance Supervisory Act. These entities are referred to in this section as "**Institutions**".

§ 46(2), 6th sentence, of the Banking Act and § 314(1), 3rd sentence, of the Insurance Supervisory Act provide that the provisions of the Insolvency Code for the protection of, *inter alia*, Financial Collateral Arrangements shall apply *mutatis mutandis*. Pursuant to § 166(3) no. 3 of the Insolvency Code (*see* E.III.(B)(1)(a)(iii) above), the receiver does not have the right to

120 *Cf.* Favoccia, *loc. cit.*, 45-54.

121 Bundesgerichtshof, Praxis des Internationalen Privat- und Verfahrensrechts 1993, 176 177; Oberlandesgericht Frankfurt, Die deutsche Rechtsprechung auf dem Gebiet des internationalen Privatrechts 1993, No. 50; Wendehorst in Münchener Kommentar, *loc. cit.*, Article 48, note 148.

122 *See* Soergel/Lüderitz, *loc. cit.*, Annex II to Article 38, note 53.

123 Bundesgerichtshof, BGHZ 118, 151 (168); Wertpapier-Mitteilungen 1997, 178 180; Gottwald/Arnold, *loc. cit.*, § 129, notes 60 *et seq.*.

liquidate Collateral which has been provided under a Financial Collateral Arrangement. Consequently, the Collateral Taker in relation to such Financial Collateral Arrangement may foreclose on this Collateral regardless of any Insolvency Proceedings. Although the matter is not entirely free from doubt, we are of the view that the reference to this provision in § 46(2), 6th sentence, of the Banking Act and § 314(1), 3rd sentence, of the Insurance Supervisory Act means that the Collateral Taker in relation to such Financial Collateral Arrangement may also foreclose on this Collateral in the event of a Payment Moratorium, without regard to a possible deferral of the secured claim. A different interpretation would, in our view, contravene the legislature's intention. The legislature sought to ensure that any measure taken by the Financial Services Supervisory Authority under § 46(2), 6th sentence, of the Banking Act and § 314(1), 3rd sentence, of the Insurance Supervisory Act should not affect the enforcement and foreclosure of Financial Collateral Arrangements.[124]

However, it need not be decided here whether or not the reference to § 166(3) no. 3 of the Insolvency Code in § 46(2), 6th sentence, of the Banking Act and § 314(1), 3rd sentence, of the Insurance Supervisory Act means that the Collateral Taker may foreclose on Collateral provided under Financial Collateral Arrangements in the event of a Payment Moratorium. We are of the view that even in the absence of the provisions in § 46(2), 6th sentence, of the Banking Act and § 314(1), 3rd sentence, of the Insurance Supervisory Act and even if a Payment Moratorium were to be construed to result in a deferral of all payment obligations of the relevant Institution,[125] such Payment Moratorium in our view would not prevent the Collateral Taker from foreclosing on the Collateral. Neither § 46(2) of the Banking Act nor § 314(1) of the Insurance Supervisory Act expressly exclude the enforcement of Collateral for an Institution's obligation which is subject to a Payment Moratorium. We believe that § 46 of the Banking Act and § 314(1) of the Insurance Supervisory Act provide for the protection of the liquidity position of an Institution in situations in which a Payment Moratorium may be issued and, therefore, should not preclude the enforcement of Collateral in respect of an obligation deferred under a Payment Moratorium. Preserving Collateral which in any event cannot be used by the insolvent Institution, and which after the end of the Payment Moratorium could in any event be used by the Collateral Taker to satisfy its claims, would not further the interest of the Institution to be protected by a Payment Moratorium. However, there is no court precedent and no developed rule of law regarding this question.

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124 Lindemann (in: Boos/Fischer/Schulte-Mattler, Gesetz über das Kreditwesen, 2nd ed., 2004, § 46a, note 41) prior to the implementation of the Financial Collateral Directive and with respect to § 46a of the Banking Act which has been replaced by additional provisions in § 46 of the Banking Act, took the view that the reference to the Insolvency Code for collateral taken by Central Banks in § 46 (2) sentence 6 of the Banking Act is superfluous. It is not clear whether Lindemann takes a similar view with regard to the treatment of financial collateral under the amended § 46 (1) of the Banking Act. More importantly, even on the basis of this analysis Lindemann is of the view that a moratorium does not affect financial collateral. He is of the opinion that a moratorium does not result in a deferral of payment obligations of the relevant bank (*loc. cit.*, § 46a, note 23). Thus, a secured claim that is due or becomes due at the moment of the imposition of the moratorium remains due, so that in Lindemann's opinion foreclosure on the collateral would be possible even if the creditor's right to foreclose on the collateral depends on the secured claim being due. Consequently, in his view there is no need for a special provision in § 46 of the Banking Act dealing with collateral taken by Central Banks.

125 Cf. Szagunn/Haug/Ergenzinger, Gesetz über das Kreditwesen, 6th ed., 1997, § 46a, note 4a; the contrary view is taken by Lindemann in Boos/Fischer/Schulte-Mattler, *loc. cit.*, § 46a note 23, each with respect to § 46a of the Banking Act which ahs been replaced by additional provisions in § 46 of the Banking Act.

F.
SECURITY INTEREST APPROACH
PURSUANT TO THE SECURITY DOCUMENTS

For the discussion in Part F.II relating to the Security Documents, you have instructed us to assume the following facts:

I. Assumptions relating to the Security Documents

(a) The Security Collateral Provider has entered into a Master Agreement and a Security Document with a Secured Party. The parties have entered into either (i) a Master Agreement governed by New York law and an Annex, or (ii) a Master Agreement governed by English law and a Deed.

(b) Although each of the Security Documents is a bilateral form in that it contemplates that either party may be required to post Collateral to the other depending on movements in Exposure under the relevant Security Document, we assume, for the sake of simplicity, that the same party is the Security Collateral Provider at all relevant times under the applicable Security Document.

(c) We assume that each party is either individually designated under B.1.(b) above or is within one of the categories set out in B.1.(b) above.

(d) Each Master Agreement and each Security Document is enforceable under the laws of New York or England, as the case may be, and that each party has duly authorized, executed and delivered, and has the capacity to enter into, each document.

(e) No provision of the Master Agreement and the relevant Security Document has been altered in any material respect. The making (i) of any selections contemplated pursuant to the standard form of Schedule to the Master Agreement, (ii) of standard elections in Paragraph 13 of either Security Document and (iii) the specification of standard variables (consistently with the other assumptions in this Memorandum) would not in our view constitute material alterations, except where expressly indicated in the discussion below.

(f) Pursuant to the relevant Security Documents, the counterparties agree that Eligible Collateral will include Cash and Securities that are located or deemed located either (i) in Germany or (ii) outside Germany.

(g) Any Securities provided as Eligible Collateral consist of (1) corporate debt securities, whether or not the issuer is organized or located in Germany; (2) debt securities issued by the German government ("*Bunds*"); (3) debt securities issued by the government of a member of the "G-l0" group of countries; and (4) corporate equity securities whether or not the issuer is organized or located in Germany, in one of the following forms:

(i) directly held bearer debt securities: this term shall mean debt securities issued in certificated form and, when held by a Secured Party as Collateral under a Security Document, held directly in this form by the Secured Party (that is, not held by the Secured Party indirectly with an Intermediary (as defined below));

(ii) directly held registered debt securities: this term shall mean debt securities issued in registered form and, when held by a Secured Party as Collateral under a Security Document, held directly in this form by the Secured Party so that the Secured Party is shown as the relevant holder in the register for such securities (that is, not held by the Secured Party indirectly with an Intermediary);

(iii) directly held dematerialized debt securities: this term shall mean debt securities issued in dematerialized form and, when held by a Secured Party as Collateral under a Security Document, held directly in this form by the Secured Party so that the Secured Party is shown as the relevant holder in the electronic register for such securities (that is, not held by the Secured Party indirectly with an Intermediary);

(iv) indirectly held debt securities: this term shall mean a form of interest in debt securities recorded in fungible book-entry form in an account maintained by a financial intermediary (which could be a CSD or a custodian, nominee or other form of financial intermediary, in each case an "**Intermediary**") in the name of the Secured Party where such interest has been credited to the account of the Secured Party in connection with a transfer of Collateral by the Security Collateral Provider to the Secured Party under a Security Document.

The Secured Party's Intermediary may itself hold its interest in the relevant debt securities indirectly with another Intermediary or directly in one of the three forms mentioned in (i), (ii) and (iii).

The assumptions made in this paragraph (g) will be subject to modification as discussed below in paragraphs (l) and (m).

(h) Any cash Collateral is denominated in a freely convertible currency and is held in an account under the control of the Secured Party.

The assumptions made in this paragraph (h) will be subject to modification as discussed below in paragraphs (l) and (m).

(i) Pursuant to the terms and conditions of the relevant Master Agreement, the Security Collateral Provider enters into a number of Transactions with the Secured Party. Such Transactions include any or all of the transactions described in Appendix A.

(j) In the case of questions 12 to 15 below, we assume that after entering into the Transactions and prior to the maturity thereof, the rights of the Security Collateral Taker under paragraph 8 of the relevant Annex or Deed (as applicable) have become exercisable following the occurrence of any of the relevant pre-conditions specified in the Annex or Deed (which shall comprise solely of the events listed in Paragraph 8 or as an election in the pro-forma Paragraph 13) which are then continuing, but that an insolvency proceeding has not been instituted (which is addressed separately in assumption (k) and questions 16 to 18 below).

(k) In the case of questions 16 to 18 below, we assume that an Event of Default under Section 5(a)(vii) of the Master Agreement with respect to the Security Collateral Provider has occurred and a formal bankruptcy, insolvency, liquidation, reorganization, administration or comparable proceeding (collectively, the "insolvency") has been instituted by or against the Security Collateral Provider.

(l) With respect to IM Security Documents only, if any of the Collateral provided under any IM Security Document is held in an account which may hold cash (in a freely convertible currency) and securities (a "**Custodial Account**") with a third-party custodian ("**Custodian**"), we assume that it is held in the following form: (x) the Custodian holds the Collateral in the Collateral Provider's name pursuant to a custodial agreement between the Collateral Provider and custodian; (y) the Custodial Account is used exclusively for the Collateral provided by the Collateral Provider; and (z) the Collateral Provider, the Collateral Taker and the Custodian have entered into an agreement (which may be a separate control agreement or may be part of the custodial agreement) under which the Collateral Taker can take control of the margin under certain circumstances.

(m) In certain circumstances, "initial margin" Collateral may be held at a central securities depository. In these circumstances, the parties will not enter into an IM Security Document. Instead please assume that (w) the Collateral is held in an account within Euroclear or Clearstream; (x) the parties have entered into the Euroclear Documents or the Clearstream Documents (as applicable) and other relevant documentation with Euroclear or Clearstream, which collectively establish collateral arrangements within Euroclear or Clearstream (as applicable) and set forth (i) the manner in which the Collateral is held in Euroclear or Clearstream and (ii) the manner in which the automated transfers of Collateral by Euroclear or Clearstream will be effected (*i.e.*, upon receipt of matching instructions from the Collateral Provider and Collateral Taker as to the overall amount of initial margin Collateral that is required in respect of such Collateral Provider's posting obligation, Euroclear or Clearstream, as applicable, will calculate any excess or deficit and make the relevant transfers accordingly on behalf of the parties in discharge of their obligations to one another); and (y) the Euroclear Documents or the Clearstream Documents and the other documents referred to in (x) (as applicable) are enforceable in accordance with their terms under applicable law (which may be different than German law).

With regard to the foregoing, we note that:

(I) in the case of Euroclear, the Collateral is held in a "Pledged Securities Account" and a "Pledged Cash Account" opened in the Euroclear System in the name of Euroclear acting in its own name but for the account of the Collateral Taker (as pledgee under the pledge granted under the Euroclear Security Agreement) and to be operated in accordance with the relevant Euroclear documents referred to in (x) above; and

(II) in the case of Clearstream, the Collateral is held in a "Collateral Account" opened in the Clearstream system in the name of the Collateral Provider and pledged to the Collateral Taker pursuant to the Clearstream Security Agreement and to be operated in accordance with the relevant Clearstream documents referred to in (x) above.

(n) The parties may enter into more than one Credit Support Document, including multiple Credit Support Documents each subject to different governing laws, and/or may also enter into Euroclear Documents and/or Clearstream Documents.

II. Questions and Answers relating to the Security Documents

A. For Non-IM Security Documents, would any of your responses to questions 1 through 21 below be different as a result of (a) the inclusion of Security Documents in this opinion that were not previously included, or (b), the inclusion of equity securities as Eligible Collateral described in assumption F.I.(g)(4)?

Subject as set out below, our responses to questions 1 through 21 below would be the same, irrespective of (a) the inclusion of the VM NY Annex in this Memorandum and (b) the inclusion of equity securities as Eligible Collateral described in assumption F.I.(g)(4).

However, where the parties in Paragraph 13(b) of the VM NY Annex specify the term "Covered Transactions" in a manner that it does not cover all Transactions under the relevant Master Agreement, depending on the circumstances of a particular case, this (i) may in the view of a court cast doubt on the qualification of Collateral provided under such VM NY Annex as Collateral under a Financial Collateral Arrangement and (ii) may lead to a higher risk of avoidance under fraudulent conveyances rules discussed under E.III.(B)(3) above.

- In particular in circumstances where in a given situation the mark-to-market value of Transactions which do not constitute Covered Transactions is higher than the mark-to-market value of Transactions which are Covered Transactions, *i.e.*, where in economic terms the Pledgor, but not the Secured Party, has an economic net exposure under the relevant Master Agreement, a court could take the view that Collateral provided to the Secured Party by its very nature may not be considered as collateral, as it economically does not serve a collateral purpose and the basis for its calculation is artificial and unrelated to the economic net exposure under the relevant Master Agreement. Accordingly, depending on the specification of "Covered Transactions" in an individual case, the view may be taken that Collateral provided under a VM NY Annex may not qualify as Collateral under a Financial Collateral Arrangement. Any legal authority on this issue is not available.

- If such view were taken, this could also increase the risk of avoidability of the provision of Collateral as described under E.III.(B)(3) above. In particular, the "safe harbor" under § 130(1), 2nd sentence, of the Insolvency Code (see, E.III.(B)(3)(b) above) according to which transactions may not be avoided if they are effected on the basis of a Financial Collateral Arrangement containing an obligation to provide collateral, substitute collateral or additional collateral in order to maintain the ratio between the value of the secured obligations and the value of the assets provided under the Financial Collateral Arrangement, as agreed upon in the relevant Financial Collateral Arrangement, may not be available in such circumstances. Again, any legal authority on this issue is not available.

- These concerns should apply to a lesser extent in circumstances where all Transactions under a Master Agreement constitute Covered Transactions, but under different Security Documents, *e.g.*, one Security Document covering Transactions being entered into prior to a certain cut-off date and another Security Document covering Transactions being entered into on or after such cut-off date. In such circumstances, all Collateral provided under all Security Documents taken together result, due to the balancing effects of Collateral provided in either direction, economically in securing the net exposure under the relevant Master Agreement. This supports the view that in such circumstances Collateral provided under a VM NY Annex which does not cover all Transactions under the relevant Master Agreement does nevertheless qualify as Collateral under a Financial Collateral Arrangement.[126] Any legal authority on this issue is not available.

- The above concerns should apply even less in circumstances where the parties enter into a Security Document covering Transactions being entered into on or after such cut-off date solely in order to fulfill newly introduced regulatory requirements[127] and leave Transactions being entered into prior to such cut-off uncollateralized. In such circumstances, it may be considered a legal contradiction if the provision of collateral made in full compliance with regulatory requirements was viewed as being avoidable in insolvency proceedings.

Given the legal uncertainty on the above issues, parties should carefully consider the specification of "Covered Transactions" when entering into a VM NY Annex. However, even where Collateral provided in the circumstances discussed above is at risk of being avoided under fraudulent conveyances rules discussed under E.III.(B)(3) above, applicable insolvency conflict rules (as discussed under E.III.(B)(3)(a) above) provide that no avoidance takes place where the person who benefited from an act detrimental to all the creditors provides proof that (i) the said act is subject to the law of a state other than that of the state of the opening of proceedings and (ii) that law does not allow any means of challenging that act in the relevant case. With respect to the VM NY Annex this means that provision of Collateral to the Collateral Taker cannot be avoided under German law if the Collateral Taker provides proof that such provision of Collateral in the relevant circumstances is not subject to avoidance under applicable New York law.

B. For the IM Security Documents only, assume that the Collateral will be held in a

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126 This view is essentially also taken by Fried, in Zerey (ed.), Finanzderivate, 4th ed., 2016, p. 485 et seq. Although the matter is not addressed in detail, the European regulations on variation margin can be read to also assume that a netting arrangement may be accompanied by more than one collateral arrangement (cf. Article 12(2)(a) in connection with Article 1(3) of Commission Delegated Regulation (EU) 2016/2251 of 4 October 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty).

127 Such as under Article 11(15) of Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories, as amended, and related regulations.

Custodial Account with a Custodian as described in assumption F.I.(l) above and not pursuant to assumptions in F.I.(g)(i), (g)(ii), (g)(iii) and (h) above or assumption F.I.(m) above.

(i) Would any of your responses to questions 1 through 21 below with respect to Collateral held pursuant the custodial arrangement described in assumption F.I.(l) above be different as a result of (a) the inclusion of the IM Security Documents in this opinion, (b) the inclusion of equity securities as Eligible Collateral described in assumption F.I.(g)(4), or (c) the holding of the Collateral pursuant to one of the custodial arrangements described in F.I.(l) above?

Our responses to questions 1 through 21 below with respect to Collateral held pursuant the custodial arrangement described in assumption F.I.(l) above would be the same as a result of (a) the inclusion of the IM Security Documents in this Memorandum, (b) the inclusion of equity securities as Eligible Collateral described in assumption F.I.(g)(4), and (c) the holding of the Collateral pursuant to one of the custodial arrangements described in F.I.(l) above, provided that:

- where Collateral is held pursuant the custodial arrangement described in assumption F.I.(l) above, certain parts of the discussion with respect to question 1 under F.II.1.(b)(1)(ii), F.II.1.(b)(2) and F.II.1(c)(2) are not applicable. Nevertheless, we reiterate with respect to the IM NY Annex and the IM Deed our recommendation set out under F.II.1.(b)(3) and F.II.1.(c)(3), respectively, that these Security Documents should not be used in circumstances where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law, unless it has been specifically amended so as to comply with the requirements of German law; and

- the discussion set out under A. above also applies where the parties in Paragraph 13(b) of the IM Security Documents specify the term "Covered Transactions" in a manner that it does not cover all Transactions under the relevant Master Agreement.

(ii) Please describe any requirements that the custodial arrangements described in assumption F.I.(l) above must meet to permit the Collateral Taker to exercise the same rights as if no such custodial arrangements were in place.

There are no such requirements as a matter of German law.

C. Assume that the Collateral will be held by Euroclear or Clearstream, as contemplated by assumption F.I.(m) above and not pursuant to assumptions F.I.(g)(i), (g)(ii), (g)(iii) and (h) above or assumption F.I.(l) above.

(i) Would any of your responses to questions 1 through 9 and 12-21 below with respect to Collateral held pursuant the arrangement described in assumption F.I.(m) above be different as a result of the holding of the Collateral pursuant to one of the custodial arrangements described in F.I.(m) above?

Our responses to questions 1 through 9 and 12-21 below with respect to Collateral held pursuant the custodial arrangement described in assumption F.I.(m) above would be the same as a result of the holding of the Collateral pursuant to one of the custodial arrangements described in F.I.(m) above, provided that:

- where Collateral is held pursuant the custodial arrangement described in assumption F.I.(m) above, certain parts of the discussion with respect to question 1 under F.II.1.(b)(1)(ii), F.II.1.(b)(2) and F.II.1(c)(2) are not applicable. Nevertheless, we reiterate with respect to the IM NY Annex and the IM Deed our recommendation set out under F.II.1.(b)(3) and F.II.1.(c)(3), respectively, that these Security Documents should not be used in circumstances where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law, unless it has been specifically amended so as to comply with the requirements of German law; and

- the discussion set out under A. above also applies where the parties in Paragraph 13(b) of the IM Security Documents specify the term "Covered Transactions" in a manner that it does not cover all Transactions under the relevant Master Agreement.

(ii) Please describe any requirements that the arrangements described in assumption F.I.(m) above must meet to permit the Collateral Taker to exercise the same rights as if no such custodial arrangements were in place.

There are no such requirements as a matter of German law.

(iii) Please assume that the Euroclear Documents are amended by the Euroclear Japanese Amendments. Would any of our responses to questions (i) and (ii) above be different with respect to Collateral held pursuant to the arrangements described in the Euroclear Japanese Amendments?

No.

(iv) Please assume that the Clearstream Documents are amended by the Clearstream Japanese Amendments. Would any of your responses to questions (i) and (ii) above be different with respect to Collateral held pursuant to the arrangements described in the Clearstream Japanese Amendments?

No.

D. Notwithstanding assumptions F.I.(e) and (l), please assume that the IM NY Annex is amended by the IM NY Annex Japanese Amendments. Would any of your responses to questions 1 through 21 below with respect to Collateral held pursuant the custodial arrangement described in the IM NY Annex Japanese Amendments be different as a result of (a) the inclusion of the IM NY Annex, as amended by the IM NY Annex Japanese Amendments, in this opinion or (b) the holding of the Collateral pursuant to one of the custodial arrangements described in the IM NY Annex Japanese Amendments? If so, please comment specifically on any such changes.

No.

E. ***Please assume that the VM NY Annex is amended by the VM NY Annex IA Amendments. Would any of your responses to questions 1 through 21 below be different as a result of the inclusion of the VM NY Annex, as amended by the VM NY Annex IA Amendments, in this opinion?***

No.

F. ***Notwithstanding assumptions F.I.(e) and (l), please assume that the IM Deed is amended by the IM Deed Japanese Amendments. Would any of your responses to questions 1 through 21 below with respect to Collateral held pursuant to the custodial arrangement described in the IM Deed Japanese Amendments be different as a result of (a) the inclusion of the IM Deed, as amended by the IM Deed Japanese Amendments, in this opinion or (b) the holding of the Collateral pursuant to one of the custodian arrangements described in the IM Deed Japanese Amendments? If so, please comment specifically on any such changes.***

No.

Validity of Security Interests

1. ***Under German law, what law governs the contractual aspects of a security interest in the various forms of Eligible Collateral deliverable under the Security Documents? Would the German courts recognize the validity of a security interest created under each Security Document, assuming it is valid under the governing law of such Security Document?***

(a) General

German law does distinguish between the contractual aspects of a security interest and its proprietary aspects in the sense that a distinction is being drawn between the obligation to provide security and the creation (*Bestellung*) of the security interest. Creation of a security interest as such results in effective security and constitutes fulfilment of the obligation to provide security. *See* E.II.(A) above.

Under German private international law, the parties may freely choose the law governing the obligation to provide security (Article 3(1) of the Rome I Regulation). However, the parties may not freely choose the law governing the creation of a security interest. The law governing the creation of a security interest is determined by mandatory rules (*see* the answer to question 2 below).

Paragraph 3 of the 1994 NY Annex and the 1995 Deed oblige the Security Collateral Provider to provide security. The choice by the parties of New York law or English law to govern the obligation to provide security is valid under German law and would be recognized by the German courts.

(b) Validity of a Security Interest Created under the 1994 NY Annex

It is not certain that a German court would uphold a security interest pursuant to the 1994 NY Annex in respect of Collateral in the form of Securities or Cash in those cases where, pursuant to German private international law, German substantive law is to be applied (*see* the discussion in E.I.(A) and (B) above).

(1) Pledge of Securities

(i) Type of Security Interest

Pursuant to the 1994 NY Annex, the parties intend to establish a pledge under New York law. This choice of New York law will not be given effect by a German court which will apply German law whenever the security interest is to be created in Securities on which, pursuant to German conflict of laws rules, German substantive law is to be applied. The agreement made in the 1994 NY Annex must therefore be interpreted in accordance with German substantive law governing the creation of security interests. The application of German law would likewise lead to the conclusion that the 1994 NY Annex purports to establish a pledge (*Pfandrecht*). According to the expressions used in Paragraph 2 of the 1994 NY Annex,[128] and in the light of other provisions contained in the 1994 NY Annex,[129] the parties do not intend to transfer full title to, but rather to create a limited interest in, the Collateral. Further, the 1994 NY Annex requires possession of the Collateral by the Collateral Taker.[130] The Collateral Taker typically does not hold possession in the event of a transfer of ownership for security purposes. In contrast, the pledge is the typical possessory security interest available under German law (*see* E.II.(B)(1) above).

(ii) Creation of a Pledge

As set out in E.II.(B)(1)(b) above, the creation of a pledge under German law requires an agreement between the pledgor and the pledgee to establish a pledge over the collateral for the benefit of the pledgee and the transfer of possession of the Collateral. The agreement between the Security Collateral Provider and the Collateral Taker to establish a pledge is contained in Paragraph 2 of the 1994 NY Annex.

As regards the transfer of possession of Collateral in the form of Securities, pursuant to the definition of "Transfer" in Paragraph 12 of the 1994 NY Annex such transfer is to be constituted by "the giving of written instructions to the relevant depositary institution ..." and is purported to be "sufficient if complied with to result in a legally effective transfer" of the Securities to the Collateral Taker. Such written instructions, however, will not constitute effective transfer of possession. As outlined above (*see* E.II.(A)(1)(b)), the transfer of possession for purposes of creating a pledge in the co-ownership interests in Securities on which pursuant to German conflict of laws rules, German substantive law is to be applied, requires the debiting of the account of the Security Collateral Provider with the

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128 The first sentence of this provision reads in part: "[T]he *Pledgor* ... *pledges* ... and grants ... a *first priority security interest* in, *lien* on and right of Set-off ..." (emphasis added).

129 For instance, Paragraph 6(a) indirectly refers to Posted Collateral as the Pledgor's property.

130 *See* the definition of "Transfer" in Paragraph 12 of the 1994 NY Annex.

relevant CSD or an intermediary depositary and the crediting of the account of Collateral Taker with such CSD or an intermediary depositary, with the relevant Securities.[131] It will also be necessary for such transfer of possession that all intermediary depositaries hold possession of the relevant Securities for the benefit of their depositors as stated under E.II.(A)(1)(b)) above. Therefore, indirect possession will be transferred under the 1994 NY Annex provided that the relevant accounts maintained with such CSD or any intermediary depositaries are duly debited and credited, respectively, and any intermediary depositaries hold indirect possession of the relevant Securities.

(iii) Violation of Mandatory Principles Applicable to a Pledge

Various provisions of the 1994 NY Annex violate mandatory statutory principles governing a pledge under German law.

Right to Dispose of Securities: Unless otherwise specifically agreed by the parties, the Collateral Taker may, pursuant to Paragraph 6(c) of the 1994 NY Annex, prior to the maturity of the secured obligation, use, sell, pledge or otherwise dispose of Collateral free from any right of the Security Collateral Provider. As set out above (*see* E.II.(B)(1)(c)), we believe that the concept and the rights and obligations under an irregular pledge in respect of Securities do not afford adequate certainty to determine the validity under German law of a right of use or appropriation agreed upon between a pledgor and a pledgee, except for circumstances where the special statutory provisions regarding the right of use or appropriation in respect of pledged securities in connection with (i) securities custody business carried on by German credit institutions and (ii) loans extended by the Bundesbank apply. As a result, it is likely that the right of disposal provided for in the 1994 NY Annex violates the rules of the Civil Code requiring that the pledgee keeps the Collateral at all times in safe custody.

Further, the Collateral Taker's appropriation rights may also violate § 1229 of the Civil Code. As has been described above (under E.II (B)(1)(c)), pursuant to § 1229 of the Civil Code the pledgor and the pledgee may not agree prior to the time at which the secured obligation has become due and payable that ownership in the collateral shall be vested in the pledgee, and any such agreement will be null and void. Under Paragraph 6(c) of the 1994 NY Annex, the Collateral Taker may appropriate Collateral while it is "deemed to continue to hold all Posted Collateral". Its rights are not conditioned upon default on the secured obligation at maturity. However, it may be argued that appropriation prior to maturity will put the pledgor in a position even more unfavorable than in the case of a forfeiture of the pledge at maturity. Therefore, the right of disposal entails the risk of being excluded in light of § 1229 of the Civil Code.

Right to Set-Off: Pursuant to Paragraph 8(a)(iii) of the 1994 NY Annex, the Collateral Taker may exercise the right to Set-off any Collateral if an Event of Default or a Specified Condition has occurred or an Early Termination Date has occurred or been designated as a result of an Event of Default or a Specified Condition. The expression "Set-off" is defined to include, *inter alia*, "offset" and "right of retention or withholding or similar

131 As this mode of transfer applies to Securities "which the parties have agreed will be *delivered by book-entry*" (*see* the definition of "Transfer" in Paragraph 12 of the 1994 NY Annex), it may safely be assumed that such debiting and crediting of accounts will follow such written instructions.

right" (Section 14 of the Master Agreement). As has been noted immediately above, prior to the maturity of the secured obligation, any agreement that the pledgor's ownership of the collateral shall be vested in the pledgee in the event of the pledgor's default at maturity will not be recognized under German law. In view of the fact that the Collateral Taker will have already taken possession of the Collateral when the pledge is created and of the possessory interest established under Paragraph 2 of the 1994 NY Annex, the agreement on the right to offset, retain or withhold Collateral made in Paragraph 8(a)(iii) of the 1994 NY Annex might be considered to be an agreement on the forfeiture of ownership which is expressly declared to be null and void under § 1229 of the Civil Code.

Realization of Collateral Prior to Maturity of the Secured Obligation: Paragraph 8(a)(iv) of the 1994 NY Annex provides that any Collateral may be realized by the Collateral Taker if and when an Event of Default or Specified Condition has occurred or an Early Termination Date has occurred or been designated.

Moreover, Paragraph 8(a)(iii) of the 1994 NY Annex grants the Collateral Taker a right to set off accounts receivable of the Security Collateral Provider against Collateral if and when an Event of Default or Specified Condition has occurred or an Early Termination Date has occurred or been designated which right, in the German law environment, requires prior realization of such Collateral.[132]

Finally, under Paragraph 6(c) of the 1994 NY Annex, the Collateral Taker is entitled to sell at any time Posted Collateral. Although Paragraph 6(c) of the 1994 NY Annex is not concerned with realization of the Collateral,[133] the Security Collateral Provider would in concepts of German law still lose title to the Collateral while the Collateral Taker would be free to use and hold on to the proceeds from the sale. Accordingly, a sale in accordance with Paragraph 6(c) of the 1994 NY Annex may have effects similar to realization prior to maturity of the secured obligation.

The Collateral Taker's right to liquidate or dispose of the Collateral prior to maturity, *i.e.*, before the secured debt becomes due and payable, violates a mandatory rule applicable to a German law pledge.

As has been outlined above (under E.II.(B)(1)(c)), the Collateral may be realized only upon maturity of the secured obligation. If the secured obligation is not an obligation for the payment of money, realization is permitted only once such obligation has become an obligation for the payment of money and is due and payable. Any realization prior to maturity of the secured obligation for the payment of money is expressed to be "illegal".

Here, the secured obligation will be the close-out balance owed by the Security Collateral Provider to the Collateral Taker pursuant to Section 6(e) of the Master Agreement, which balance will become due and payable in accordance with Section 6(d)(ii) of the Master

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132 § 387 Civil Code provides, *inter alia*, that obligations may only be set off if they are equal in kind (*e.g.*, payment claims).

133 Pursuant to Paragraph 6(c) of the 1994 NY Annex, the Secured Party is deemed to continue to hold the Posted Collateral.

Agreement. Pursuant to the provisions of the Master Agreement, the obligation to pay the close-out balance may not become due and payable even if an Event of Default or a Specified Condition has occurred, because the occurrence of any of these events will not necessarily result in the termination of the Transactions. Even if the close-out balance were to become due and payable, the due date would in any event fall after the occurrence of the Event of Default, Specified Condition or Early Termination Date.

The realization of Posted Collateral prior to maturity of the close-out balance would result in the nullity of the enforcement and be without legal effect. Ownership would remain in the Security Collateral Provider and the pledge would continue to encumber the Posted Collateral (*see* E.II.(B)(1)(c) above). Only if the sale were effected by a bailiff on behalf of the Collateral Taker (*cf.* §§ 1244, 1233(2) of the Civil Code) or by way of a public auction or a sale by a licensed broker or licensed auctioneer (§§ 1244, 1235 of the Civil Code) would the Security Collateral Provider lose title to a *bona fide* purchaser. In that case, the secured obligation would be deemed discharged as a matter of law, and any excess proceeds would have to be returned to the Security Collateral Provider (*cf.* § 1247 of the Civil Code). The Collateral Taker, furthermore, may be liable for damages to the Security Collateral Provider. The right to realize the Collateral prior to maturity under the 1994 NY Annex, in our view, is particularly questionable as it results in a separation of the pledge and the secured debt contrary to the German law concept of the pledge being an accessory right *in rem*.[134]

Right of Retention: Paragraph 8(a) of the 1994 NY Annex specifies the Collateral Taker's rights for purposes of enforcement of the Posted Collateral. Paragraph 8(a)(iii) of the 1994 NY Annex establishes a right of the Secured Party to set-off, retain or withhold Collateral if an Event of Default or a Specified Condition has occurred or an Early Termination Date has occurred or been designated.

Under § 1228(1) Civil Code, a pledge may only be enforced by the sale of the Collateral. In principle, pledgor and pledgee may not agree upon any other manner of enforcement or liquidation.[135] The right of liquidation by sale is provided in Paragraph 8(a)(iv) of the 1994 NY Annex. However, the right of set-off, retention and withholding pursuant to Paragraph 8(a)(iii) of the 1994 NY Annex provides the Collateral Taker with additional means of enforcing the pledge which are not permitted means of liquidation under German law.[136]

(2) Pledge of Cash

For purposes of determining the validity of the pledge of Cash as provided for under the 1994 NY Annex, a German court, as has been mentioned (*see* E.I.(B) above), is likely to apply German law where the Cash is being transferred to an account of the Collateral Taker maintained with a bank in Germany. As outlined in E.II.(B) above, under German

134 As indicated in E.I. above, the survival of the pledge is conditioned upon the secured obligation.

135 Reichsgericht, Juristische Wochenschrift 1935, 2886; Soergel/Mühl, *loc.cit.*, § 1245, note 4.

136 As indicated in E.I. above, the survival of the pledge is conditioned upon the secured obligation.

law the pledge of Cash is conceivable in the form of the pledge of a payment claim. Pursuant to the terms of the 1994 NY Annex, however, the Security Collateral Provider does not pledge to the Collateral Taker a claim under an account which it maintains with a bank. Accordingly, the pledge of Cash as provided in the 1994 NY Annex does not constitute a meaningful agreement under German law. Therefore, it is unlikely that it will be given effect whenever German law applies.

(3) Legal consequences of the invalidity and ineffectiveness of provisions of the 1994 NY Annex

The invalidity of various provisions of the 1994 NY Annex together with the ineffectiveness of the pledge of cash thereunder, in circumstances where German law is to be applied, may lead a German court to hold that in these circumstances the 1994 NY Annex will not create an effective security interest whatsoever.

Regarding the choice of New York law in respect of the 1994 NY Annex,[137] the choice-of-law clause and the remainder of the pledge agreement are clearly separable and, pursuant to the terms of the 1994 NY Annex, the Security Collateral Provider and Collateral Taker do not appear to exclude the creation of a pledge governed by the laws of a jurisdiction other than New York if such laws apply according to relevant mandatory conflict-of-laws principles. In our view, the choice of New York law does not constitute a *conditio sine qua non* under the 1994 NY Annex. Rather, the parties purport to create a pledge the terms of which are modelled on New York law. Under German law, where the Posted Collateral consists of securities on which pursuant to German conflict of laws rules, German substantive law is to be applied the 1994 NY Annex results in the creation of a German law pledge governed by mandatory rules set forth in the Civil Code, while a number of provisions made in the 1994 NY Annex would be void under German law, and where the Posted Collateral consists of cash transferred to an account maintained with a bank in Germany, the pledge of cash purported to be created under the 1994 NY Annex is likely to be without effect.

However, if a German court were to hold the above-mentioned provisions of the 1994 NY Annex to be void and not give effect to the pledge of Cash made thereunder, the court may conceivably also hold that even the creation of a pledge in Securities on which pursuant to German conflict of laws rules, German substantive law is to be applied as such is null and void. Under German law, the agreement between pledgor and pledgee to create a pledge for the benefit of the pledgee is subject to the general rules on legal acts (*Rechtsgeschäfte*). Pursuant to § 139 Civil Code, any legal act is void in its entirety if one or more parts thereof are void, unless it may be assumed that such legal act would have been undertaken even without such void part(s).[138] [139] It is uncertain in our view that in

137 Such a choice of law is to be contained in Part 4(h) of the Schedule to the Master Agreement. Pursuant to the preamble of the 1994 NY Annex, such Annex forms part of, and is subject to, the Master Agreement and its Schedule.

138 Notwithstanding the fact that the 1994 NY Annex is governed by New York law, a German court would have to revert to the German law rule of construction in § 139 Civil Code because under mandatory German conflicts principles, the creation of the security interest is a legal act subject to German law.

the circumstances it could be established that the parties would have agreed on the pledge of Securities on which pursuant to German conflict of laws rules, German substantive law is to be applied had they known of the invalidity of the above-mentioned clauses in respect of such Securities and the ineffectiveness of the pledge of Cash. As a result, the agreement on the pledge may be held to be without effect in its entirety.

Accordingly, we recommend that the 1994 NY Annex should not be used in circumstances where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law, unless it has been specifically amended so as to comply with the requirements of German law.

(c) Validity of a security interest created under the 1995 Deed

Again, as in the case of the 1994 NY Annex, it is uncertain that a German court would uphold a security interest pursuant to the 1995 Deed in respect of Posted Collateral in those cases where, pursuant to German conflict of laws rules, German substantive law is to be applied. In respect of Securities, that is the case under the circumstances described under E.I.(A) above. In respect of Cash, German substantive law is likely to apply in those cases where the cash is to be transferred to an account maintained with a bank in Germany (*see* E.I.(B) above).

(1) Pledge of Securities

(i) Type of security interest

Pursuant to the 1995 Deed, the parties intend to establish a "first fixed legal mortgage" under English law on Posted Collateral in the form of Securities. This choice of English law will not be honoured by a German court which will apply German law whenever the security interest is to be created in Securities on which pursuant to German conflict of laws rules, German substantive law is to be applied. In these circumstances, the agreement on the security interest to be established must therefore be interpreted in accordance with German substantive law regarding the creation of security interests. It is likely that a German court in applying German law would conclude that the 1995 Deed purports to grant a pledge (*Pfandrecht*). Paragraph 2(b) of the 1995 Deed provides that the "Chargor ... mortgages, charges and pledges and agrees to mortgage, charge and pledge, with full title guarantee, in favour of the Collateral Taker by way of first fixed legal mortgage" all Posted Collateral in the form of securities. Understandably, these terms and expressions are largely without meaning in German law. It is clear, though, from various provisions of the 1995 Deed that no full title transfer of the Collateral in the form of Securities is desired. In particular, Paragraph 6(c) of the 1995 Deed provides explicitly that such Posted Collateral "shall at all times remain the property of the Chargor ... and shall at no time constitute the property of ... the Secured Party".

(ii) Creation of Pledge

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139 The party who wishes to enforce the pledge would have the burden of proof that the act would have been undertaken even without the void parts.

As mentioned in E.II.(B)(1)(b) above, the creation of a pledge under German law requires an agreement between the pledgor and the pledgee to establish a pledge over the collateral for the benefit of the pledgee and the transfer of possession of the Collateral (§§ 1205, 1206 Civil Code). The agreement between the Security Collateral Provider and the Collateral Taker to establish a pledge may be found in Paragraph 2(b) of the 1995 Deed. As regards the transfer of possession, reference is made to what is said in respect of the 1994 NY Annex above regarding the transfer of possession. In the case of the 1995 Deed, the matter is dealt with in Paragraph 4(b)(iii) of the 1995 Deed corresponding substantially to the definition of "Transfer" in Paragraph 12 of the 1994 NY Annex.

(iii) Assignment of rights

Under Paragraph 2(b)(iii) of the 1995 Deed, the Security Collateral Provider "assigns and agrees to assign, with full title guarantee, the Assigned Rights to the Secured Party absolutely". The expression "Assigned Rights" includes, inter alia, "all rights relating to the Posted Collateral which the Chargor may have now or in the future against the Secured Party" (*see* Paragraph 12 of the 1995 Deed).

The assignment under Paragraph 2(b) of the 1995 Deed appears to include the Security Collateral Provider's claims under Paragraph 3(b) of the 1995 Deed for redelivery (in the case of Securities) or repayment (in the case of Cash) of Posted Credit Support following a Valuation Date as well as under Paragraph 8(e) of the 1995 Deed for the final return of Posted Credit Support upon the discharge of all Obligations of the Security Collateral Provider. Where a pledge of assets is governed by German law, the rights and obligations of the pledgor and the pledgee in the event of the expiration of the pledge are likewise determined by German law. Under § 1223(1) of the Civil Code, the pledgee is obligated to return the pledged asset to the pledgor upon the expiration of the pledge. Under German law, as has been mentioned above (under E.II.(C)(2)), an assignment of a claim by the holder thereof to the debtor results in the extinguishment of the claim.[140] Accordingly, the assignment pursuant to Paragraph 2(b) of the 1995 Deed by the Security Collateral Provider of its claims under Paragraph 4(b) and 8(e) of the 1995 Deed, which corresponds to the German law claim under § 1223(1) of the Civil Code, leads to the extinguishment of these claims.

(iv) Violation of mandatory principles applicable to a pledge

Various provisions of the 1995 Deed violate mandatory statutory principles governing a pledge under German law.

Realization of Collateral Prior to Maturity of the Secured Obligation: Under Paragraph 8(a) of the 1995 Deed the Collateral Taker may realize Posted Collateral if a Relevant Event or Specified Condition has occurred or an Early Termination Date has occurred or been designated as a result of an Event of Default or Specified Condition. Pursuant to Paragraph 7 of the 1995 Deed, a "Relevant Event" includes, *inter alia*, the occurrence of an Event of Default, the failure to transfer or return when due Collateral (provided that such failure continues for two business days after notice is received) and the failure to perform any other obligation under the Master Agreement or the 1995 Deed

140 Bundesgerichtshof, BGHZ 48, 219; Palandt/Grüneberg, *loc.cit.*, Introduction to § 362, note 4.

(provided that such failure continues for 30 days after notice has been given). Paragraph 8(a) of the 1995 Deed offends the mandatory rule of German law contained in § 1228(2) of the Civil Code pursuant to which the Collateral may be realized only upon maturity of the secured obligation (*see* E.II.(B)(1)(c) above). The legal position is here substantially the same as that under the 1994 NY Annex, and reference may be made, therefore, to the discussion of the 1994 NY Annex regarding realization prior to maturity (*see* (b)(1)(iii) immediately above).

Manner of Realization: Under Paragraph 8(a)(1)(A) of the 1995 Deed the Collateral Taker shall have power, in respect of Posted Collateral in the form of Securities, "to sell all or any of the Posted Collateral in any manner permitted by law upon such terms as the Secured Party shall in its absolute discretion determine". As has been outlined above (under E.II.(B)(1)(c)), German law provides for comprehensive rules regarding the manner of realization of the collateral, many of which are mandatory and not subject to disposition of pledgor and pledgee. The quoted provision of Paragraph 8(a)(1)(A) is in compliance with German law only if it may be interpreted to refer to German law, rather than to English law, regarding the manner of realization, in circumstances where the pledge of the collateral is subject to German law. A doubt on such interpretation is cast by the fact that in the immediate context of the quoted provision the 1995 Deed refers to statutory provisions of English law enforcement rules. If Paragraph 8(a)(1)(A) should refer to English law even in circumstances where the pledge and the manner of its realization is subject to German law, it will be upheld only in as much as English law complies in relevant aspects with the applicable mandatory German law rules.

Waiver of Security Collateral Provider's Defenses: Paragraph (2)(e) of the 1995 Deed provides, *inter alia*, that any pledge established pursuant to the 1995 Deed shall not be affected by any change or release of any terms of the Master Agreement or of any rights (which means rights of the Collateral Taker) against the Security Collateral Provider (Paragraph (2)(e)(ii)), any invalidity or unenforceability of any obligations of the Security Collateral Provider under the Master Agreement (Paragraph (2)(e)(iii)) or by any legal limitation, disability, incapacity or other circumstance relating to the Security Collateral Provider (Paragraph (2)(e)(iv)).

As has been outlined above (under E.II.(B)(1)(a)) a pledge under German law is strictly accessory to the obligation which it is to secure. If such obligation does not arise, the pledge does not arise. If such obligation ceases to exist for whatever reason, the pledge ceases to exist. If such obligation is subject to a permanent defense, the pledge is unenforceable and the pledgee is required to return the pledged asset to the pledgor. All these principles constitute mandatory rules of law. Accordingly, Paragraph (2)(e) of the 1995 Deed offends mandatory German law rules to the extent that it provides that the non-existence, invalidity or nullity of the secured obligation shall not affect the validity of the pledge or that a permanent defense with respect to such obligation shall be without effect on the obligations of the Security Collateral Provider under the 1995 Deed.

Moreover, if the pledge itself, as distinct from the obligation which it is to secure, should not be validly created due to "any legal limitation, disability, incapacity or other circumstance relating to the Chargor" (Paragraph (2)(e)(iv) of the 1995 Deed), the waiver by the German party pursuant to Paragraph (2)(e) of the 1995 Deed will be ineffective under German law and will be disregarded by a German court.

Reinstatement: Paragraph (2)(g) of the 1995 Deed provides, in substance, that where any discharge in respect of the pledge or secured obligation is made or any arrangement affecting the pledge or the secured obligation is avoided, or any amount paid pursuant to such discharge or arrangement must be repaid on insolvency or otherwise, the pledge constituted by the 1995 Deed shall continue as if there had been no such discharge or arrangement. Paragraph (2)(b) of the 1995 Deed violates mandatory rules of German law to the extent that it disregards the accessory nature of a German law pledge. As noted before, where the obligation to be secured has not come into existence or, upon coming into existence, has ceased to exist, the pledge has likewise not come into existence or has ceased to exist. Where such obligation is subject to a permanent defense, the pledge becomes unenforceable. Moreover, where the pledge itself has not come into existence or ceased to exist, because of discharge, avoidance or otherwise, it cannot be reinstated as provided in Paragraph (2)(g) of the 1995 Deed.

Bona Fide Purchaser: Pursuant to Paragraph 8(c)(ii), the dealings between the Collateral Taker and a *bona fide* purchaser shall be deemed valid and within the powers conferred by the 1995 Deed and the Security Collateral Provider's remedy shall be in damages only. Under German law the effects of *bona fide* dealings are set out in the Civil Code and cannot be expanded or supplemented by contractual provision. As noted in F.I. (B)(3)(c) above, the sale of Collateral is subject to the enforcement rules of the Civil Code. Where the sale of Collateral violates mandatory rules regarding the realization of the Collateral, a *bona fide* purchaser will acquire good title only if the Collateral is sold by a licensed broker or licensed auctioneer. Any other sale violating the liquidation rules of the Civil Code will be without effect (§§ 1243, 1244 Civil Code).

(2) Pledge of Cash

Pursuant to Paragraph 2(b), the Security Collateral Provider "charges and agrees to charge, with full title guarantee, in favour of the Collateral Taker by way of first fixed charge all Posted Collateral in the form of cash" (emphasis supplied). Here again, the English law terms and expressions used are not meaningful in German law. Nevertheless, it would appear to be likely that a German court would infer from the quoted language, and from other provisions of the 1995 Deed, that the parties intend to create a limited interest for security purposes, which would be, in terms of German law, a pledge (*Pfandrecht*). While the transfer of the ownership is not expressly excluded under the 1995 Deed in respect of Cash, as it is in respect of Securities, it seems unlikely that a German court would hold that the type of interest to be created by the 1995 Deed in respect of Cash should differ from the (security) interest to be created under the 1995 Deed in respect of Securities.

As has been explained above with regard to the pledge of Cash under the 1994 NY Annex (*see* (b)(2) immediately above), a pledge of Cash is conceivable under German law only in the form of a pledge of a payment claim. Clearly, a pledge of a payment claim is not purported to be made under the 1995 Deed, as it is not under the 1994 NY Annex. Accordingly, as concluded with respect to the 1994 NY Annex, the pledge of Cash as provided in the 1995 Deed does not constitute a meaningful agreement under German law. It is unlikely, therefore, that such pledge will be given effect whenever German law is to be applied.

(3) Legal consequences of the invalidity and ineffectiveness of provisions of the 1995 Deed

The invalidity of certain provisions of the 1995 Deed and the ineffectiveness of the pledge of Cash thereunder in circumstances where German law falls to be applied entails the risk that a German court may conclude in these circumstances that no security interest whatsoever will be created under the 1995 Deed.

Here, substantially the same considerations apply as are applicable in the case of the 1994 NY Annex. Reference is therefore made to the discussion of this topic in relation to the 1994 NY Annex (*see* (b)(3) immediately above). Similarly, we recommend not to use the 1995 Deed in circumstances where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law, unless it has been specifically amended so as to comply with the requirements of German law.

2. ***Under German law, what law governs the proprietary aspects of a security interest (that is, the formalities required to protect as security interest in Collateral against competing claims) granted by the Security Collateral Provider under each Security Document, the jurisdiction where the Collateral is located, or the jurisdiction of location of the Secured Party's Intermediary in relation to Collateral in the form of indirectly held securities)? What factors would be relevant to this question? Where the location (or deemed location) of the Collateral is the determining factor, please briefly describe the principles governing such determination under German law with respect to the different types of Collateral. In particular, please describe how German law applies to each form in which securities Collateral may be held under (x) the Non-IM Security Documents pursuant to assumption F.I.(g) above; (y) the IM Security Documents pursuant to assumptions F.I.(g)(iv) and (l) above and (z) the arrangements described in assumption F.I.(m) above.***

In respect of Securities, reference is made generally to the discussion under E.I.(A) above. With respect to the forms in which securities Collateral may be held under (x) the Non-IM Security Documents pursuant to assumption F.I.(g) above, (y) the IM Security Documents pursuant to assumptions F.I.(g)(iv) and (l) above and (z) the arrangements described in assumption F.I.(m), the following specific references are made:

(i) in respect of directly held bearer debt securities as described in assumption F.I.(g)(i) above, to the discussion under E.I.(A)(1)(b) above;

(ii) in respect of directly held registered debt securities as described in assumption F.I.(g)(ii) above, to the discussion under E.I.(A)(1)(c) above;

(iii) in respect of directly held dematerialized debt securities as described in assumption F.I.(g)(iii) above, to the discussion under E.I.(A)(1)(a) above; and

(iv) in respect of indirectly held debt securities as described in assumptions F.I.(g)(iv), F.I.(l) and F.I.(m) above, to the discussion under E.I.(A)(1)(a) above.

In respect of Cash, reference is made to the discussion under E.I.(B) above.

3. ***Would the German courts recognize a security interest in each type of Eligible Collateral created under each Security Document? In answering this question, please bear in mind the different forms in which securities Collateral may be held, as described in assumption F.I.(g) above with respect to Non-IM Security Documents, in assumptions F.I.(g) (iv) and (l) above with respect to IM Security Documents and in assumption F.I.(m). Please indicate, in relation to cash Collateral, if your answer depends on the location of the account in which the relevant deposit obligations are recorded and/or upon the currency of those obligations.***

(a) Securities

Subject as set out in the answer to question 2 above and subject to the discussion of insolvency matters under E.III.(B) and (C), if a security interest in Securities is valid, binding and enforceable in accordance with the law applicable under German conflict of laws rules German law will recognize such a security interest.

(b) Cash

The 1994 NY Annex provides for a pledge of Cash. For purposes of determining the validity of such pledge, as has been mentioned (*see* E.I.(B) above), a German court is likely to apply German law where the Cash is being transferred to an account of the Collateral Taker maintained with a bank in Germany. As outlined in E.II.(C)(1) above, under German law the pledge of Cash is conceivable in the form of the pledge of a payment claim. Pursuant to the terms of the 1994 NY Annex, however, the Security Collateral Provider does not pledge to the Collateral Taker a claim under an account which it maintains with a bank. Accordingly, the pledge of Cash as provided in the 1994 NY Annex does not constitute a meaningful agreement under German law and it is unlikely that it will be given effect whenever German law applies.

Pursuant to Paragraph 2(b) of the 1995 Deed, the Security Collateral Provider "charges and agrees to charge, with full title guarantee, in favour of the Collateral Taker by way of first fixed charge all Posted Collateral in the form of *cash*" (emphasis supplied). The English law terms and expressions used are not meaningful in German law. Nevertheless, it would appear to be likely that a German court would infer from the quoted language, and from other provisions of the 1995 Deed, that the parties intend to create a limited interest for security purposes, which would be, in terms of German law, a pledge (*Pfandrecht*). While the transfer of the ownership is not expressly excluded under the 1995 Deed in respect of Cash, as it is in respect of Securities, it seems unlikely that a German court would hold that the type of interest to be created by the 1995 Deed in respect of Cash should differ from the (security) interest to be created under the 1995 Deed in respect of Securities. As has been explained above with regard to the pledge of cash under the 1994 NY Annex, a pledge of Cash is conceivable under German law only in the form of a pledge of a payment claim. Clearly, a pledge of a payment claim is not purported to be made under the 1995 Deed, as it is not under the 1994 NY Annex. Accordingly, as concluded with respect to the 1994 NY Annex, the pledge of Cash as provided in the 1995 Deed does not constitute a meaningful agreement under German law. It is unlikely, therefore, that such pledge will be given effect whenever German law is to be applied.

Consequently, in the case that the account in which Cash (in whatever currency) is held is maintained with a bank in Germany, a security interest over Cash as perceived in the Security Documents is inconceivable in concepts of German law and would likely be without effect.

What has been set out above, applies *mutatis mutandis* to the IM Security Documents.

4. ***What is the effect, if any, under German law of the fact that the amount secured or the amount of Eligible Collateral subject to the security interest will fluctuate under the Master Agreement and the relevant Security Document (including as a result of entering into additional Transactions under that Master Agreement from time to time)? In particular:***

(a) would the security interest be valid in relation to future obligations of the Security Collateral Provider?

(b) would the security interest be valid in relation to future collateral (that is, Eligible Collateral not yet delivered to the Secured Party at the time of entry into the relevant Security Document)?

(c) is there any difficulty with the concept of creating a security interest over a fluctuating pool of assets, for example, by reason of the impossibility of identifying in the Security Documents the specific assets transferred by way of security?

(d) is it necessary under German law for the amount secured by each Security Document to be a fixed amount or subject to a fixed maximum amount?

(e) is it permissible under German law for the Secured Party as Secured Party to hold collateral in excess of its actual exposure to the Security Collateral Provider under the related Master Agreement?

(a) Creation of the security interest governed by German law

The recognition under German law of the validity and enforceability of a security interest in Eligible Collateral pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflicts rules, mandatorily governed by German law. Reference is made to the answer to question 1 above. Therefore, an answer to the questions set out under (a) to (e) above appears to be unnecessary.

(b) Creation of the security interest governed by foreign law

Where the creation of a security interest is governed by foreign law pursuant to German conflict of laws principles, the answers to the questions set out under (a) to (e) above are subject to applicable foreign law, with respect to which we are not in a position to express an opinion. If such applicable foreign law were to validate a security interest in Eligible Collateral in the circumstances described above, German law would also validate the security interest, subject to the discussion under E.III.(C)(1) above.

5. ***Assuming that the German courts would recognize the security interest in each type of Eligible Collateral created under each Security Document, is any action (filing, registration, notification, stamping, notarization or any other action or the obtaining of any governmental, judicial, regulatory or other order, consent or approval) required in Germany to perfect that security interest? If so, please indicate what actions must be taken and how such actions may differ depending on the type of Eligible Collateral in question.***

Irrespective of which law governs the creation of a security interest in Eligible Collateral, no filing, registration, notification, stamping, notarization or any other action or the obtaining of any governmental, judicial, regulatory or other order, consent or approval is required under German law.

6. ***If there are any other requirements to ensure the validity or perfection of a security interest in each type of Eligible Collateral created by the Security Collateral Provider under each Security Document, please indicate the nature of such requirements. For example, is it necessary as a matter of formal validity that the Security Document be expressly governed by German law or translated into any other language or for the Security Document to include any specific wording? Are there any other documentary formalities that must be observed in order for a security interest created under each Security Document to be recognized as valid and perfected under German law?***

Irrespective of which law governs the creation of a security interest and subject to the answer to question 4 above, no other requirements need to be observed under German law.

In particular, it is not required under German law that an agreement creating a security interest be expressly governed by German law, written in the German language or any specific wording be used.

7. ***Assuming that the Secured Party has obtained a valid and perfected security interest in the Eligible Collateral under German law, to the extent German law applies, by complying with the requirements set forth in the responses to questions (1) to (6) above, as applicable, will the Secured Party or the Security Collateral Provider need to take any action thereafter to ensure that the security interest in the Eligible Collateral continues and/or remains perfected, particularly with respect to additional Collateral transferred by way of security from time to time whenever the Credit Support Amount (or the amount of Collateral required to be delivered under the relevant Security Document, as applicable) exceeds the Value of the Collateral held by the Secured Party?***

The recognition under German law of the validity and enforceability of a security interest in Eligible Collateral pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law. Reference is made to the answers to questions 1 and 4 above. Therefore, an answer to this question appears to be unnecessary.

However, if the creation of a security interest is governed by foreign law pursuant to German conflict of laws principles, the answer is subject to applicable foreign law. Accordingly, we cannot express an opinion with regard to this question. If such applicable foreign law were to validate a security interest in securities, German law would also validate the security interest, subject to the discussion under E.III.(C)(1) above.

8. ***Assuming that (a) pursuant to German law, the laws of another jurisdiction govern the creation and/or perfection of a security interest in the Eligible Collateral transferred by way of security pursuant to each Security Document (for example, because such Collateral is located or deemed to be located outside of Germany) and (b) the Secured Party has obtained a valid and perfected security interest in the Eligible Collateral under the laws of such other jurisdiction, will the Secured Party have a valid security interest in the Collateral so far as German law is concerned? Is any action (filing, registration, notification, stamping or notarization or any other action or the obtaining or any governmental, judicial, regulatory or other order, consent or approval) required under German law to establish, perfect, continue or enforce this security interest? Are there any other requirements of the type referred to in question 6 above?***

As stated in the answer to question 3 above and subject to the discussion of insolvency matters under E.III., German law will recognize a security interest in Eligible Collateral validly created under the law applicable pursuant to German conflict of laws rules.

No action as described in questions 5 and 6 is required under German law to establish, perfect, continue or enforce a security interest in Eligible Collateral validly created under applicable foreign law. Moreover, it is not necessary that the Security Documents be expressly governed by the law of that jurisdiction, translated into the German language or include specific wording. No other documentary formalities must be observed in order for a security interest created under the Security Documents to be recognized in Germany.

9. ***Are there any particular duties, obligations or limitations imposed on the Secured Party in relation to the care of the Eligible Collateral held by it pursuant to each Security Document?***

The recognition under German law of the validity and enforceability of a security interest pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law. Reference is made to the answers to questions 1 and 4 above. Therefore, an answer to this question appears to be unnecessary.

However, if the creation of a security interest is subject to foreign law pursuant to German conflict of laws principles, we are not in a position to express an opinion with regard to this question.

10. ***Please note that pursuant to the terms of each Deed and the IM NY Annex, the Secured Party is not permitted to use any Collateral securities it holds. This is because (a) at the time that the Deed was published, it was thought, as a matter of English law, that any such use is or may be incompatible with the limited nature of the interest that the Secured Party has in the Collateral and (b) the rules promulgated by various regulators prohibit the use of any Collateral securities held by the Secured Party due to the Collateral being "initial margin". On the other hand, unless otherwise agreed to by the parties, Paragraph 6(c) of the 1994 NY Annex and the VM NY Annex grants the Secured Party broad rights with respect to the use of Collateral, provided that it returns equivalent Collateral when the Pledgor is entitled to the return of Collateral pursuant to the terms of the 1994 NY Annex or the VM NY Annex, as applicable. Such use might include pledging or rehypothecating the securities, disposing of the securities under a securities repurchase (repo) agreement or simply selling the securities. Does German law recognize the right of the Secured Party so to use such Collateral pursuant to an agreement with the Pledgor? In particular, how does such use of the Collateral affect, if at all, the validity, continuity, perfection or priority of a security interest otherwise validly created and perfected prior to such use? Are there any other obligations, duties or limitations imposed on the Secured Party with respect to its use of the Collateral under German law?***

The right of the Collateral Taker to use and dispose of Posted Collateral in the form of securities in accordance with Paragraph 6(c) of the 1994 NY Annex or the VM NY Annex, as applicable, violates basic concepts of German law regarding pledges and constitutes one of the attributes of the 1994 NY Annex and VM NY Annex that raises uncertainty about recognition of these arrangements under German law. Reference is made to the discussion under E.II.(B)(1)(c) and the answer to question 1 above.

11. ***What is the effect, if any, under German law on the validity, continuity, perfection or priority of a security interest in Eligible Collateral under each Security Document of the right of the Pledgor to substitute Collateral pursuant to Paragraph 4(d) of the 1994 NY Annex and the 1995 Deed? How does the presence or absence of consent to substitution by the Secured Party affect your response to this question? Please comment specifically on whether the Pledgor and the Secured Party are able validly to agree in the Security Document that the Pledgor may substitute Collateral without specific consent of the Secured Party and whether and, if so, how this may affect the nature of the security interest or otherwise affect your conclusions regarding the validity or enforceability of the security interest.***

The recognition under German law of the validity and enforceability of a security interest pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law. Reference is made to the answers to questions 1 and 4 above. Therefore, an answer to this question appears to be unnecessary.

However, if the creation of a security interest is governed by foreign law pursuant to German conflict of laws principles, we are not in a position to express an opinion with regard to this question.

Enforcement of Rights under the Security Documents by the Secured Party in the Absence of an Insolvency Proceeding

12. ***Assuming that the Secured Party has obtained a valid and perfected security interest in the Eligible Collateral under German law, to the extent such law applies, by complying with the requirements set forth in the responses to questions 1 to 6 above, as applicable, what are the formalities (including the necessity to obtain a court order or conduct an auction), notification requirements (to the Security Collateral Provider or any other person) or other procedures, if any, that the Secured Party must observe or undertake in exercising its rights as a Secured Party under each Security Document, such as the right to liquidate Collateral? For example, is it free to sell the Collateral (including to itself) and apply the proceeds to satisfy the Security Collateral Provider's outstanding obligations under the Master Agreement? Do such formalities or procedures differ depending on the type of Collateral involved?***

The recognition under German law of the validity and enforceability of a security interest pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law. Reference is made to the answer to question 1 above. Therefore, an answer to this question appears to be unnecessary.

13. ***Assuming that (a) pursuant to German law, the laws of another jurisdiction govern the creation and/or perfection of a security interest in the Eligible Collateral transferred by way of security pursuant to each Security Document (for example, because such Collateral is located or deemed located outside of Germany) and (b) the Secured Party has obtained a valid and perfected security interest in the Eligible Collateral under the laws of such other jurisdiction, are there any formalities, notification requirements or other procedures, if any, that the Secured Party must observe or undertake in Germany in exercising its rights as a Secured Party under each Security Document?***

If pursuant to German conflict rules the laws of a foreign jurisdiction govern the creation and/or perfection of a security interest in the Eligible Collateral under each Security Document, German substantive law is inapplicable and any formalities, notification requirements or other procedures that Party B must observe or undertake are subject to the laws of such foreign jurisdiction. If enforced in Germany, enforcement would be governed by, and subject to all formalities applicable under, German law (*see* E.III.(C)(1) above). No special registration of a foreign security interest is required under German law.

14. ***Are there any laws of regulations in Germany that would limit or distinguish a creditor's enforcement rights with respect to Collateral depending on (a) the type of transaction underlying the creditor's exposure, (b) the type of Collateral or (c) the nature of the creditor or the debtor? For example, are there any types of "statutory liens" that would be deemed to take precedence over a creditor's security interest in the Collateral?***

The recognition under German law of the validity and enforceability of a security interest pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by

German law. Reference is made to the answers to questions 1 and 4 above. Therefore, an answer to this question appears to be unnecessary.

However, if the creation of a security interest is governed by foreign law pursuant to German conflict of laws principles, the answer is subject to applicable foreign law with respect to which we cannot express an opinion. If enforced in Germany, enforcement would be governed by German law. There are no "statutory liens" that would be deemed to take precedence over a creditor's priority right in respect of a security interest determined by the time of creation (*see* E.II.(B)(1)(a)).

15. ***How would the responses to questions 12 to 14 above change, if at all, assuming that an Event of Default, Relevant Event or Specified Condition, as the case may be, exists with respect to the Secured Party rather than or in addition to the Security Collateral Provider? (For example, would this affect this ability of the Secured Party to exercise its enforcement rights with respect to the Collateral?)***

Our answers to questions 12 to 14 above are the same, assuming that an Event of Default, Relevant Event or Specified Condition, as the case may be, exists with respect to the Secured Party.

Enforcement of Rights under the Security Documents by the Secured Party After the Commencement of an Insolvency Proceeding

16. ***How are competing priorities between creditors determined in Germany? What conditions must be satisfied if the Secured Party's security interest is to have priority over all other claims (secured or unsecured) of an interest in the Eligible Collateral?***

(a) Priority between a secured creditor und unsecured creditors

As set out under E.III.(B)(1), in Insolvency Proceedings a secured creditor holding a security interest is entitled to realize the collateral by way of "separate liquidation" (*Absonderung*) in accordance with §§ 50 *et seq.*, §§ 166 *et seq.* of the Insolvency Code. This means that the secured creditor may seek preferential satisfaction out of the Collateral. Only the excess of the proceeds of the liquidation of the Collateral over the secured obligation is subject to the general distribution to the unsecured creditors. In other words, claims secured by a security interest take precedence over unsecured claims.

To the extent (i) the Insolvency Regulations apply and (ii) the Collateral is situated within the territory of another EC Member State at the time of the opening of such proceedings, a secured creditor's right to dispose of the Collateral or have it disposed of and to obtain satisfaction from the proceeds of or income from such Collateral is not affected by the opening of Insolvency Proceedings in Germany (Article 5(1) of the 2000 Insolvency Regulation and Article 8(1) of the 2000 Insolvency Regulation). Accordingly, the rules set out in the Insolvency Code on the realization of collateral and the preferential satisfaction of secured creditors entitled to separate liquidation do not apply.

(b) Priority between secured creditors

Where the Collateral is subject to one or more security interests in the form of a pledge (*Pfandrecht*) under German law, priority between creditors is determined, before as well as after commencement of Insolvency Proceedings, by reference to the time of creation of the pledge (*see* E.II.(B)(1)(a) above). The first pledge validly created in respect of the Collateral takes precedence over all subsequent pledges in the distribution of the proceeds upon separate liquidation of the Collateral. Reference is made to E.III.(B) above. This answer applies *mutatis mutandis* to foreign security interests which may be "transposed" into comparable German law security interests (*see* E.III.(C)(1)).

17. ***Would the Secured Party's rights under each Security Document, such as the right to liquidate the Collateral, be subject to any stay or freeze or otherwise be affected by commencement of the insolvency (that is, how does the institution of an insolvency proceeding change the responses to questions 12 and 13 above, if at all)?***

Prior to the opening of such proceedings, the insolvency court (*Insolvenzgericht*) may pursuant to § 21(1) of the Insolvency Code take appropriate actions to prevent a deterioration of the insolvent debtor's financial position, in particular by prohibiting dispositions over its assets (§ 21(2), 1st sentence, no. 2 of the Insolvency Code). This may affect a release of Collateral pledged or charged, as applicable, under a Security Document until such ban is lifted or insolvency proceedings are opened. However, pursuant to § 21(2), 2nd sentence, of the Insolvency Code, measures taken by the insolvency court (*Insolvenzgericht*) do not affect dispositions in respect of collateral provided under a Financial Collateral Arrangement.

Upon the institution of Insolvency Proceedings in Germany, any individual enforcement proceedings by secured or unsecured creditors against the insolvent debtor are suspended. With respect to the rights of the secured creditors to liquidate the Collateral according to the rules governing insolvency proceedings, reference is made to E.III.(B) above.

The recognition under German law of the validity and enforceability of a security interest pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflict rules, mandatorily governed by German law.

However, if a security interest is validly established under foreign law in accordance with each of the Security Documents, it may be enforced in an Insolvency Proceeding in compliance with German law if, as "transposed" (*see* E.III.(C)(1)), it is comparable with a German law type of security interest. In this regard, reference is made to the discussion under E.III.(C) above.

18. ***Will the Security Collateral Provider (or its administrator, provisional liquidator, conservator, receiver, trustee, custodian or other similar official) be able to recover any transfers of Collateral made to the Secured Party during a certain "suspect period" preceding the date of the insolvency as a result of such a transfer constituting a "preference" (however called and whether or not fraudulent) in favor of the Secured Party or on any other basis? If such a period exists, would the substitution of Collateral by a counterparty during this period invalidate an otherwise valid security interest if***

the substitute Collateral is of no greater value than the assets it is replacing? Would the posting of additional Collateral pursuant to the mark-to-market provisions of the Security Documents during the suspect period be subject to avoidance, either because the Collateral was considered to relate to an antecedent or pre-existing obligation or for some other reason?

The recognition under German law of the validity and enforceability of a security interest pursuant to the Security Documents is uncertain where the creation and effects of the security interest are, according to German conflicts rules, mandatorily governed by German law. Reference is made to the answers to questions 1 and 4 above. Therefore, an answer to this question appears to be unnecessary.

A security interest validly created pursuant to foreign law may be subject to avoidance under fraudulent conveyances rules by a German receiver, *see* E.III.(C)(3) above.

With respect to the substitution of, and the posting of additional, Collateral under the Security Documents, including the IM Security Documents, during any suspect period prior to the filing of an insolvency petition in Germany, such substitution or posting will fall under the voidable preference rules of German insolvency laws. Reference is made to E.III.(B)(3) and E.III.(C)(3) above.

Miscellaneous

19. ***Would the parties' agreement on governing law of each Security Document and submission to jurisdiction be upheld in Germany, and what would be the consequences if they were not?***

(a) Choice of Law

Regarding the choice of New York or English law, reference is made to the answer to question 1 above.

(b) Submission to Jurisdiction

(1) Annexes

The submission to the non-exclusive jurisdiction of the courts of the State of New York and the United States District Court located in the Borough of Manhattan in New York City, which is stipulated in Section 13(b) of the Master Agreement, is, subject to the following, valid and binding under German law.

According to § 38 of the Code of Civil Procedure (*Zivilprozeßordnung* – "**Procedure Code**"),[141] submission to the jurisdiction of the courts of a non-German jurisdiction must

141 The Regulation (EU) No 1215/2012 of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Official Journal no. L 351 of 20 December 2012, pp. 1 et seq.), as amended ("**Regulation on Jurisdiction**") is not applicable in the case of submission to the jurisdiction of a state or country (such as New York or the United States of America) which is not an EU Member State in which the Regulation on Jurisdiction applies, *cf.* Article 25(1) thereof.

be made in writing and requires that either (i) both parties be merchants, public law entities[142] or public law funds or (ii) at least one party does not have a place of general jurisdiction (*allgemeiner Gerichtsstand*)[143] in Germany. For these purposes, the expression "merchants" includes, without limitation, banks and other financial institutions, all corporations in the form of a stock corporation (*Aktiengesellschaft*) or limited liability company (*Gesellschaft mit beschränkter Haftung*), general or limited partnerships (*Offene Handelsgesellschaft* or *Kommanditgesellschaft*) and individuals or entities registered in the local commercial register.[144] A party will be deemed to have its principal place of business outside of Germany if its head office or the place in which its business decisions are actually taken (*tatsächlicher Hauptverwaltungssitz*) is located outside of Germany notwithstanding its place of incorporation and whether or not it maintains one or more branch(es) or representative office(s) or has assets in Germany.[145]

(2) Deed

As regards the submission to the jurisdiction of the English courts stipulated in Paragraph 11(g) of the 1995 Deed and Paragraph 11(j) of the IM Deed, we believe that, subject to what is stated, such submission is valid and binding under German law.

In the event that at least one party to the Master Agreement is domiciled or has its statutory seat, central administration or principal place of business[146] in Germany, the United Kingdom[147] or another EU Member State in which the Regulation on Jurisdiction applies,[148] the rules of the Regulation on Jurisdiction take precedence over § 38 of the Procedure Code. Article 25 of the Regulation on Jurisdiction provides that submission to the jurisdiction of the courts in an EU Member State in which the Regulation on Jurisdic-

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142 "Public law entities" would include German credit institutions organized under public law, such as the Landesbanken, Kreditanstalt für Wiederaufbau, Landwirtschaftliche Rentenbank and others.

143 With respect to individuals, the place of general jurisdiction is the place of domicile. The place of general jurisdiction for legal entities such as corporations is the principal place of business (*Sitz*). *See* §§ 13 *et seq*. of the Code of Civil Procedure (*Zivilprozeßordnung*).

144 §§ 6, 2 of the Commercial Code (*Handelsgesetzbuch*).

145 Geimer, Internationales Zivilprozeßrecht, 5th ed., 2005, note 1613; Kropholler, Handbuch des Internationalen Zivilverfahrensrechts, ch. III, note 504.

146 *See* Article 63(1) of the Regulation on Jurisdiction. Under German conflicts principles, the central administration is the head office or the place in which the business decisions are actually made (*tatsächlicher Hauptverwaltungssitz*).

147 For the purposes of the United Kingdom "statutory seat" means the registered office or, where there is no such office anywhere, the place of incorporation or, where there is no such place anywhere, the place under the law of which the formation took place, Article 63(2) of the Regulation on Jurisdiction.

148 The Regulation on Jurisdiction applies in all EC Member States except for Denmark. It does not apply in certain territories of EU Member States which are excluded from the Regulation on Jurisdiction according to Article 299 of the EC Treaty. The Brussels Convention continues to apply in Denmark and such territories.

tion applies requires an agreement in writing or in such other form as is standard practice among the parties or customary in international trade.[149] Accordingly, the submission to the jurisdiction of the English courts is effective under German law. Under the Regulation on Jurisdiction, such submission is exclusive.

Conversely, in the event that no party to the Master Agreement is domiciled or has its statutory seat, central administration or principal place of business (other than a branch) in an EC Member State in which the Regulation on Jurisdiction applies, the rules of the Procedure Code are applicable. Under § 38 of the Procedure Code, as more fully outlined above, the jurisdiction clause must be in writing and requires that either (i) both parties be merchants, public law entities or public law funds or (ii) at least one party has no place of general jurisdiction (*allgemeiner Gerichtsstand*) in Germany.

The jurisdictional clause of Paragraph 11(g) of the 1995 Deed or Paragraph 11(j) of the IM Deed, as applicable, is not qualified as exclusive or non-exclusive.[150] Under the Procedure Code, the submission to a specified jurisdiction is not presumed to be exclusive.[151] Conversely, under the Regulation on Jurisdiction an agreement on the submission to a specified jurisdiction is deemed to be exclusive unless the parties provide otherwise.[152] If the Regulation on Jurisdiction applies, in the absence of a specific agreement between the parties in Paragraph 13(l) of the 1995 Deed in regard of the non-exclusivity of the submission to the English courts, Paragraph 11(g) of the 1995 Deed would be considered as an exclusive jurisdictional provision. If, however, one party is a branch located and licensed to conduct banking business in Germany of a foreign financial institution pursuant to § 53 of the Banking Act, the place of jurisdiction pertaining to the branch may not be excluded by virtue of an agreement between the parties.[153] This restriction does not apply to branches established in Germany under § 53b of the Banking Act by banks which have their head office in other EC Member State.[154] Therefore, we believe that in the case that one party is a German branch of a foreign financial institution pursuant to § 53 of the Banking Act and an effort is made to enforce in Germany the submission to the exclusive jurisdiction of the English courts pursuant to Paragraph 11(g) of the 1995 Deed, such submission would not exclude the bringing of a suit in Germany relating to the business of the branch.

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149 Article 25(1), third sentence, (a), (b) or (c) of the Regulation on Jurisdiction.

150 Conversely, the jurisdictional clause contained in Section 13(b) of the Master Agreement which applies to the 1994 NY Annex and the 1995 Transfer Annex is expressed to be non-exclusive.

151 Hanseatisches Oberlandesgericht Hamburg, Recht der Internationalen Wirtschaft 1983, 125; Oberlandesgericht München, Neue Juristische Wochenschrift 1987, 2166.

152 Article 23(1), second sentence, of the Regulation on Jurisdiction.

153 § 53(3) of the Banking Act; *see* Geimer, *loc. cit.*, note 1462.

154 § 53b(1), second sentence, of the Banking Act.

20. ***Are there any other local law considerations that you would recommend the Secured Party to consider in connection with taking and realizing upon the Eligible Collateral from the Security Collateral Provider?***

There are no German law considerations that we would recommend the Secured Party to consider in connection with taking and realizing upon the Eligible Collateral from the Security Collateral Provider except for those expressed in this Memorandum.

21. ***Are there any other circumstances you can foresee that might affect the Secured Party's ability to enforce its security interest in Germany?***

There are no other circumstances that might affect the Secured Party's ability to enforce its security interest validly created under applicable foreign law in Germany other than those mentioned in this Memorandum.

G.
TITLE TRANSFER APPROACH
PURSUANT TO EACH TRANSFER ANNEX

I. Assumptions relating to each Transfer Annex

The facts are the same as set forth under F.I above, as modified below, provided that references to "Security Document(s)" shall be deemed to be references to "Transfer Annex(es)", references to "Security Collateral Provider" and "Secured Party" shall be deemed to be references to "Transferor" and "Transferee", respectively, references to "Eligible Collateral" shall be deemed to be references to "Eligible Credit Support". The assumptions made in F.I.(l) and (m) will not apply to this Part G. In addition, you have instructed us to assume the following facts for the discussion in Part G.II below:

(a) The Transferor has entered into a Master Agreement governed by English law and a Transfer Annex with the Transferee. Pursuant to the terms of each Transfer Annex, and as a matter of English law, transfers of Eligible Credit Support involve an outright transfer of title, free and clear of any liens, claims, charges or encumbrances or any other interest of the transferring party or of any third person (other than a lien routinely imposed on all securities in a relevant clearance system). If an Event of Default exists with respect to either party, an amount equal to the Value of the Credit Support Balance is deemed to be an Unpaid Amount under the Master Agreement and therefore is taken into account for purposes of determining the amount due upon close-out of the Transaction pursuant to Section 6(e) of the Master Agreement. Although such arrangement has an economic effect similar to the Collateral arrangements evidenced by the Security Documents, neither Transfer Annex is intended to create any form of security interest. There are also significant differences to the rights of the parties under each Transfer Annex, as further described in the description of the Credit Support Documents under C. above.

(b) Transfers under each Transfer Annex would not be recharacterized as creating a form of security interest by an English court, provided that the relevant Transfer Annex was not amended in any material way and provided further that the parties by their conduct did

not otherwise clearly evidence an intention to create a security interest in the transferred Collateral.

II. Questions and Answers relating to each Transfer Annex

D. ***For Transfer Annexes, would any of your responses to questions 22 through 29 below be different as a result of (a) the inclusion of the VM Transfer Annex in this Memorandum that was not previously included, or (b) the inclusion of equity securities as Eligible Collateral described in assumption F.I.(g)(4)?***

Our responses to questions 22 through 29 would be the same as a result of (a) the inclusion of the VM Transfer Annex in this Memorandum that was not previously included, or (b) the inclusion of equity securities as Eligible Collateral described in assumption F.I.(g)(4), provided that the discussion set out under F.II.A. above applies with the necessary changes where the parties in Paragraph 11(b) of the VM Transfer Annex specify the term "Covered Transactions" in a manner that it does not cover all Transactions under the relevant Master Agreement.

Please assume that the VM Transfer Annex is amended by the VM Transfer Annex IA Amendments. Would any of your responses to questions 1 through 21 below be different as a result of the inclusion of the VM Transfer Annex, as amended by the VM Transfer Annex IA Amendments, in this opinion?

No.

22. ***Does German law characterize each transfer of Eligible Credit Support as effecting an unconditional transfer of ownership in the assets transferred? Is there any risk that any such transfer would be recharacterized as creating a security interest? If so, is there any way to minimize such risk? What would be the consequences of such a recharacterization?***

Collateral arrangements in the form of an outright transfer of ownership as perceived by each Transfer Annex, are recognised in German law. With respect to Financial Collateral Arrangements, § 1(17), 1st sentence, of the Banking Act specifically addresses such arrangements in the form of Title Transfer Financial Collateral Arrangements. Thus, German law would give effect to each transfer of Eligible Credit Support as a full transfer of ownership and an effective payment of money, respectively, and there is no recharacterization risk. Reference is made to the discussion under E.II.(B)(4) and E.II.(D)(2) above.

23. ***Assuming that the Transferee receives an absolute ownership interest in the Eligible Credit Support, will it need to take any action thereafter to ensure that its title therein continues? Are there any filing or perfection requirements necessary or advisable, including taking any of the actions referred to in question 5? Are there any other procedures that must be followed or consents or other governmental or regulatory approvals that must be obtained to establish, enforce or continue such ownership interest?***

Where the Transferee receives an absolute ownership interest in the Eligible Credit Support, it will not need to take any action thereafter to ensure that its title therein conti-

nues. There are no filing or perfectionary requirements necessary or advisable, including taking any of the actions referred to in question 5 above. There are no other procedures that must be followed or consents or other governmental or regulatory approvals that must be obtained to establish, enforce or continue such ownership interest.

24. ***What is the effect, if any, under German law of the right of the Transferor to exchange Eligible Credit Support pursuant to Paragraph 3(c) of each Transfer Annex? Does the presence or absence of consent to exchange by the Transferee have any bearing on this question? Please comment specifically on whether the Transferor and the Transferee are able validly to agree in the Security Document that the Transferor may exchange Eligible Credit Support without specific consent of the Transferee and whether and, if so, how this may affect your conclusions regarding the validity or enforceability of each Transfer Annex.***

Paragraph 3(c) of each Transfer Annex will be enforceable as written. However, where German law applies to the transfer of ownership pursuant to German conflict of laws rules (*see* the discussion under E.I.(A) and (B)), the absence of consent to substitution by the Transferee would be held to constitute a refusal to agree to a transfer of ownership. Under German substantive law applicable pursuant to German conflict of laws rules, transfer of ownership (co-ownership) in securities applies requires an agreement between the transferor and the transferee that ownership (co-ownership) in the securities be transferred to the transferee, and the transfer of possession of the securities to the transferee (*see* the discussion under E.II.(B)(4)). Thus, in the circumstances described above, a requirement for effective transfer of ownership would be wanting.

25. ***The Transferee's rights in relation to the transferred Eligible Credit Support upon the occurrence of an Event of Default will be governed by Section 6 of the Master Agreement. Assuming that Section 6 of the Master Agreement is valid and enforceable under German law in so far as it relates to the determination of a net amount payable by either party on the termination of the Transactions, is Paragraph 6 of each Transfer Annex would also be valid to the extent that it provides for the Value of the Credit Support Balance to be included in the calculation of the net amount payable under Section 6(e) of the Master Agreement?***

Under Paragraph 6 of each Transfer Annex and Section 6(e) of the Master Agreement, in the event of an Early Termination Date occurring as a result of an Event of Default, an amount equal to the value of the Collateral furnished, whether of Securities or Cash, is to be taken into account in the calculations of the balance due upon close-out of the Transactions under the relevant Master Agreement.

These arrangements will be recognized and given effect to by a German court in the following circumstances:

(a) Non-insolvency-related Event of Default

Where the Early Termination Date occurs as a result of a non-insolvency-related Event of Default and there is no subsequent opening of Insolvency Proceedings in respect of the German Party in the context of such Event of Default, these arrangements will be recognized and given effect to by a German court.

(b) Insolvency-related Event of Default

Where the Early Termination Date occurs as a result of an insolvency-related Event of Default in respect of the German Party, the position is as follows:

(1) German substantive insolvency law not applicable

Where, in accordance with the rules of German international insolvency laws set out under VI. of the Netting Memorandum , German substantive insolvency law does not apply with respect to the enforceability of close-out netting under an Agreement, the arrangements described above will be recognized and given effect to by a German court.

(2) German substantive insolvency law applicable

Where, in accordance with the rules of German international insolvency laws set out under VI. of the Netting Memorandum, German substantive insolvency law does apply with respect to the enforceability of close-out netting under an Agreement, we refer to the discussion set out under VII.(C) of the Netting Memorandum. On the basis of this discussion, and subject to the qualifications and reservations set out therein, we are of the view that the contractual netting arrangement contained in Paragraph 6 of each Transfer Annex and Section 6(e) of the Master Agreement with respect to Collateral provided under a Collateral Financial Arrangement is valid and enforceable irrespective of whether the Transactions under the relevant Master Agreement fall within the scope of application of the statutory netting provisions.

The basis of this view is Article 7(1) of the EC Collateral Directive according to which EC Member States are required to ensure that a close-out netting provision can take effect in accordance with its terms, notwithstanding the commencement or continuation of winding-up proceedings in respect of the collateral provider and/or the collateral taker. A "close-out netting provision" is defined in Article 2(1)(n) of said Directive as

> "a provision of a financial collateral arrangement, or of an arrangement of which a financial collateral arrangement forms part, or, in the absence of any such provision, any statutory rule by which, on the occurrence of an enforcement event, whether through the operation of netting or set-off or otherwise:
>
> (i) the obligations of the parties are accelerated so as to be immediately due and expressed as an obligation to pay an amount representing their estimated current value, or are terminated and replaced by an obligation to pay such an amount; and/or
>
> (ii) an account is taken of what is due from each party to the other in respect of such obligations, and a net sum equal to the balance of the account is payable by the party from whom the larger amount is due to the other party."

Article 7(1) of the EC Collateral Directive aims to protect collateral arrangements the terms of which provide that, upon termination of the agreement that is collateralised, the

value of collateral provided may be combined with the secured claim into a single net claim.[155] Where such an arrangement is a Title Transfer Collateral Arrangement, it can only take effect upon the opening of Insolvency Proceedings against a party of such arrangement if the relevant close-out netting provision is enforceable in such proceedings, as the value of collateral provided can solely be realized through such close-out netting mechanism.

§ 104(1), 3rd sentence, no. 6 of the Insolvency Code lists Financial Collateral Arrangements within the meaning of § 1(17) of the Banking Act (through which part of the EC Collateral Directive has been implemented in German law) as one of the categories of "financial transaction" (*Finanzleistung*) within the meaning of § 104(1), 3rd sentence, of the Insolvency Code. This demonstrates the legislature's general intention to implement Article 7(1) of the EC Collateral Directive. For further details, we refer to the discussion set out under VII.(C) of the Netting Memorandum

(c) Excursus

For the purposes of the discussion above, we have considered whether or not an assignment or pledge by the Transferor of its (conditional or unconditional) claim for restitution of the Collateral to a third party or an attachment of such claim by a third party creditor of the Transferor, if occurring at any time preceding an Early Termination Date, would prevent or otherwise prejudice the inclusion of such claim in the calculation of the balance due on close-out.

These claims, whether conditional or unconditional, constitute assets of the Transferor. They qualify for being assigned or pledged or otherwise encumbered by the Transferor as the holder thereof in favour of any person and for being attached by a third party creditor of the Transferor. Clearly, for German law purposes, being claims arising under each Transfer Annex, they would be subject to English law, being the law governing each Transfer Annex. Likewise, the arrangements pursuant to Paragraph 6 of each Transfer Annex and Section 6(e) of the relevant Master Agreement regarding the netting of these claims on default are governed by English law.

Assuming that German law would govern these matters, we have concluded that neither an assignment of these claims (§§ 404, 406 Civil Code)[156] nor the pledging of these claims (§§ 1279, 1275, 404 Civil Code) nor an attachment of these claims (§ 392 Civil

155 Cf. recital (14) of the EC Collateral Directive which reads: "The enforceability of bilateral close-out netting should be protected, not only as an enforcement mechanism for title transfer financial collateral arrangements including repurchase agreements but more widely, where close-out netting forms part of a financial collateral arrangement. Sound risk management practices commonly used in the financial market should be protected by enabling participants to manage and reduce their credit exposures arising from all kinds of financial transactions on a net basis, where the credit exposure is calculated by combining the estimated current exposures under all outstanding transactions with a counterparty, setting off reciprocal items to produce a single aggregated amount that is compared with the current value of the collateral."

156 *See* Staudinger/Kaduk, *loc. cit.*, § 406, note 59; Palandt/Grüneberg, *loc.cit.*, § 406, note 2; Larenz, Schuldrecht I, 14th ed., 1987, § 34 IV, p. 592.

Code),[157] even when occurring at any time prior to an Early Termination Date, will affect in any way the inclusion of such claims into the calculation of the balance due on close-out.

26. ***Are the rights of the Transferee enforceable in accordance with the terms of the Master Agreement and each Transfer Annex, irrespective of the insolvency of the Transferor?***

Subject to the opinions and qualifications expressed elsewhere herein, we are of the opinion that such rights will be enforceable in accordance with their respective terms under German law, including insolvency laws.

Under German law a contract which is, pursuant to German rules of conflict of laws, validly governed by a foreign law, is binding under German substantive law, unless:

(a) it violates applicable mandatory provisions of German law (Article 3(3) and (4) of the Rome I Regulation); or

(b) it is obviously incompatible with fundamental principles of German law (*ordre public*). Article 21 of the Rome I Regulation sets out this general principle of law, the application of which will be decided upon by the German courts by reference to the circumstances of a particular case.

With respect to (a) above, we are of the view that none of the provisions of each Transfer Annex violates any mandatory provisions of German law which must be applied to the matters covered by them irrespective of the law by which they are governed. As has been mentioned before, the Insolvency Code constitutes, as a rule, mandatory provisions of German law. The enforceability of the rights of the Transferee in the insolvency of the Transferor has been discussed in the answer to question 25 above.

With respect to (b) above, we are of the opinion that none of the provisions of each Transfer Annex is obviously incompatible with fundamental principles of German law.

Although neither (i) nor (ii) below impairs in our view the enforceability of the rights of the Transferee under each Transfer Annex, we note the following:

(i) German conflict rules will require the application of German law in respect of the transfer of ownership of Collateral in the form of Securities on which, pursuant to German conflict of laws rules, German substantive law applies and will be likely to require the application of German law if Collateral in the form of Cash is transferred to an account maintained with a bank in Germany (*see* the answer to question 28 below). German conflict rules may require the application of laws other than English or German law in accordance with the conflict of law principles outlined above (*see* the discussion under E.I. above).

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157 *See* Bundesgerichtshof, Neue Juristische Wochenschrift 1968, 835; OLG Hamburg, Neue Juristische Wochenschrift 1952, 388; Palandt/Grüneberg, *loc.cit.*, § 392, note 2; Staudinger/Gursky, *loc. cit.*, § 392, note 20.

(ii) Where German law will apply to a transfer of Cash, the following needs to be observed: According to Paragraphs 3(a) and 5(a) of the 1995 Transfer Annex, the parties purport to transfer the ownership of cash from the Transferor to the Transferee by transfer of money into one or more bank accounts of the Transferee.

The concept that underlies Paragraph 5(a) of the 1995 Transfer Annex is misconceived from the perspective of German law. The reason is that in concepts of German law a sum of money placed or kept in an account with a bank does not convey ownership rights to the account holder, but merely a contractual claim of the account holder against his bank. In circumstances where German law applies, an account holder originating a funds transfer has no "ownership" in the cash standing to his credit in the account from which the transfer is made, but holds a contractual claim against the bank for payment of money. Similarly, the recipient of a funds transfer does not obtain "ownership" in the funds credited upon the transfer to his account, but holds a contractual claim against his bank for payment of money in amount equal to the sum that has been credited to his account.

Notwithstanding the misconception which, from the perspective of German law, underlies Paragraph 5(a) of the 1995 Transfer Annex, in our opinion a German court should view the purported transfer of ownership of cash simply as a payment of money by the Transferor to the Transferee which will be at the unrestricted disposal of the Transferee, in accordance with, and subject to, the provisions of the 1995 Transfer Annex.

27. ***Will the Transferor (or its administrator, provisional liquidator, conservator, receiver, trustee, custodian or other similar official) be able to recover any transfers of Eligible Credit Support made to the Transferee during a certain "suspect period" preceding the date of the insolvency? If so, how long before the insolvency does this suspect period begin? If such a period exists, would the substitution of Eligible Credit Support by a counterparty during this period invalidate an otherwise valid transfer, assuming the substitute assets are of no greater value than the asset they are replacing? Would the transfer of additional Eligible Credit Support pursuant to the mark-to-market provisions of each Transfer Annex during the suspect period be subject to avoidance, either because it was considered to relate to an antecedent or pre-existing obligation or for some other reason?***

In respect of matters of avoidance of transactions, including related "suspect periods", reference is made to the discussion under E.III.(B)(3) above.

28. ***Would the parties' agreement on governing law of each Transfer Annex and submission to jurisdiction be upheld in Germany, and what would be the consequences if it were not?***

(1) Agreement on Governing Law

As set out above (*see* E.II.(A)), German law distinguishes between the obligation to provide security and the creation (*Bestellung*) of the security interest.

Under German conflict of laws rules, the parties may freely choose the law governing the obligation to transfer ownership (Article 3(1) of the Rome I Regulation). Accordingly, the choice by the parties of English law to govern the obligation to transfer ownership as established under Paragraph 2 of each Transfer Annex is valid under German law.

However, the parties may not freely choose the law governing the creation of a security interest which under German conflict of laws rules is determined by mandatory rules. With respect to the relevant conflict rules regarding the transfer of ownership (or co-ownership) in Securities, we refer to the discussion under E.I.(A) above. As set out under E.I.(A)(3) above, the choice of English law to govern the transfer of ownership of Securities pursuant to each Transfer Annex will be recognized by German law in the following cases:

(a) Where, in the case of Securities in respect of which dispositions are booked in accounts with constitutive effect in favor of the transferee, the account entry in respect of such transfer is made with constitutive effect for such transferee by the principal or branch office of a custodian bank located in England or Wales.

(b) Where, in the case of Securities in respect of which dispositions are entered into a register with constitutive effect in favor of the transferee, the register is maintained under the supervision of England or Wales.

(c) Where, in the case of Securities other than those mentioned under (a) or (b) above, the law governing the Security provides that the transfer of ownership requires the delivery of a certificate, such certificate is physically located in England or Wales upon completion of such transfer.

(d) In the case of Securities other than those mentioned under (a) or (b) above,

    (i) where the law governing the Security provides that the transfer of ownership requires an indorsement, such indorsement is made in England or Wales;

    (ii) where the law governing the Security provides that the transfer of ownership requires both delivery and indorsement, the certificate is physically located upon completion of such transfer, and the indorsement is made, in England or Wales;

    (iii) where a Security bears a blank indorsement and may, under the laws which govern such Security, in such event be transferred by delivery alone, the certificate is physically located in England or Wales upon completion of such transfer.

(e) In the case of Securities other than those mentioned under (a), (b), (c) or (d) above, such Securities are governed by English law.

If under German conflict rules the transfer of ownership is subject to a law other than English law, German law should still recognize the choice of English law if such other

law were to give effect to the choice of English law (*see* the detailed discussion under E.I.(A)(3) above).

With respect to Collateral in the form of Cash, German conflict rules will be likely to require the application of German law if such Cash is transferred to an account maintained with a bank in Germany.

(2) Submission to English Jurisdiction

Each Transfer Annex forms part of the Master Agreement and has been prepared for use with Master Agreements subject to English law.[158] If each Transfer Annex is governed by English law, Section 13(b)(i) of each Master Agreement provides for the submission to the jurisdiction of the English courts. Such submission, subject to the requirements set out in the answer to question 19 above, is valid and binding under German law.[159]

29. ***Is each Transfer Annex in an appropriate form to create the intended outright transfer of ownership in the Eligible Credit Support to the Transferee? Are there any other requirements to be observed in Germany in order to ensure the validity of such transfer in each type of Eligible Credit Support by the Transferor under a Transfer Annex? For example, are there any other requirements of the type referred to in question 6?***

Subject as set out above, each Transfer Annex is in an appropriate form for purposes of German law. There are no other requirements to be observed in order to ensure the validity of any transfer of ownership in securities or payment of cash. There are, in particular, no requirements of the type referred to in question 6 above.

H.
SOME RECOMMENDATIONS

In the light of the conclusions contained in this Memorandum it would appear to be advisable, where a German entity either individually designated under B.1.(b) above or being within one of the categories set out under B.1.(b) above is a party to the Master Agreement:

(i) to use the Deed or a Transfer Annex, both being governed by English law, in those circumstances where, in view of the type of Collateral, German conflict rules refer to English law, it being understood that the enforcement in Germany of an English law security interest created under a Deed is subject to its "transposition" (*see* E.III.(C)(1) above) into a similar German law security interest;

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158 *Cf.* the preamble to each Transfer Annex and footnote 2 thereto.

159 It is our view that a German court should not consider such submission to be exclusive. Under Section 13(b) of the Master Agreement, the parties may also bring proceedings elsewhere in connection with the Master Agreement including the relevant Transfer Annex (*see* the preamble thereto). In the event that the Regulation on Jurisdiction governs such submission to the jurisdiction of the English courts, Article 23(1), 2nd sentence, of the Regulation on Jurisdiction provides that an agreement on jurisdiction under the Regulation on Jurisdiction shall be exclusive unless the parties have agreed otherwise. Therefore, the non-exclusive submission under a Master Agreement should be recognized by a German court.

(ii) to use an Annex, being governed by New York law, in those circumstances where, in view of the Collateral, German conflict rules point to New York law, it being understood that the enforcement in Germany of a New York law security interest created under an NY Annex is subject to its "transposition" (*see* E.III.(C)(1) above) into a similar German law security interest;

(iii) not to use a Deed and an Annex in those circumstances where, in view of the Collateral, German conflicts rules refer to German law, *i.e.*, in the case of Securities pursuant the rules described under E.I.(A) above and/or Cash to be transferred to an account maintained with a bank in Germany, unless the relevant document has been specifically amended so as to comply with the requirements of German law; and

(iv) to use a Transfer Annex in those circumstances where, in view of the Collateral, German conflict rules require the application of German law, *i.e.*, in respect of Securities pursuant the rules described under E.I.(A) above and/or Cash to be transferred to an account maintained with a bank in Germany, or of English law. From the perspective of German law alone, it would not matter if a Transfer Annex were, where appropriate, subjected to New York law instead of English law. Irrespective of whether subjected to English or New York law, it must in either case be understood that German law will not honour such choice of law to the extent German conflicts rules require the application of German law. Where that is the case, transfer of ownership will be governed by German law in respect of Collateral in the form of Securities, while a transfer of ownership of Collateral in the form of Cash, as perceived by each Transfer Annex, will not occur, since the transfer of Cash will be viewed merely as an effective payment of money (*see* E.I.(B) and E.II.(C)(1) above). German law will generally recognize a full ownership interest in respect of Collateral obtained by the Collateral Taker pursuant to each Transfer Annex. Therefore, if German conflict-of-laws principles refer to a law other than German law in respect of the transfer of ownership or the establishment of a security interest, it would appear to be preferable for the purpose of enforcement in Germany of the relevant collateral arrangement to use a Transfer Annex instead of any of the Security Documents.

I.
CLOSE-OUT AMOUNT PROTOCOL

We refer to the Close-out Amount Protocol published by ISDA on February 27, 2009 (the "**Close-out Amount Protocol**"). On the assumption that the changes intended by the Close-out Amount Protocol Protocol are effective as a matter of the governing law of the Covered Master Agreement (as defined in the Close-out Amount Protocol Protocol) and the relevant Credit Support Document, we confirm that the changes made by the Protocol including, without limitation, Annexes 10, 11 and 12 do not adversely affect the conclusions reached herein.

J.
COLLATERAL AGREEMENT NEGATIVE INTEREST PROTOCOL

We refer to the Collateral Agreement Negative Interest Protocol published by ISDA on May 12, 2014 (the "**Collateral Agreement Negative Interest Protocol**"). On the assumption that the changes intended by the Collateral Agreement Negative Interest Protocol are effective as

a matter of the governing law of the Protocol Covered Collateral Agreement (as defined in the Collateral Agreement Negative Interest Protocol), we confirm that the changes made by the Collateral Agreement Negative Interest Protocol including, without limitation, those set out in the Attachment thereto do not adversely affect the conclusions reached herein.

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HENGELER MUELLER
Partnerschaft von Rechtsanwälten mbB

(Haag) (Peters)

APPENDIX A

CERTAIN TRANSACTIONS UNDER THE ISDA MASTER AGREEMENTS

Basis Swap. A transaction in which one party pays periodic amounts of a given currency based on a floating rate and the other party pays periodic amounts of the same currency based on another floating rate, with both rates reset periodically; all calculations are based on a notional amount of the given currency.

Bond Forward. A transaction in which one party agrees to pay an agreed price for a specified amount of a bond of an issuer or a basket of bonds of several issuers at a future date and the other party agrees to pay a price for the same amount of the same bond to be set on a specified date in the future. The payment calculation is based on the amount of the bond and can be physically-settled (where delivery occurs in exchange for payment) or cash-settled (where settlement occurs based on the difference between the agreed forward price and the prevailing market price at the time of settlement).

Bond Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to purchase (in the case of a call) or sell (in the case of a put) a specified amount of a bond of an issuer, such as Kingdom of Sweden or Unilever N.V., at a specified strike price. The bond option can be settled by physical delivery of the bonds in exchange for the strike price or may be cash settled based on the difference between the market price of the bonds on the exercise date and the strike price.

Bullion Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to purchase (in the case of a call) or sell (in the case of a put) a specified number of Ounces of Bullion at a specified strike price. The option may be settled by physical delivery of Bullion in exchange for the strike price or may be cash settled based on the difference between the market price of Bullion on the exercise date and the strike price.

Bullion Swap. A transaction in which one party pays periodic amounts of a given currency based on a fixed price or a fixed rate and the other party pays periodic amounts of the same currency or a different currency calculated by reference to a Bullion reference price (for example, Gold-COMEX on the COMEX Division of the New York Mercantile Exchange) or another method specified by the parties. Bullion swaps include cap, collar or floor transactions in respect of Bullion.

Bullion Trade. A transaction in which one party agrees to buy from or sell to the other party a specified number of Ounces of Bullion at a specified price for settlement either on a "spot" or two-day basis or on a specified future date. A Bullion Trade may be settled by physical delivery of Bullion in exchange for a specified price or may be cash settled based on the difference between the market price of Bullion on the settlement date and the specified price.

For purposes of Bullion Trades, Bullion Options and Bullion Swaps, "Bullion" means gold, silver, platinum or palladium and "Ounce" means, in the case of gold, a fine troy ounce, and in the case of silver, platinum and palladium, a troy ounce (or in the case of reference prices not expressed in Ounces, the relevant Units of gold, silver, platinum or palladium).

Buy/Sell-Back Transaction. A transaction in which one party purchases a security (in consideration for a cash payment) and agrees to sell back that security (or in some cases an equivalent security) to the other party (in consideration for the original cash payment plus a premium).

Cap Transaction. A transaction in which one party pays a single or periodic fixed amount and the other party pays periodic amounts of the same currency based on the excess, if any, of a specified floating rate (in the case of an interest rate cap), rate or index (in the case of an economic statistic cap) or commodity price (in the case of a commodity cap) in each case that is reset periodically over a specified per annum rate (in the case of an interest rate cap), rate or index (in the case of an economic statistic cap) or commodity price (in the case of a commodity cap).

Collar Transaction. A collar is a combination of a cap and a floor where one party is the floating rate, floating index or floating commodity price payer on the cap and the other party is the floating rate, floating index or floating commodity price payer on the floor.

Commodity Forward. A transaction in which one party agrees to purchase a specified quantity of a commodity at a future date at an agreed price, and the other party agrees to pay a price for the same quantity to be set on a specified date in the future. A Commodity Forward may be settled by the physical delivery of the commodity in exchange for the specified price or may be cash settled based on the difference between the agreed forward price and the prevailing market price at the time of settlement.

Commodity Index Transaction. A transaction, structured in the form of a swap, cap, collar, floor, option or some combination thereof, between two parties in which the underlying value of the transaction is based on a rate or index based on the price of one or more commodities.

Commodity Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to purchase (in the case of a call) or sell (in the case of a put) a specified quantity of a commodity at a specified strike price. The option can be settled either by physically delivering the quantity of the commodity in exchange for the strike price or by cash settling the option, in which case the seller of the option would pay to the buyer the difference between the market price of that quantity of the commodity on the exercise date and the strike price.

Commodity Swap. A transaction in which one party pays periodic amounts of a given currency based on a fixed price and the other party pays periodic amounts of the same currency based on the price of a commodity, such as natural gas or gold, or a futures contract on a commodity (e.g., West Texas Intermediate Light Sweet Crude Oil on the New York Mercantile Exchange); all calculations are based on a notional quantity of the commodity.

Contingent Credit Default Swap. A Credit Default Swap Transaction under which the calculation amounts applicable to one or both parties may vary over time by reference to the mark-to-market value of a hypothetical swap transaction.

Credit Default Swap Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to enter into a Credit Default Swap.

Credit Default Swap. A transaction in which one party pays either a single fixed amount or periodic fixed amounts or floating amounts determined by reference to a specified notional amount, and the other party (the credit protection seller) pays either a fixed amount or an amount determined by reference to the value of one or more loans, debt securities or other financial instruments (each a "Reference Obligation") issued, guaranteed or otherwise entered into by a third party (the "Reference Entity") upon the occurrence of one or more specified credit events with respect to the Reference Entity (for example, bankruptcy or payment default). The amount payable by the credit protection seller is typically determined based upon the market value of one or more debt securities or other debt instruments issued, guaranteed or otherwise entered into by the Reference Entity. A Credit Default Swap may also be physically settled by payment of a specified fixed amount by one party against delivery of specified obligations ("Deliverable Obligations") by the other party. A Credit Default Swap may also refer to a "basket" (typically ten or less) or a "portfolio" (eleven or more) of Reference Entities or may be an index transaction consisting of a series of component Credit Default Swaps.

Credit Derivative Transaction on Asset-Backed Securities. A Credit Default Swap for which the Reference Obligation is a cash or synthetic asset-backed security. Such a transaction may, but need not necessarily, include "pay as you go" settlements, meaning that the credit protection seller makes payments relating to interest shortfalls, principal shortfalls and write-downs arising on the Reference Obligation and the credit protection buyer makes additional fixed payments of reimbursements of such shortfalls or write-downs.

Credit Spread Transaction. A transaction involving either a forward or an option where the value of the transaction is calculated based on the credit spread implicit in the price of the underlying instrument.

Cross Currency Rate Swap. A transaction in which one party pays periodic amounts in one currency based on a specified fixed rate (or a floating rate that is reset periodically) and the other party pays periodic amounts in another currency based on a floating rate that is reset periodically. All calculations are determined on predetermined notional amounts of the two currencies; often such swaps will involve initial and or final exchanges of amounts corresponding to the notional amounts.

Currency Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to purchase (in the case of a call) or sell (in the case of a put) a specified amount of a given currency at a specified strike price.

Currency Swap. A transaction in which one party pays fixed periodic amounts of one currency and the other party pays fixed periodic amounts of another currency. Payments are calculated on a notional amount. Such swaps may involve initial and or final payments that correspond to the notional amount.

Economic Statistic Transaction. A transaction in which one party pays an amount or periodic amounts of a given currency by reference to interest rates or other factors and the other party pays or may pay an amount or periodic amounts of a currency based on a specified rate or index pertaining to statistical data on economic conditions, which may include economic growth, retail sales, inflation, consumer prices, consumer sentiment, unemployment and housing.

Emissions Allowance Transaction. A transaction in which one party agrees to buy from or sell to the other party a specified quantity of emissions allowances or reductions at a specified price for settlement either on a "spot" basis or on a specified future date. An Emissions Allowance Transaction may also constitute a swap of emissions allowances or reductions or an option whereby one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to receive a payment equal to the amount by which the specified quantity of emissions allowances or reductions exceeds or is less than a specified strike. An Emissions Allowance Transaction may be physically settled by delivery of emissions allowances or reductions in exchange for a specified price, differing vintage years or differing emissions products or may be cash settled based on the difference between the market price of emissions allowances or reductions on the settlement date and the specified price.

Equity Forward. A transaction in which one party agrees to pay an agreed price for a specified quantity of shares of an issuer, a basket of shares of several issuers or an equity index at a future date and the other party agrees to pay a price for the same quantity and shares to be set on a specified date in the future. The payment calculation is based on the number of shares and can be physically-settled (where delivery occurs in exchange for payment) or cash-settled (where settlement occurs based on the difference between the agreed forward price and the prevailing market price at the time of settlement).

Equity Index Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to receive a payment equal to the amount by which an equity index either exceeds (in the case of a call) or is less than (in the case of a put) a specified strike price.

Equity Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to purchase (in the case of a call) or sell (in the case of a put) a specified number of shares of an issuer or a basket of shares of several issuers at a specified strike price. The share option may be settled by physical delivery of the shares in exchange for the strike price or may be cash settled based on the difference between the market price of the shares on the exercise date and the strike price.

Equity Swap. A transaction in which one party pays periodic amounts of a given currency based on a fixed price or a fixed or floating rate and the other party pays periodic amounts of the same currency or a different currency based on the performance of a share of an issuer, a basket of shares of several issuers or an equity index, such as the Standard and Poor’s 500 Index.

Floor Transaction. A transaction in which one party pays a single or periodic amount and the other party pays periodic amounts of the same currency based on the excess, if any, of a specified per annum rate (in the case of an interest rate floor), rate or index level (in the case of an economic statistic floor) or commodity price (in the case of a commodity floor) over a

specified floating rate (in the case of an interest rate floor), rate or index level (in the case of an economic statistic floor) or commodity price (in the case of a commodity floor).

Foreign Exchange Transaction. A deliverable or non-deliverable transaction providing for the purchase of one currency with another currency providing for settlement either on a "spot" or two-day basis or a specified future date.

Forward Rate Transaction. A transaction in which one party agrees to pay a fixed rate for a defined period and the other party agrees to pay a rate to be set on a specified date in the future. The payment calculation is based on a notional amount and is settled based, among other things, on the difference between the agreed forward rate and the prevailing market rate at the time of settlement.

Freight Transaction. A transaction in which one party pays an amount or periodic amounts of a given currency based on a fixed price and the other party pays an amount or periodic amounts of the same currency based on the price of chartering a ship to transport wet or dry freight from one port to another; all calculations are based either on a notional quantity of freight or, in the case of time charter transactions, on a notional number of days.

Fund Option Transaction: A transaction in which one party grants to the other party (for an agreed payment or other consideration) the right, but not the obligation, to receive a payment based on the redemption value of a specified amount of an interest issued to or held by an investor in a fund, pooled investment vehicle or any other interest identified as such in the relevant Confirmation (a "Fund Interest"), whether i) a single class of Fund Interest of a Single Reference Fund or ii) a basket of Fund Interests in relation to a specified strike price. The Fund Option Transactions will generally be cash settled (where settlement occurs based on the excess of such redemption value over such specified strike price (in the case of a call) or the excess of such specified strike price over such redemption value (in the case of a put) as measured on the valuation date or dates relating to the exercise date).

Fund Forward Transaction: A transaction in which one party agrees to pay an agreed price for the redemption value of a specified amount of i) a single class of Fund Interest of a Single Reference Fund or ii) a basket of Fund Interests at a future date and the other party agrees to pay a price for the redemption value of the same amount of the same Fund Interests to be set on a specified date in the future. The payment calculation is based on the amount of the redemption value relating to such Fund Interest and generally cash-settled (where settlement occurs based on the difference between the agreed forward price and the redemption value measured as of the applicable valuation date or dates).

Fund Swap Transaction: A transaction a transaction in which one party pays periodic amounts of a given currency based on a fixed price or a fixed rate and the other party pays periodic amounts of the same currency based on the redemption value of i) a single class of Fund Interest of a Single Reference Fund or ii) a basket of Fund Interests.

Interest Rate Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to receive a payment equal to the amount by which an interest rate either exceeds (in the case of a call option) or is less than (in the case of a put option) a specified strike rate.

Interest Rate Swap. A transaction in which one party pays periodic amounts of a given currency based on a specified fixed rate and the other party pays periodic amounts of the same currency based on a specified floating rate that is reset periodically, such as the London inter-bank offered rate; all calculations are based on a notional amount of the given currency.

Longevity/Mortality Transaction. (a) A transaction employing a derivative instrument, such as a forward, a swap or an option, that is valued according to expected variation in a reference index of observed demographic trends, as exhibited by a specified population, relating to aging, morbidity, and mortality/longevity, or (b) A transaction that references the payment profile underlying a specific portfolio of longevity- or mortality- contingent obligations, e.g. a pool of pension liabilities or life insurance policies (either the actual claims payments or a synthetic basket referencing the profile of claims payments).

Physical Commodity Transaction. A transaction which provides for the purchase of an amount of a commodity, such as oil including oil products, coal, electricity or gas, at a fixed or floating price for actual delivery on one or more dates.

Property Index Derivative Transaction. A transaction, often structured in the form of a forward, option or total return swap, between two parties in which the underlying value of the transaction is based on a rate or index based on residential or commercial property prices for a specified local, regional or national area.

Repurchase Transaction. A transaction in which one party agrees to sell securities to the other party and such party has the right to repurchase those securities (or in some cases equivalent securities) from such other party at a future date.

Securities Lending Transaction. A transaction in which one party transfers securities to a party acting as the borrower in exchange for a payment or a series of payments from the borrower and the borrower's obligation to replace the securities at a defined date with identical securities.

Swap Deliverable Contingent Credit Default Swap. A Contingent Credit Default Swap under which one of the Deliverable Obligations is a claim against the Reference Entity under an ISDA Master Agreement with respect to which an Early Termination Date (as defined therein) has occurred.

Swap Option. A transaction in which one party grants to the other party the right (in consideration for a premium payment), but not the obligation, to enter into a swap with certain specified terms. In some cases the swap option may be settled with a cash payment equal to the market value of the underlying swap at the time of the exercise.

Total Return Swap. A transaction in which one party pays either a single amount or periodic amounts based on the total return on one or more loans, debt securities or other financial instruments (each a "Reference Obligation") issued, guaranteed or otherwise entered into by a third party (the "Reference Entity"), calculated by reference to interest, dividend and fee payments and any appreciation in the market value of each Reference Obligation, and the other party pays either a single amount or periodic amounts determined by reference to a specified notional amount and any depreciation in the market value of each Reference Obligation.

A total return swap may (but need not) provide for acceleration of its termination date upon the occurrence of one or more specified events with respect to a Reference Entity or a Reference Obligation with a termination payment made by one party to the other calculated by reference to the value of the Reference Obligation.

Weather Index Transaction. A transaction, structured in the form of a swap, cap, collar, floor, option or some combination thereof, between two parties in which the underlying value of the transaction is based on a rate or index pertaining to weather conditions, which may include measurements of heating, cooling, precipitation and wind.

Appendix B

Certain Counterparty Types[160]

Description	**Covered by Memorandum**	**Legal form(s)**
Bank/Credit Institution. A legal entity, which may be organized as a corporation, partnership or in some other form, that conducts commercial banking activities, that is, whose core business typically involves (a) taking deposits from private individuals and/or corporate entities and (b) making loans to private individual and/or corporate borrowers. This type of entity is sometimes referred to as a "commercial bank" or, if its business also includes investment banking and trading activities, a "universal bank". (If the entity only conducts investment banking and trading activities, then it falls within the "Investment Firm/Broker Dealer" category below.) This type of entity is referred to as a "credit institution" in European Community (**EC**) legislation. This category may include specialised types of bank, such as a mortgage savings bank (provided that the relevant entity accepts deposits and makes loans), or such an entity may be considered in the local jurisdiction to constitute a separate category of legal entity (as in the case of a building society in the United Kingdom (**UK**)).	Covered by our Memorandum if the requirements set out under B.1.(b)(i)(1) of the Memorandum are met, subject to the reservations under B.2(b)(1) and (2).	Banks/Credit institutions in the legal form of a AG, GmbH, KGaA, eG, oHG, KG or public law institutions
Central Bank. A legal entity that performs the function of a central bank for a Sovereign or for an area of monetary union (as in the case of the European Central Bank in respect of the euro zone).	Covered by our Memorandum, see B.1.(b)(vi) of the Memorandum.	
Corporation. A legal entity that is organized as a corporation or company rather than a partnership, is engaged in	Covered by our Memorandum if the requirements set out under B.1.(b)(ix) of the Memo-	AG, GmbH, KGaA, eG

160 In these definitions, the term "legal entity" means an entity with legal personality other than a private individual.

industrial and/or commercial activities and does not fall within one of the other categories in this Appendix B.	randum are met.	
Hedge Fund/Proprietary Trader. A legal entity, which may be organized as a corporation, partnership or in some other legal form, the principal business of which is to deal in and/or manage securities and/or other financial instruments and/or otherwise to carry on an investment business predominantly or exclusively as principal for its own account.	Covered by our Memorandum if the requirements set out under B.1.(b)(ix) of the Memorandum are met.	InvAG and financial services institutions in the legal form of a AG, GmbH, KGaA, eG, oHG or KG
Insurance Company. A legal entity, which may be organised as a corporation, partnership or in some other legal form (for example, a friendly society or industrial & provident society in the UK), that is licensed to carry on insurance business, and is typically subject to a special regulatory regime and a special insolvency regime in order to protect the interests of policyholders.	Covered by our Memorandum if the requirements set out under B.1.(b)(i)(4) or (5) of the Memorandum are met, subject to the reservations under B.2(b)(3).	Insurance companies in the legal form of a AG, VVaG or public law institutions
International Organization. An organization of Sovereigns established by treaty entered into between the Sovereigns, including the International Bank for Reconstruction and Development (the World Bank), regional development banks and similar organizations established by treaty.	Covered by our Memorandum if the requirements set out under B.1.(b)(vii) of the Memorandum are met.	
Investment Firm/Broker Dealer. A legal entity, which may be organized as a corporation, partnership or in some other form, that does not conduct commercial banking activities but deals in and/or manages securities and/or other financial instruments as an agent for third parties. It may also conduct such activities as principal (but if it does so exclusively as principal, then it most likely falls within the "Hedge Fund/Proprietary Trader" category above.) Its business normally includes holding securities and/or other financial instruments for third parties and operating related cash accounts. This type of entity is referred to as a "broker-dealer" in US legislation and as an "investment firm" in EC legislation.	Covered by our Memorandum if the requirements set out under B.1.(b)(i)(2) of the Memorandum are met.	Investment firms in the legal form of a AG, GmbH, KGaA, eG, oHG or KG

Investment Fund. A legal entity or an arrangement without legal personality (for example, a common law trust) established to provide investors with a share in profits or income arising from property acquired, held, managed or disposed of by the manager(s) of the legal entity or arrangement or a right to payment determined by reference to such profits or income. This type of entity or arrangement is referred to as a "collective investment scheme" in EC legislation. It may be regulated or unregulated. It is typically administered by one or more persons (who may be private individuals and/or corporate entities) who have various rights and obligations governed by general law and/or, typically in the case of regulated Investment Funds, financial services legislation. Where the arrangement does not have separate legal personality, one or more representatives of the Investment Fund (for example, a trustee of a unit trust) contract on behalf of the Investment Fund, are owed the rights and owe the obligations provided for in the contract and are entitled to be indemnified out of the assets comprised in the arrangement.	Covered by our Memorandum if the requirements set out under B.1.(b)(i)(6) or B.1.(b)(ix) of the Memorandum are met, subject to the reservations under B.2(a).	
Local Authority. A legal entity established to administer the functions of local government in a particular region within a Sovereign or State of a Federal Sovereign, for example, a city, county, borough or similar area.	Covered by our Memorandum, see B.1.(b)(viii) of the Memorandum.	
Partnership. A legal entity or form of arrangement without legal personality that is (a) organised as a general, limited or some other form of partnership and (b) does not fall within one of the other categories in this Appendix B. If it does not have legal personality, it may nonetheless be treated as though it were a legal person for certain purposes (for example, for insolvency purposes) and not for other purposes (for example, tax or personal liability).	Covered by our Memorandum if the requirements set out under B.1.(b)(ix) of the Memorandum are met.	oHG, KG
Pension Fund. A legal entity or an arrangement without legal personality	Covered by our Memorandum if the requirements set out	

(for example, a common law trust) established to provide pension benefits to a specific class of beneficiaries, normally sponsored by an employer or group of employers. It is typically administered by one or more persons (who may be private individuals and/or corporate entities) who have various rights and obligations governed by pensions legislation. Where the arrangement does not have separate legal personality, one or more representatives of the Pension Fund (for example, a trustee of a pension scheme in the form of a common law trust) contract on behalf of the Pension Fund and are owed the rights and owe the obligations provided for in the contract and are entitled to be indemnified out of the assets comprised in the arrangement.	under B.1.(b)(ix) of the Memorandum are met.	
Sovereign. A sovereign nation state recognized internationally as such, typically acting through a direct agency or instrumentality of the central government without separate legal personality, for example, the ministry of finance, treasury or national debt office. This category does not include a State of a Federal Sovereign or other political sub-division of a sovereign nation state if the sub-division has separate legal personality (for example, a Local Authority) and it does not include any legal entity owned by a sovereign nation state (see "Sovereign-owned Entity").	Covered by our Memorandum, see B.1.(b)(viii) of the Memorandum.	
Sovereign Wealth Fund. A legal entity, often created by a special statute and normally wholly owned by a Sovereign, established to manage assets of or on behalf of the Sovereign, which may or may not hold those assets in its own name. Such an entity is often referred to as an "investment authority". For certain Sovereigns, this function is performed by the Central Bank, however for purposes of this Appendix B the term "Sovereign Wealth Fund" excludes a Central Bank.	Covered by our Memorandum if the requirements set out under B.1.(b)(ix) of the Memorandum are met.	
Sovereign-Owned Entity. A legal entity wholly or majority-owned by a Sovereign, other than a Central Bank, or by a State of a Federal Sovereign, which	Covered by our Memorandum if falling into one of the categories set out under B.1.(b)(i) to (viii) of the Memorandum	

may or may not benefit from any immunity enjoyed by the Sovereign or State of a Federal Sovereign from legal proceedings or execution against its assets. This category may include entities active entirely in the private sector without any specific public duties or public sector mission as well as statutory bodies with public duties (for example, a statutory body charged with regulatory responsibility over a sector of the domestic economy). This category does not include local governmental authorities (see "Local Authority").	or, if not so falling, the requirements set out under B.1.(b)(ix) of the Memorandum are met.	
State of a Federal Sovereign. The principal political sub-division of a federal Sovereign, such as Australia (for example, Queensland), Canada (for example, Ontario), Germany (for example, Nordrhein-Westfalen) or the United States of America (for example, Pennsylvania). This category does not include a Local Authority.	Covered by our Memorandum, see B.1.(b)(viii) of the Memorandum.	