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DEUTSCHLAND LLP

GERMAN LAW OPINION OF CLIFFORD CHANCE

ISSUED IN CONNECTION WITH

THE GENERAL AGREEMENT CONCERNING THE DELIVERY AND ACCEPTANCE OF NATURAL GAS TO THE EUROPEAN FEDERATION OF ENERGY TRADERS

7 JUNE 2017

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7 June 2017

Dear Sirs,

Legal Opinion Regarding the Enforceability of Close-Out Netting and the Validity and Enforceability of Collateral Arrangements, and Other Related Issues, under the EFET General Agreement Concerning the Delivery and Acceptance of Natural Gas

We refer to our instruction letter of 18 January 2017 in which we have been asked, as legal advisers to the European Federation of Energy Traders ("**EFET**"), to give an opinion in respect of the laws of the Federal Republic of Germany ("**Germany**") on the enforceability of close-out netting provisions (namely sections 10 and 11) of the EFET General Agreement Concerning the Delivery and Acceptance of Natural Gas (Version 2.0(a), published by EFET on 11 May 2007, which is either governed by the laws of Germany or by the laws of England and Wales (the "**General Agreement**")) (the "**Netting Provisions**"), the validity and enforceability of collateral provided under the EFET Credit Support Annex to the General Agreement (Version 2.0, published by EFET on 1 May 2010) (the "**Credit Support Annex**") and certain other related issues.

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1. DOCUMENTS CONSIDERED

For the purposes of this opinion (the "**Opinion**") we have considered the following documents:

(a) the General Agreement;

(b) the Credit Support Annex;

(c) the EFET Allowances Appendix to the General Agreement Concerning the Delivery and Acceptance of Natural Gas (Version 3.0, published 3 April 2012);

(d) Annex 2(A) to the EFET Allowances Appendix to the General Agreement Concerning the Delivery and Acceptance of Natural Gas (Version 2, published 20 July 2005) (including EUA, CER and ERU Transactions);

(e) the EFET Allowances Appendix to the General Agreement Concerning the Delivery and Acceptance of Natural Gas (Version 2.0, published 17 June 2008);

(f) the EFET VAT Annex for use with the EFET General Agreement Concerning the Delivery and Acceptance of Natural Gas (Version 1.0, published November 2005);

(g) for purposes of Paragraph 4.5 (Confirmation Practice) only: the EFET Electronic Confirmation Agreement (published 28 June 2005);

(h) for purposes of Paragraph 4.6 (Core Provisions) only: the EFET Cross Product Payment Netting Agreement (Version 1, published 20 October 2005); and

(i) for purposes of Paragraph 4.6 (Core Provisions) only: the CPMA Cross-Product Master Agreement (Version February 2000) as amended by the EFET/IECA Commodities Schedule to the Cross-Product Master Agreement (Version 1.0, published 23 June 2003).

This Opinion does not relate to any individual contract evidenced by a confirmation ("**Confirmation**") under the General Agreement ("**Individual Contracts**"). We do not opine on any tax, accounting, regulatory or related matters other than to the extent we express an opinion hereunder.

2. SCOPE OF REVIEW

2.1 The opinions given in this Opinion relate only to German law (including any EU regulations directly applicable in Germany) as applied by the German courts as at today's date. We express no opinion on the laws of any other jurisdiction, even where, under German law, a foreign law would be applicable. This Opinion expresses and describes German legal concepts in the English language rather than in their original form and such expressions and/or descriptions may not be fully reflective in their meaning of the underlying German law concepts. Any issues of interpretation arising in respect of the General Agreement and any Individual Contract (to the extent governed by German law) which are in the English language as well as this Opinion will be determined by the German courts in accordance with German law and we express no opinion on the interpretation that the German courts may give to any such expressions or descriptions. Please note in the general context of the aforesaid that German courts have held that, under German law, documents which are governed by German law may, if they have been executed in the English language, be interpreted with a view to the meaning of such English terms in an English legal environment.

2.2 We express no opinion as to any provisions of the agreements referred to in Paragraph 1(a) through 1(h) above, other than those to which express reference is made in this Opinion except insofar as any such provision relates to the effectiveness of the Netting Provisions.

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

2.4 This Opinion is given solely in respect of parties which are:[1]

(a) companies,

(b) partnerships,

(c) credit institutions,[2]

(d) financial services institutions,

(e) external investment management companies,[3] and

(f) insurance companies,[4]

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[1] We do not express an opinion on general regulatory restrictions, including investment guidelines, under the German Insurance Supervisory Act (*Versicherungsaufsichtsgesetz*; "**Insurance Supervisory Act**"), the German Covered Bond Act (*Pfandbriefgesetz*; "**Covered Bond Act**") or the German Capital Investment Code (*Kapitalanlagegesetzbuch*; "**Capital Investment Code**") or other regulatory laws or regulations regarding entities subject to further regulatory restrictions other than those generally applicable for all credit institutions or financial services institutions under the German Banking Act (*Kreditwesengesetz*; "**Banking Act**").

[2] We do not express an opinion on credit institutions holding a licence as a covered bond bank (*Pfandbriefbank*) with respect to any transactions relating to or included in the cover register (*Deckungsregister*) and we do not give an opinion on general regulatory restrictions under the Covered Bond Act.

[3] Please also refer to section 93 para 5 of the Capital Investment Code pursuant to which claims against an investment management company and claims belonging to fund assets cannot be set off against each other. However, this does not apply to master agreements for transactions pursuant to sections 197 para 1 sentence 1, 200, 203 of the Capital Investment Code or certain transactions with prime brokers.

[4] With respect to insurance companies, section 130 para 2 sent. 2 of the Insurance Supervisory Act imposes restrictions on the set-off of claims against claims held by insurance companies if the claim held by the insurance company belongs to its "cover assets" (*Sicherungsvermögen*) within the meaning of section 125 para 1 of the Insurance Supervisory Act. The cover assets are subject to certain investment restrictions pursuant to section 124 of the Insurance Supervisory Act to secure the financial stability of the insurance company. In addition, section 130 para 2 sent. 2 of the Insurance Supervisory Act provides that satisfaction

in each case incorporated, organised, established or formed under private law in accordance with the laws of Germany,

(g) the Federal Republic of Germany (*Bund*), Federal States (*Bundesländer*) of the Federal Republic of Germany and German municipalities (*Gemeinden*), and

(h) German public law entities with legal capacity (*rechtsfähige juristische Personen des öffentlichen Rechts*) in the form of a corporation (*Körperschaft des öffentlichen Rechts*) or an agency (*Anstalt des öffentlichen Rechts*).[5]

2.5 For purposes hereof, a reference to a "**company**", is a reference to a stock corporation (*Aktiengesellschaft*) incorporated under the German Stock Corporation Act (*Aktiengesetz*), or a European stock company (*Societas Europaea*) incorporated under the German Act on the Introduction of the European Company (*Gesetz zur Einführung der Europäischen Gesellschaft*),[6] or a limited liability company (*Gesellschaft mit beschränkter Haftung*) incorporated under the German Act on Limited Liability Companies (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung*). A reference to a "**partnership**" is a reference to a general partnership (*offene Handelsgesellschaft*) or a limited partnership (*Kommanditgesellschaft*) (including all permutations thereof) organised under the German Commercial Code (*Handelsgesetzbuch*) – the "**Commercial Code**". A reference to a "**credit institution**" is a reference to a credit institution (*Kreditinstitut*) within the meaning of section 1 para 1 of the Banking Act, and a reference to a "**CRR Credit Institution**" is a reference to a CRR credit institution (*CRR-Kreditinstitut*) as defined in section 1 para 3d sent. 1 of the Banking Act,[7] the home member state (as defined in Article 2 of the EU Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions ("**Winding-Up Directive**")[8]) of which is Germany,[9] and a reference to a "**European CRR**

of a third party by way of set-off against a claim contained in the cover assets is only permitted if the claim for the benefit of which any such set-off has been effected has to be allocated to the cover assets (section 125 paras. 1 to 3, section 126 para 3 and section 127 of the Insurance Supervisory Act) and if such allocation has actually been made.

5 We do not express an opinion on the capacity of any of the parties including those listed in Paragraphs 2.4(g) and 2.4(h). Please also refer to our Assumptions made under Paragraph 4.1(b).

6 Pursuant to Article 10 of the Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE), an SE is treated in every Member State as if it were a public limited-liability company formed in accordance with the law of the Member State in which it has its registered office. Thus, the provisions of the German Stock Corporation Act are applicable unless the provisions of the Council Regulation prevail.

7 Pursuant to Article 4 para 1 no 1 of Regulation 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation 648/2012 (OJ No L 321 of 30 November 2013, p. 6, "**CRR**") CRR credit institution means an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account.

8 OJ No L 125 of 5 May 2001, p. 15, as amended by Article 117 of the Directive 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

Institution" is a reference to a CRR Institution the home member state (*Herkunftsstaat*) of which is a state of the European Economic Area (the "**EEA**") (other than Denmark). A reference to a "**financial services institution**" is a reference to a financial services institution (*Finanzdienstleistungsinstitut*) within the meaning of section 1 para 1a of the Banking Act. A reference to an "**external investment management company**" (*externe Kapitalverwaltungsgesellschaft*) is a reference to an external investment management company within the meaning of section 18 of the Capital Investment Code. A reference to an "**insurance company**" is a reference to an insurance company (*Versicherungsunternehmen*) within the meaning of section 1 para 1 no. 1 of the Act on the Supervision of Insurance Companies (*Versicherungsaufsichtsgesetz*; "**Insurance Supervisory Act**"), a reference to a "**German insurance company**" is a reference to an insurance company the home state of which is Germany,[10] and a reference to an "**European insurance company**" is a reference to an insurance company the home member state of which is a state within the European Economic Area (other than Denmark).

This Opinion also applies to any non-German company ("**foreign company**") which is incorporated or established under the laws of another jurisdiction but with a branch or branches established or located in Germany. Where such foreign company is neither an insurance company, CRR Credit Institution, investment undertaking (*Wertpapierfirma*)[11] which provides services involving the holding of funds or

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Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council (OJ No L 173 of 12 June 2014, p. 190) ("**BRRD**"). The WUD is applicable to CRR Credit Institutions and their branches as defined under Article 4 para 1 no. 17 of the CRR set up in member states other than those in which they have their head offices ("**EU Branches**"), subject to the conditions and exemptions laid down in Article 2 para 5 of Directive 2013/36/EU 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 2006/49/EC (OJ No L 176 of 26 June 2013, p. 338, "**CRD IV**"). The Winding-Up Directive also applies to investment firms as defined Article 4 para 1 no. 2 of the CRR ("**CRR Investment Firms**", CRR Credit Institutions and CRR Investment Firms are together referred to as "**CRR Institutions**") and their EU Branches. It also applies to the financial institutions, firms and parent undertakings falling within the scope of the BRRD. If a CRR Credit Institution has its head office outside the EU, the Winding-Up Directive only applies if such CRR Credit Institution has at least two EU Branches.

9 According to section 1 para 4 of the Banking Act, the home member state is the state where a bank has its main office (*Hauptniederlassung*).

10 Section 61 para 1 sent. 1 of the Insurance Supervisory Act defines the term home state (*Herkunftsstaat*) as member or contracting state in which the undertaking has its seat. Section 312 para 2 sent. 1 of the Insurance Supervisory Act, which provides that insolvency proceedings regarding the assets of an insurance company in the EEA may only be opened by the competent authorities of the home state, implements Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the Reorganisation and Winding-up of Insurance Undertakings. Article 2 lit (e) of such Directive defines the term "home member state" (*Herkunftsmitgliedstaat*) as the member state of the EEA "in which an insurance undertaking has been authorised in accordance with Article 6 of Directive 73/239/EEC or Article 6 of Directive 79/267/EEC".

11 There is no definition of "investment undertaking" in EU directives but Article 4 (1) no. 1 of the Directive 2014/65/EU of the European Parliament and Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU ("**MiFID II**") defines the term "investment firm" to include 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 (see also *Virgos/Schmit*, Report on the Convention on Insolvency Proceedings, no. 59).

securities for third parties, nor a collective investment undertaking (*Organismen für gemeinsame Anlagen*), [12] it is assumed that each branch will constitute an "**establishment**" within the meaning of EU Council Regulation No. 1346/2000 of 29 May 2000 on insolvency proceedings, which applies to all EU member states other than Denmark (the "**EU Insolvency Regulation**"[13]).

2.6 **Defined terms and expressions**

Unless otherwise defined herein or the context requires otherwise, words and expressions used in this Opinion have the meanings and constructions ascribed to them in the General Agreement.

In this Opinion, unless otherwise specified:

(a) "**Party**" means a party to the General Agreement;

(b) references to a "**Paragraph**" are to a paragraph of this Opinion;

(c) a reference to "**Financial Collateral**" is a reference to an arrangement defined as such in section 1 para 17 sent. 1 and 2 of the Banking Act.[14]

The German wording of both the EU Insolvency Regulation (as defined below) and the MiFID II uses the term "*Wertpapierfirma*" which confirms this interpretation. Further, the English version of the Recast EU Insolvency Regulation (as defined below) now also uses the term "investment firm". Pursuant to Article 1 para 2 lit (c) of the Recast EU Insolvency Regulation, investment firms and other firms, institutions and undertakings would be covered by the (Recast) EU Insolvency Regulation insofar as they do not fall within the scope of the Winding-Up Directive (as amended).

[12] The term "collective investment undertaking" means, in accordance with Article 1 no. 2 of the Council Directive 86/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for the collective investment in transferable securities (UCITS) ("**UCITS Directive**" as amended) undertakings (i) the sole object of which is the collective investment in transferable securities 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 the holders, re-purchased or redeemed, directly or indirectly, out of those undertakings' assets. This interpretation is based on the assumption made by *Virgos/Schmit* (Report on the Convention on Insolvency Proceedings, no. 56 *et seq.*) according to which the rationale behind the exceptions provided in Article 1 para 2 of the EU Insolvency Regulation is to exclude such entities, which are subject to specific EU regulations and supervision by regulators in their respective EU member states. Investment undertakings that qualify as UCITS are regulated and supervised in accordance with the UCITS Directive and, hence, they are to be excluded from the scope of application of the EU Insolvency Regulation. From our point of view, this general analysis prevails over the wording of the EU Insolvency Regulation that might lead to the conclusion that the term "collective investment undertaking" within the meaning of the EU Insolvency Regulation corresponds to the equivalent term in the UCITS Directive according to which it is used for such undertakings which do not qualify as UCITS as defined in the UCITS Directive. It must be noted, however, that due to the lack of court precedents dealing with this topic a certain degree of uncertainty remains.

[13] OJ No L 160 of 30 June 2000, p. 1. The EU Insolvency Regulation will be replaced by the Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) of 20 May 2015, OJ (EU) No L 141 of 5 June 2015, p. 19 ("**Recast EU Insolvency Regulation**"). The Recast EU Insolvency Regulation will become effective, for the most part, on 26 June 2017.

[14] Financial collateral is defined in section 1 para 17 sent. 1 and 2 of the Banking Act as cash, securities, money market instruments and other credit claims within the meaning of Article 2 (1) (o) of the Directive

2.7 Interpretation

This Opinion may only be relied upon on the express condition that any issues of interpretation arising hereunder will be governed by and construed in accordance with German law and all disputes in relation to this Opinion shall be brought before the courts of Frankfurt/Main, Germany.

2.8 Non-official translations

Translations of German legal provisions into English are non-official translations and are provided by us for convenience only. The German version is the only binding version.

2.9 No Updating

We assume no duty to update this Opinion or inform EFET or any other person to whom a copy of this Opinion may be communicated of any change in German law (including, in particular, applicable court decisions), or any other circumstance that occurs, or is disclosed to us, after the date on which this Opinion is given, which might have an impact on the opinions given in this Opinion.

2.10 Assumptions and Reservations

The opinions given in this Opinion are given on the basis of the assumptions set out in Paragraph 4 (*Assumptions*) below and are subject to the reservations set out in Paragraph 6 (*Reservations*) below in each case in their entirety. The opinions given in this Opinion are strictly limited to the matters expressly stated in Paragraph 5 (*Opinions*) below and do not extend to any other matters.

3. EXECUTIVE SUMMARY

On the basis of the scope of review in Paragraph 2 and the assumptions in Paragraph 2 4 respectively, and subject to the reservations set out in Paragraph 6, this is an executive summary of the opinion expressed in Paragraph 5 with regard to close-out

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2002/47/EC of the European Parliament and the Council on financial collateral dated 6 June 2002 as amended by Directive 2009/44/EC (the "**Financial Collateral Directive**" or "**FCD**") and payment claims under an agreement pursuant to which an insurance undertaking within the meaning of section 1 para 1 of the Insurance Supervisory Act has granted credit in the form of a loan, in each case including all related rights or claims which have been transferred as collateral either by way of an *in rem* security arrangement (*beschränktes dingliches Sicherungsrecht*) or by way of a money transfer or by way of full title transfer on the basis of an agreement between a secured party and a security provider, each belonging to one of the categories named in Article 1 para 2 lit (a) to (e) of the Financial Collateral Directive. Should the security provider be a person or business undertaking named in Article 1 para 2 lit (e) of the Financial Collateral Directive, financial collateral is only given, if the collateral secures obligations arising under agreements or the procurement of agreements which serve

(a) the acquisition and sale of financial instruments,

(b) repurchase, lending or similar transactions on financial instruments or,

(c) loans to finance the acquisition of financial instruments."

netting only. This executive summary does not form part of this Opinion and is provided for ease of reference only, and in no circumstances may be interpreted or read as amending, affecting or having any interpretative effect on the opinion expressed in Paragraph 5, which is the only opinion which can be relied upon. Reading this executive summary does not substitute reading the entire Opinion.

(a) Close-out netting based on a non-insolvency related termination event exercised before the opening of Insolvency Proceedings is generally enforceable (see Paragraph 5.1.1(i)(i) and Paragraph 5.1.1(i)(ii)(A) below).

(b) The Resolution Act contains far-reaching powers of the Resolution Authority that may affect Resolution Firms and their creditors (see Paragraph 5.1.1(d)(D) below). These powers include, *inter alia*, the conversion into equity as well as the write-off of liabilities of a relevant Resolution Firm and the temporary suspension of payment and delivery obligations or of rights to enforce a security interest. Affected creditors must not exercise early termination rights on the basis of the imposition of resolution measures provided that the main obligations including obligations to provide security under the relevant agreements continue to be performed.

(c) Close-out netting based on an insolvency related termination event exercised prior to the point in time in which, based on a valid application for the opening of Insolvency Proceedings, the opening of Insolvency Proceedings is to be seriously expected (*mit der Eröffnung eines Insolvenzverfahrens ernsthaft zu rechnen ist*) should generally be enforceable (see Paragraph 5.1.1(i)(ii)(A) below).

(d) Close-out netting based on an insolvency related termination event should generally be enforceable with respect to all Individual Contracts that fall within the scope of application of section 104 of the German Insolvency Code (*Insolvenzordnung*, "**Insolvency Code**") (i.e. Individual Contracts that constitute a fixed date transaction or a financial transaction within the meaning of that provision) (see Paragraph 5.1.1(i)(ii)(C) below) and the results of such close-out netting should be determined by the terms of the General Agreement provided that the early termination has occurred before the opening of Insolvency Proceedings, subject to limitations imposed on the method for calculating a close-out amount by application of the restrictions under sections 104 para 4, 119 of the Insolvency Code (see Paragraph 5.1.1(i)(ii)(G) below) and subject to any challenge rights of an Insolvency Administrator (see Paragraph 5.1.1(c) below).

(e) The clauses with regard to automatic termination in the event of insolvency should generally be upheld by a German court (see Paragraph 5.1.1(i)(ii)(B) below), with respect to Individual Contracts falling within the scope of application of section 104 of the Insolvency Code (i.e. Individual Contracts that constitute a fixed date transaction or a financial transaction within the meaning of that provision) (see Paragraph 5.1.1(i)(ii)(D) below), subject to limitations imposed on the method for calculating a close-out amount by application of the restrictions under sections 104 para 4, 119 of the Insolvency Code (see Paragraph 5.1.1(i)(ii)(I) below) and subject to any challenge rights of an Insolvency Administrator (see Paragraph 5.1.1(c) below).

(f) With respect to Individual Contracts falling within the scope of application of section 104 of the Insolvency Code (see Paragraph 5.1.1(i)(ii)(C) below) the determination of the Termination Amount would generally be enforceable in the event of insolvency, see Paragraph 5.1.1(i)(i)(B), subject to the limitations imposed on the method for calculating a close-out amount by application of the restrictions under sections 104 para 4, 119 of the Insolvency Code (see Paragraph 5.1.1(i)(ii)(I) below) and subject to any challenge rights of an Insolvency Administrator (see Paragraph 5.1.1(c) below).

(g) Upon the opening of Insolvency Proceedings, all Individual Contracts not yet terminated in accordance with the General Agreement would either terminate by virtue of section 104 of the Insolvency Code if falling within its scope of application or become subject to the Insolvency Administrator's right to decide whether to assume or reject such contracts ("**Selection Right**" - such "selection right" by the Insolvency Administrator often being referred to as "cherry-picking" right) under section 103 of the Insolvency Code (see Paragraph 5.1.1(i)(ii)(A) below).

4. ASSUMPTIONS

4.1 Assumptions Relating to the Parties

(a) Two Parties enter into the General Agreement and at least one of the Parties is incorporated or organised or has its centre of main interest in Germany ("**Party A**").

(b) Each Party is, and will continue to be, a validly existing legal entity with capacity, power and authority under any applicable laws to enter into and perform its obligations under the General Agreement and any Individual Contract that may be entered into by the Parties, and each of the Parties have taken all necessary steps to execute, deliver and perform the General Agreement and any Individual Contract and to ensure their legal validity.

(c) None of the Parties qualifies as a consumer (*Verbraucher*) within the meaning of section 13 of the German Civil Code (*Bürgerliches Gesetzbuch*), i.e. a natural person entering into a legal transaction for a purpose which belongs neither to its commercial business nor to its self-employed business, but qualifies – as applicable – as a merchant (*Kaufmann*) within the meaning of section 1 of the Commercial Code or as an entrepreneur (*Unternehmer*) within the meaning of section 14 of the German Civil Code, i.e. any natural or legal person or partnership entering into a legal transaction in the course of its commercial business or its self-employed business.

(d) Where any authority or power of attorney (including sub-power of attorney) has been used in connection with the General Agreement or any Individual Contract, or any decisions or operations contemplated thereby, such authority or power of attorney and its communication to other parties had/have under all applicable laws the effect of binding the person or entity purportedly represented under such authority or power of attorney and such power of attorney has not been revoked prior to such execution.

(e) The General Agreement and any Individual Contract entered into thereunder have been duly authorised, executed and delivered by each Party in accordance with all applicable laws and the General Agreement and any Individual Contract have been properly completed by the Parties.

(f) Each of the Parties has obtained, complied with the terms of, and maintained all authorisations, approvals, licences and consents required to enable it to lawfully enter into, and perform its obligations under the General Agreement and any Individual Contract and to ensure the legality, validity, enforceability or admissibility in evidence of the General Agreement and any Individual Contract.

(g) None of the Parties is entitled to claim in relation to itself or its assets immunity from suit, attachment, execution or other legal process. However, insofar as the Federal Republic of Germany, any German Federal State (*Bundesland*) and any entity established under German public law that enters into the General Agreement as a Party, the execution of the General Agreement and Individual Contracts constitutes, and the exercise of that Party's rights and performance of its obligations thereunder will constitute, private and commercial acts done and performed for private and commercial purposes.

4.2 **Assumptions Relating to the General Agreement and Individual Contracts**

(a) The relevant General Agreement is governed by the laws of Germany or the laws of England. Where the relevant General Agreement is governed by the laws of England, under the laws of England (including its insolvency laws) and under all other relevant laws (other than the law of this jurisdiction):

(i) the relevant General Agreement constitutes and will at all times constitute valid and legally binding obligations of the Parties thereto, enforceable in accordance with its terms;

(ii) the choice of the laws of England as the governing law of the relevant General Agreement is a valid and binding selection; and

(iii) the Netting Provisions are valid and enforceable.

(b) On the basis of the terms and conditions of the General Agreement and other relevant factors, and acting in a manner consistent with the intentions stated in the General Agreement, the Parties over time enter into a number of Individual Contracts which belong to the Individual Contracts described in Annex 3.

(c) The Individual Contracts provide for the physical delivery of commodities or emission rights in exchange for cash, however, some of them may also provide for cash settlement or, in the event that offsetting physical delivery obligations are entered at different times, may be settled by agreement through the combination of, as applicable, a partial or total cancellation of otherwise offsetting physical delivery obligations, coupled with a net financial payment.

(d) Save for any specification in the election sheet contained in the General Agreement (the "**Election Sheet**"), none of the terms of the General Agreement will be varied, waived or discharged and any Individual Contract entered into after the date of this Opinion will be entered into as specified in the General Agreement and the General Agreement and each Individual Contract cannot be voided or otherwise held ineffective (in whole or in part) by reason of mistake, illegality or otherwise.

(e) Subject to a termination for Material Reason, each Party will perform its obligations under the General Agreement and any Individual Contract in accordance with their respective terms and nothing in the terms of any Individual Contract contradicts the assumptions set out in this Paragraph 4 or the reservations set out in Paragraph 6 below.

(f) The Individual Contracts constitute and will at all times constitute valid and legally binding obligations of the Parties thereto, enforceable in accordance with their terms with the valid and enforceable Netting Provisions prevailing over any netting provisions under the Individual Contracts.

(g) None of the Individual Contracts or operations contemplated by the General Agreement will infringe the terms of, or constitute a default under, any trust deed, debenture, agreement or other instrument or obligation to which any of the Parties to the General Agreement or an Individual Contract is a Party or by which any of its property, undertaking, assets or revenues are bound.

(h) Where Individual Contracts are governed by laws other than the laws of Germany, this Opinion is given exclusively in respect of those Individual Contracts which are capable under their governing laws, of being included in the General Agreement and of being terminated and set-off in accordance with the provisions of the General Agreement.

(i) The obligations under the General Agreement and any Individual Contract are mutual between the Parties. "**Mutuality**" (*Gegenseitigkeit*) generally exists where each Party is personally and solely liable as regards obligations owed by it and is solely entitled to the benefit of obligations owed to it. Circumstances in which the requisite mutuality will not be established include, without limitation, where a Party is acting as agent for another person, or is a trustee, or in respect of which a Party has a joint interest (including partnership) or such in respect of which a Party's rights or obligations or any interest therein have been assigned, charged or transferred (whether in whole or in part) whether unilaterally, by agreement or by operation of law.

(j) All of the representations and warranties given by any of the Parties to the General Agreement or any Individual Contract (other than representations and warranties as to such matters of German law on which we express an opinion herein) are and will be, when made or repeated or when deemed to be made or repeated (as the case may be), and were at all relevant times, true and accurate. Any representation or warranty given by any of the Parties to the General Agreement or any Individual Contract (other than representations and warranties as to such matters of German law on which we express an opinion herein) that such Party is not aware of or has no notice of any act, matter, thing or circumstance means that the same does not exist or has not occurred.

4.3 **Assumptions relating to the Credit Support Annex**

(a) The Eligible Credit Support provided under the Credit Support Annex only takes the form of Cash (as defined therein) and Letters of Credit (as defined therein).

(b) The provision and creation of Eligible Credit Support is not restricted by law, contractual agreement, court order, procedural, administrative or other rulings. We give no opinion on the ownership of any of the Parties to any Eligible Credit Support or on the legal existence of any Eligible Credit Support.

(c) At the time of the transfer of Cash under section 7 of the Credit Support Annex the transferor is the unrestricted owner of the transferred Cash and entitled to dispose of the transferred Cash, which at that time is unencumbered.

(d) All necessary steps and requirements for the valid and legally binding creation of the Eligible Credit Support that are required pursuant to the laws applicable to the creation of the Eligible Credit Support have been taken or fulfilled in order to effect such transfer. Please note that in relation to each relevant Eligible Credit Support and its creation the applicable law has to be determined and complied with.

(e) The rights of each relevant Transferor in connection with the provision of Eligible Credit Support are not subject to any lien, right of rescission, counterclaim, set-off or other defence and the performance of any of the terms of any Eligible Credit Support or the exercise of any rights will not render such Eligible Credit Support unenforceable in whole or in part or subject it to such lien, right of rescission, set-off, counterclaim or defence.

4.4 ***Bona Fide* Purpose and Insolvency**

(a) In respect of the General Agreement and each Individual Contract:

(i) each of the Parties has entered into and will enter into the same in good faith and for the purpose of carrying on its business;

(ii) each of the Parties has entered into and will enter into the same on arm's length commercial terms;

(iii) each of the Parties has and will have reasonable grounds for believing that the same will benefit it; and

(iv) none of the Parties has entered into or will enter into the same if entering into the same would prejudice any of its creditors.

(b) None of the Parties is or would (as a consequence of entering into the General Agreement or each Individual Contract or performing any obligation or allowing or doing any act or thing which the General Agreement or each Individual Contract contemplates, permits or requires such Party to do) be in each case within the meaning of sections 16 *et seqq*. of the Insolvency Code:

(i) in a stoppage of payment situation (including German law *Zahlungsunfähigkeit*); or

(ii) a status of overindebtedness (including German law *Überschuldung*); or

(iii) in any other situation justifying an application for the opening of Insolvency Proceedings under German law or in any analogous situation as contemplated by the laws of any jurisdiction other than Germany.

At the time at which the General Agreement or any Individual Contract is entered into neither Party has actual notice of the insolvency of the other Party and no Regulatory Proceedings as outlined under Paragraph 5.1.1(d) have been commenced.

5. OPINION AND LEGAL ANALYSIS

5.1 Enforceability of Close-out Netting

5.1.1 Winding-up, Insolvency or Attachment

(a) *Brief general discussion of the relevant German insolvency proceedings, laws and terminology applicable to the Parties and the contract types listed in the Annex*

The main procedures (*Hauptverfahren*) under the Insolvency Code are the only insolvency procedures (for example liquidation, administration, receivership or voluntary arrangement) to which a Party would be subject in Germany.

The main procedures[15] pursuant to the Insolvency Code are together called **"Insolvency Proceedings"**.[16] A Party which is insolvent is called the **"Insolvent Party"** and the other Party is called the **"Solvent Party"**.**"Insolvency Administrator"** [17] means a liquidator, administrator, administrative receiver or analogous or equivalent official appointed under the Insolvency Code in Germany.

In this Opinion, in relation to Insolvency Proceedings under the laws of Germany, the opening of Insolvency Proceedings refers to the time of the issue of an order of commencement *(Eröffnungsbeschluss)* by the competent insolvency court of Insolvency Proceedings. The point in time of formal commencement of Insolvency Proceedings (i.e. the opening of Insolvency Proceedings) is in all likelihood not the point in time in which a party is insolvent.

Insolvency Proceedings over the assets of either a credit institution, a financial services institution or an insurance company may only be instituted by the German Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* – **"BaFin"**) (section 46b para 1 sent. 4 of the Banking Act, section 312 para 1 of the Insurance Supervisory Act) by filing a petition for commencement of Insolvency Proceedings with the competent insolvency court.[18] To avert Insolvency Proceedings with respect to credit and financial

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15 As opposed to any preliminary proceedings immediately following the filing for insolvency but before the opening of main proceedings – preliminary insolvency proceedings (*Vorverfahren*).

16 As a matter of principle, the Insolvency Code does not provide for group insolvency proceedings, i.e. each Insolvent Party being part of a group of companies would be subject to separate proceedings which may involve different Insolvency Administrators. On 13 April 2017, the German Parliament (*Bundestag*) has adopted a law to facilitate the management of group insolvencies (*Gesetz zur Erleichterung der Bewältigung von Konzerninsolvenzen,* BGBl. 2017 I, p. 866 *et. seqq*.) which will enter into force on 21 April 2018. The law introduces changes to the Insolvency Code which, *inter alia*, allow an insolvent debtor in respect of which Insolvency Proceedings are being opened in Germany and being part of a group of companies in Germany to request the court to declare itself competent in respect of any subsequent proceedings of any member of the group in Germany. In the absence of any conflicts of interest, it may be possible for the same Insolvency Administrator to be appointed for all group companies. In addition, the new law provides for rules governing the cooperation between insolvency courts and Insolvency Administrators.

17 Where an insolvency court has, upon application of the Insolvent Party ordered the management of the Insolvent Party to continue its activities in accordance with section 270 of the Insolvency Code (*Eigenverwaltung*, self administration proceedings), numerous rights which normally would belong to the Insolvency Administrator may be exercised by the Insolvent Party itself (e.g. the Selection Right as further referred to in Paragraph 5.1.1(i)(ii)(A), see section 279 of the Insolvency Code) or by a creditors' trustee (*Sachwalter*) (e.g. any challenging rights in accordance with section 129 *et seq*. of the Insolvency Code as further referred to in Paragraph 5.1.1(c), see section 280 of the Insolvency Code).

18 Accordingly, pursuant to sections 46b para 1 sent. 1 of the Banking Act, section 311 para 1 sent. 1 of the Insurance Supervisory Act or section 43 para 1 of the Capital Investment Code, the management of the relevant credit institution, a financial services institution, an insurance company or an investment management company must inform BaFin of an actual or impeding insolvency of such institution or company.

services institutions, the BaFin may, *inter alia*, temporarily prohibit the disposition of assets by the relevant institution and issue a payment moratorium, close the institution for ordinary business with customers and, unless a deposit or customer protection scheme applies, prohibit the institution from accepting payments except those made in respect of obligations owed to the institution (section 46 para 1 sent. 2 of the Banking Act). Similar orders may be issued by the BaFin in respect of insurance companies pursuant to section 314 of the Insurance Supervisory Act. Such measures are not considered to be Insolvency Proceedings themselves. With respect to capital investment companies BaFin may institute measures under sections 41 and 42 of the Capital Investment Code.

Insolvency Proceedings may not be opened over the assets of the Federal Republic of Germany or a German Federal State (section 12 para 1 no. 1 of the Insolvency Code).

Legal entities established under public law (including German municipalities) which are subject to the supervision of a German Federal State may be exempt from Insolvency Proceedings in Germany by the law of such German Federal State (section 12 para 1 no. 2 of the Insolvency Code).

Where a legal entity established under public law is exempt from Insolvency Proceedings, German insolvency law generally should not interfere with netting as specified by the General Agreement if such legal entity becomes insolvent. Therefore, the insolvency law related limitations on the enforceability of the Netting Provisions as referred to in this Opinion (please refer in particular to Paragraph 5.1.1(i)(ii) below) should not apply to such entities. However, special rules may apply under public law to the winding-up of such entities and such special rules may have an impact on netting. Where a legal entity established under public law is not exempt from Insolvency Proceedings, it is generally treated as any other Party to the General Agreement.

A municipality may also act through an enterprise which is legally not a separate legal entity (*Eigenbetrieb*). In this case, only the municipality (which is exempt from Insolvency Proceedings) becomes a Party to the General Agreement.

Legal entities incorporated under private law which are publicly owned are not exempt from Insolvency Proceedings and are treated as any other Party to the General Agreement.[19]

[19] *Ott/Vuia* in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 12 no. 16.

(b) *Discussion on whether the contract types listed in the Annex are governed by different rules and whether these rules would result in a split or segregation of the portfolio of Individual Contracts under a General Agreement into two or more "netting pools" of disparate treatment or would otherwise limit or render wholly or partially unenforceable the early termination and close-out netting rights provided for in the General Agreement.*

If the contractual Netting Provisions of the General Agreement are recognised in Insolvency Proceedings and the General Agreement and all Individual Contracts entered into thereunder are validly terminated prior to the opening of the Insolvency Proceedings (please see Paragraph 5.1.1(d) below and Paragraph 5.1.1(i)(i)), based on a "non insolvency related" Termination Event, the contractual netting agreement would be recognised (subject to sections 94 *et seqq.* of the Insolvency Code, please see Paragraph 5.1.1(o)).

The statutory rules provided for in sections 103 *et seq.* of the Insolvency Code apply to contracts that are terminated upon the occurrence of an "insolvency related" Termination Event at the time of or after the opening of the main Insolvency Proceedings (please see to Paragraph 5.1.1(i)(ii)) and may render an insolvency related termination invalid with respect to those Individual Contracts. Based on a judgment of 15 November 2012 of the German Federal Court of Justice (*Bundesgerichtshof* – "**BGH**")[20] the term "insolvency related" refers to termination provisions under which a contract may be terminated or terminates automatically upon a stoppage of payment (*Zahlungseinstellung*), the filing for Insolvency Proceedings (*Insolvenzantrag*) or the opening of Insolvency Proceedings (*Insolvenzeröffnung*). According to that court decision this even applies to situations created prior to the opening of Insolvency Proceedings from the point in time in which, based on a valid application for the opening of Insolvency Proceedings, such opening of Insolvency Proceedings is to be seriously expected (*mit der Eröffnung eines Insolvenzverfahrens ernsthaft zu rechnen ist*).[21]

To the extent section 103 of the Insolvency Code applies excluding any contractual or statutory termination of Individual Contracts, the portfolio of Individual Contracts under the General Agreement may be subject to disparate treatment. Pursuant to section 103 of the Insolvency Code, transactions (in this case, Individual Contracts) which have not, or not fully, been performed by either of the parties and which have not been effectively terminated prior to the opening of Insolvency Proceedings are subject to the Insolvency Administrator's

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[20] BGH WM 2013, 274.

[21] This was confirmed by BGH WM 2016, 1168.

Selection Right. Consequently, the Insolvency Administrator has the power to disclaim unprofitable transactions and to enforce profitable ones ("**cherry-picking**") (please see Paragraph 5.1.1(i)(ii)).[22]

However, section 104 of the Insolvency Code provides in our view for exceptions to the Insolvency Administrator's "cherry-picking" right if the respective transaction qualifies as a fixed date transaction (*Fixgeschäft*) under section 104 para 1 sent. 1 of the Insolvency Code, or if it falls within the definition of financial transactions (*Finanzleistung*) of section 104 para 1 sent. 2 of the Insolvency Code. For an analysis whether certain Individual Contract types fall within these exceptions, please see Paragraph 5.1.1(i)(ii)(C) below and Annex 3 to this Opinion below.

(c) *Opinion on whether the termination of the General Agreement, the calculation and/or payment of the Termination Amount is voidable, challengeable or in any way capable of being invalidated, deleted, frozen, stayed or otherwise retroactively impacted by a liquidator, receiver, other third party or the court if insolvency procedures are opened.*

The early termination, set-off and payment of the Termination Amount, as provided for in Sections 10 and 11 of the General Agreement could be challenged by an Insolvency Administrator during insolvency challenge periods (*Anfechtungsfristen*) on the basis of prejudicing the Insolvent Party's creditors as set out below (Paragraph 5.1.1(c) and Paragraph 5.1.1(o)(i)(C)). There is no general exemption from the application of the provisions on insolvency challenge rights of the Insolvency Administrator under substantial German insolvency law with respect to netting agreements.

However, even when these preconditions are fulfilled, the possibility of an insolvency challenge (*Anfechtung*) of legal acts under German law may be excluded pursuant to Article 13 of the EU Insolvency Regulation / Article 16 of the Recast EU Insolvency Regulation or section 339 of the Insolvency Code (please refer to Paragraph 5.2.1(d)(i)(D) and Paragraph 5.2.1(d)(ii)(A)). Moreover, pursuant to section 142 para 1 of the Insolvency Code, a payment on the part of the Insolvent Party in return for which the Insolvent Party's property benefited directly (*unmittelbar*) [23] from an equivalent

[22] *Kreft/Huber* in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 103 nos. 196 *et seq*.

[23] According to section 142 para 2 of the Insolvency Code, the reciprocal obligations are performed "directly" (*unmittelbar*) if there is – taking into account the nature of the goods and services exchanged and the relevant business practices in relation to relevant types of contract – only a short delay between the respective performances (*enger zeitlicher Abstand*). This does not necessarily require a simultaneous performance. However, in order to be able to rely on this exemption, the exchange would still ideally take place simultaneously as it could be difficult to prove any particular business practice in this type of

(*gleichwertig*) consideration may only be challenged if such payment was made with the intention to prejudice the creditors as set out in section 133 paras 1 to 3 of the Insolvency Code and the other party is aware that the Insolvent Party was acting dishonestly (*unlauter*).

Under German law, a legal act (*Rechtshandlung*) made prior to the opening of Insolvency Proceedings which prejudices other creditors of the Insolvent Party may be challenged by the Insolvency Administrator under sections 129 *et seq.* of the Insolvency Code. The term "legal act" refers to acts within the scope of contractual agreements, in particular the execution of a declaration of intention, such as a declaration to terminate, but also to other acts having a legal effect,[24] as well as to factual acts in the context of *in rem* transfers and assignments. Thus, the entering into the General Agreement or an Individual Contract under the General Agreement, the exercise of termination rights under the General Agreement and/or payment of the Termination Amount may be challengeable (voidable) subject to the fulfilment of the preconditions as set out below. Further legal acts that are typically subject to the satisfaction of corresponding challenge in insolvency requirement, are for example (without being conclusive) the entering into of the General Agreement and Annexes, the entering into Individual Contracts, the transfer or granting of collateral, any payment or delivery under an Individual Contract, any agreement on a modification or waiver with respect to the General Agreement and/or an Individual Contract, the exercise of any discretion, etc.[25]

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transaction so that there remains a risk that, where the exchange is not simultaneous, this exemption may not apply.

[24] According to a judgment of BGH dated 7 May 2013 (BGH WM 2013, 1132 *et seq.*) a set-off declared by the Solvent Party after the commencement of Insolvency Proceedings against an Insolvent Party's claim arising from a contract that has been terminated by the Solvent Party prior to the commencement of Insolvency Proceedings is invalid in accordance with section 96 para 1 No. 3 in connection with section 130 para 1 sent. 1 no. 2 of the Insolvency Code if the terminating Party had knowledge of the insolvency of the other Party. In the case underlying the decision, the Insolvency Administrator did not challenge the termination of the relevant contract but the creation of a situation giving a right to set off (*Herstellung der Aufrechnungslage*). When declaring the invalidity of the set-off invalid, the BGH explicitly did not consider the entire consequences of the termination but took an isolated view on the creation of a situation giving a right to set off.

However, in contrast to the case on which BGH had to decide (the Insolvent Party's claim resulted from termination of a commercial agency agreement (*Vertragshändlervertrag*) falling within the scope of section 108 para 1 sent. 1 of the Insolvency Code, i.e. regularly to be continued after the commencement of main Insolvency Proceedings), contracts falling within the scope of section 104 para 1 of the Insolvency Code do not continue after the opening of Insolvency Proceedings. Rather, upon commencement of Insolvency Proceedings any payment and delivery claims terminate and are replaced by a claim for damages by virtue of law.

[25] Whether the determination of the Termination Amount could be qualified as a legal act, please see Paragraph 5.1.1(o).

Challenge periods are ascertained separately in respect of each legal act (and not on an "aggregated" transaction basis) and whether a legal act is detrimental to the creditors of the Insolvent Party is also considered separately for each legal act. In particular, further indirect consequences of such legal act which may have even had a positive effect on the Insolvent Party's assets need not be taken into account[26] and do not prevent the Insolvency Administrator from exercising a right to challenge. However, where the legal act consists of the entering into an agreement, the Insolvency Administrator is not permitted to separately challenge specific clauses but may only challenge conclusion of the agreement in its entirety.[27]

However, in case of a legal act that is subject to a condition precedent, which is for example the case if an agreement automatically terminates if certain circumstances occur, the satisfaction of such condition precedent is not regarded as a legal act (section 140 para 3 of the Insolvency Code).[28] Whether or not a specific legal act is voidable therefore depends on the individual circumstances of the respective transaction.[29]

The periods of time set out in Paragraph 5.1.1(c)(i) to Paragraph 5.1.1(c)(iv) begin on the day on which the filing for the commencement of the Insolvency Proceedings is received by the relevant insolvency court (section 139 para 1 of the Insolvency Code), or, where the debtor is a credit institution or a financial services institution and the BaFin has issued an order pursuant to section 46 para 1 sent. 2 no. 4 to 6 of the Banking Act (please see Paragraph 5.1.1(a)), from the time when such order is issued (section 46c of the Banking Act).

(i) Challenge in insolvency pursuant to section 130 para 1 sent. 1 of the Insolvency Code

Pursuant to section 130 para 1 sent. 1 of the Insolvency Code, a legal act is subject to challenge if it gives or makes available to a creditor security or satisfaction (i) where it was effected in the last three months prior to filing for the opening of Insolvency

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26 BGH ZIP 2002, 489, 490; BGH WM 2005, 1712, 1714; *Kayser*, in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 129 nos. 175 *et seq*.

27 *Kayser*, in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 129 nos. 175 *et seq*.

28 The condition may however not refer to an "insolvency event" (*Insolvenzfall*) which we understand will be given upon the formal opening of insolvency proceedings; see *Huhn/Bayer*, ZIP 2013, p. 1965 *et seqq*.; *Kirchhof* in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 140 no. 52c; Bundesarbeitsgericht NZI 2007, p. 58 *et seqq*., p. 61.

29 The following enumeration is not conclusive, as additional circumstances may be relevant for the challenge of a specific legal act. For example, section 138 of the Insolvency Code provides for a definition of "related persons" (*nahestehende Personen*) of the debtor.

Proceedings, if the Insolvent Party was unable to pay its debts when due at the time of the legal act and if the creditor had knowledge of such inability to make payments at such time; or (ii) where it was effected after filing for the opening of Insolvency Proceedings and the creditor had knowledge of the Insolvent Party's inability to make payments or the petition for opening of Insolvency Proceedings at the time of the legal act.

Knowledge of circumstances that compel the conclusion as to the Insolvent Party's pending inability to make payments or of the filing for the opening of Insolvency Proceedings are regarded as equivalent to actual knowledge of the Insolvent Party's inability to make payments or of the petition for opening of Insolvency Proceedings (section 130 para 2 of the Insolvency Code).

However, these provisions are not applicable where the legal act is based on a security agreement which contains an obligation to provide Financial Collateral, to replace Financial Collateral by other Financial Collateral or to provide additional Financial Collateral in order to readjust the relation between the value of the obligation and the value of the collateral as set forth in the security agreement (*Margensicherheit* - margin collateral, section 130 para 1 sent. 2 of the Insolvency Code).[30]

(ii) Challenge in insolvency pursuant to section 131 para 1 of the Insolvency Code

Pursuant to section 131 para 1 of the Insolvency Code, a challenging period of one to three months applies where a legal act gives or makes available to a creditor, security or satisfaction to which it has no right or no right to claim in such manner or at such time. Such legal act is subject to challenge if either (i) the legal act was effected in the last month prior to filing for the opening of Insolvency Proceedings or following such filing or (ii) the legal act was effected during the second or third month prior to filing for the opening of Insolvency Proceedings and the Insolvent Party was unable to make payments at the time of the legal act or (iii) the legal act was effected during the second or third month prior to filing for the

[30] Notwithstanding this exemption, the provision of margin collateral may still be challengeable (voidable) pursuant to section 131 of the Insolvency Code concerning incongruent coverage. However, according to the legislative materials (BT-Drs. 15/1853, p. 16), and although the German legislator did not expressly incorporate this into law, the German legislator recommended to construe section 131 of the Insolvency Code in the light of the exemption made to section 130 of the Insolvency Code and the relevant provisions in the Financial Collateral Directive. It remains to be seen whether German courts will follow this recommendation.

opening of Insolvency Proceedings and the creditor had knowledge at the time of the legal act that it was detrimental to the Insolvent Party. In relation to (iii), knowledge of circumstances that compel the conclusion that a legal act is detrimental to the Insolvent Party is equivalent to actual knowledge of such detriment (section 131 para 2 of the Insolvency Code).

(iii) Challenge in insolvency pursuant to section 132 para 1 of the Insolvency Code

A legal act by the Insolvent Party that is directly detrimental to the creditors is subject to challenge (i) if it was effected in the last three months prior to filing for the opening of Insolvency Proceedings, if the Insolvent Party was unable to pay its debts when due at the time of the legal act and if the other party had knowledge of such inability to make payments at such time; or (ii) where it was effected after filing for the opening of Insolvency Proceedings and the other party had knowledge of the inability of the Insolvent Party to make payments or of the petition for opening of Insolvency Proceedings at the time of the legal act (section 132 para 1 of the Insolvency Code).

A legal act which involves the Insolvent Party losing a right, or pursuant to which the Insolvent Party is no longer able to assert such a right, or which results in a property claim against the Insolvent Party being maintained or becoming enforceable is equivalent to a legal act that is directly detrimental to the creditors (section 132 para 2 of the Insolvency Code).

(iv) Challenge in insolvency pursuant to section 133 of the Insolvency Code

Pursuant to section 133 para 1 sent. 1 of the Insolvency Code, a legal act made by the Insolvent Party during the last ten years prior to the request to open Insolvency Proceedings, or subsequent to such request, with the intention to disadvantage its creditors may be challenged if the other party was aware of the debtor's intention on the date of such legal act. If such legal act was made to satisfy or secure an existing obligation, the challenge period is shortened to four years pursuant to section 133 para 2 of the Insolvency Code. Awareness of the other party is presumed if such party knew (1) of the imminent inability of the Insolvent Party to make payments when due (*drohende Zahlungsunfähigkeit*) or, where the other party is entitled to receive the satisfaction or security in such way or at such time, of the (actual) inability of the Insolvent Party to pay its debt (*eingetretene Zahlungsunfähigkeit*) and (2) that the legal act constituted a disadvantage for the creditors (section 133 para 1 sent. 2, para 2 sent. 1 of the Insolvency Code). Awareness of corresponding circumstances provides severe evidence for knowledge of the other party of the imminent inability of the Insolvent Party to make payments when due.[31] Further, pursuant to section 133 para 3 sent. 2 of the Insolvency Code, the other party is deemed not to have had knowledge of the inability to pay, if it has agreed upon special payment terms with, or has granted any other form of payment relief to, the Insolvent Party.

Under section 133 para 4 InsO, a contract for consideration entered into by the Insolvent Party and a person with whom the Insolvent Party has a close relationship which is directly detrimental to the creditors is subject to challenge in insolvency action, unless it was entered into more than two years prior to the filing for the opening of Insolvency Proceedings or the other party was unaware of an intention of the Insolvent Party to prejudice the creditors. In respect of persons with whom the Insolvent Party has a close relationship, the requisite knowledge or awareness of the relevant circumstances under the different challenge in insolvency provisions is presumed (sections 130 para 3, 131 para 2 sent. 2 and 132 para 2 of the Insolvency Code).[32]

(d) *Opinion on whether or not there is a distinction in time with respect to a creditor's rights between: (i) the filing of proceedings seeking a judgment of insolvency; (ii) a bankruptcy court recognising the filing of proceedings seeking a judgment of insolvency; (iii) the date on which a bankruptcy court determines a party first becomes insolvent; and (iv) any other stage of the proceedings where a creditor's rights may be affected.*

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[31] A former view of the BGH which resulted in a reversal of the burden of proof regarding the absence of knowledge has been abandoned (BGH NZI 2013, 133, 135; BGH NZI 2009, 768, 769).

[32] If the insolvent party is a legal person, the term "person with whom the insolvency debtor has a close relationship" means, pursuant to an English convenience translation of section 138 para 2 of the Insolvency Code:

"1. the members of the management or supervisory board and personally liable shareholders of the insolvent party as well as person which hold more than one quarter of the insolvent party's share capital;

2. a natural or legal person which due to a comparable connection with the insolvent party established under the articles of association, partnership agreement or under a service contract is able to obtain information on the insolvent party's economic situation;

3. a person as described under nos. 1 and 2 which has a personal relationship as set out under paragraph 1 (i.e. in particular near relatives and persons which under contractual arrangements are able obtain information on the insolvent party's economic status) unless the person described under nos. 1 and 2 is under a statutory obligation to maintain confidentiality in matters of the insolvent party."

In a crisis including any scenarios which may result in the opening of Insolvency Proceedings, creditor's rights may be affected by pre-insolvency proceedings, regulatory proceedings, reorganisation proceedings and recovery and resolution proceedings. We will first cover these proceedings before answering your questions.

(A) Pre-insolvency proceedings

Under German law, the term "commencement" of any proceedings under any insolvency law is likely to be construed to refer to the opening of Insolvency Proceedings, i.e. the time of the issue of an order of commencement of Insolvency Proceedings (*Eröffnungsbeschluss*) by the competent insolvency court.

Upon the filing of an application for the commencement of Insolvency Proceedings and prior to that order of commencement of Insolvency Proceedings, a German insolvency court is entitled to appoint a preliminary administrator (*vorläufiger Insolvenzverwalter*) or initiate pre-insolvency proceedings (**"Pre-Insolvency Proceedings"**) with the following effects:

The court may, *inter alia*, prohibit the Insolvent Party from transferring assets in the course of Pre-Insolvency Proceedings pursuant to sections 21 *et seq.* of the Insolvency Code. However, such measures do not affect the validity of dispositions over Financial Collateral. In the Pre-Insolvency Proceedings, the insolvency court's competences are restricted to attachments (freezing injunctions) that prevent the Insolvent Party from disposing of its assets and thus jeopardising the purpose of formal Insolvency Proceedings. Such a freezing injunction might refer to the current assets of the Insolvent Party or parts thereof. Within the scope of Pre-Insolvency Proceedings, the insolvency court may impose a general prohibition of dispositions (*Verfügungen*) on the debtor (section 21 para 2 sent. 1 no. 2 of the Insolvency Code), order that the debtor's dispositions of property require the consent of the preliminary administrator (section 21 para 2 sent. 1 no. 2 of the Insolvency Code) or order a restriction (or temporary restriction) in certain measures of enforcement (*Zwangsvollstreckungsmaßnahmen*) against the Insolvent Party (section 21 para 2 sent. 1 no. 3 of the Insolvency Code). The preliminary administrator is however not entitled to exercise a "cherry-picking" right according to section 103 of the Insolvency Code (see Paragraph 5.1.1(i)(ii) for further details on the Insolvency Administrator's Selection Right). The scope of application of section 103 of the Insolvency Code is in terms of timing restricted to the opening of Insolvency Proceedings.[33]

According to the BGH,[34] section 119 of the Insolvency Code protects the Insolvency Administrator's Selection Right (please refer to Paragraph 5.1.1(i)(ii) below) under section 103 of the Insolvency Code following the opening of Insolvency Proceedings and, in the view of the BGH also applies prior to the opening of Insolvency Proceedings from the point in time at which, based on a valid application for the opening of Insolvency Proceedings, such opening of Insolvency Proceedings is to be seriously expected *(mit der Eröffnung eines Insolvenzverfahrens ernsthaft zu rechnen ist*). This means that a termination of an agreement may be invalid if it is based on an insolvency related termination right even if the termination occurred prior to the opening of Insolvency Proceedings.

According to a decision of the BGH[35] of 2004, preliminary measures pursuant to section 21 para 2 sent. 1 nos. 2 and 3 of the Insolvency Code do not exclude the permissibility of set-off since the provisions concerning insolvency set-off pursuant to sections 94 through 96 of the Insolvency Code (see Paragraph 5.1.1(o)(i) below) are deemed to be both comprehensive and exclusive.[36] Pursuant to the BGH, even though, from a genuinely economic perspective, a set-off could be deemed as a payment by the Insolvent Party, a general prohibition of transfers does not include the prohibition of set-off of claims against the Insolvent Party (although it may be subject to challenge in insolvency (*anfechtbar*)). In particular, a general prohibition of transfers is only targeted at the Insolvent Party and, hence, cannot effectively prevent the other party from effecting a set-off in the course of Pre-Insolvency Proceedings[37] such as under the Netting Provisions.

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[33] BGH WM 2007, 2331; BGHZ 97, 87, 90; 130, 38, 42; OLG Düsseldorf ZInsO 2005, 820, 821; *Gottwald/Huber*, Insolvenzrechts-Handbuch, 5th ed. (2015), § 35 no. 2; *Wegener* in: Uhlenbruck, Insolvenzordnung, 14th ed. (2015), § 103 no. 99; *Tintelnot* in: Kübler/Prütting/Bork, InsO, 70th update (2017), § 103 no. 210; *Marotzke* in: Heidelberger Kommentar zur Insolvenzordnung, 8th ed. (2016) § 103 no. 116.

[34] BGH WM 2013, 274; BGH WM 2016, 1168.

[35] BGH NJW 2004, 3118, 3119; BGH ZIP 2005, 181.

[36] See also *Lüke* in: Kübler/Prütting/Bork, InsO, 70th update (2017), § 94 nos. 96 *et seqq.*; *Gerhardt*, Festschrift für Zeuner, p. 353, 366; *Häsemeyer*, Kölner Schrift zur Insolvenzordnung, 2nd ed. (1999), p. 663 no. 50; *Brandes/Lohmann* in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 94 no. 5.

[37] BGH ZInsO 2004, 852.

Likewise, a restriction on measures of execution against the Insolvent Party is not aimed at the other Party who can unilaterally declare set-off without the involvement of a court and/or the enforcement of a court decision. Notwithstanding the fact that a set-off achieves an economically similar effect to a measure of execution, it is therefore supported by legal literature that a restriction pursuant to section 21 para 2 sent. 1 no. 3 of the Insolvency Code does not directly prohibit any set-offs.[38]

Preliminary measures do not affect the validity of dispositions over Financial Collateral and the validity of the netting of obligations based on transfer orders that have been entered into a system pursuant to section 1 para 16 of the Banking Act ("**System**") (see Paragraph 5.1.1(o)(i)(G)).[39]

(B) Regulatory proceedings

With regard to credit institutions, financial services institutions, insurance companies and capital investment management companies, Insolvency Proceedings may only be instituted by BaFin.

Regulatory proceedings may be instituted and measures may be taken by BaFin or any other relevant competent authority, including the European Central Bank ("**ECB**") when acting in its capacity as supervisory authority for CRR Credit Institutions, or by the competent resolution authority ("**Resolution Authority**"). Such measures include regulatory measures under sections 45 to 46g of the Banking Act with respect to credit institutions and financial services institutions licensed under the Banking Act, reorganisation measures with respect to credit institutions under the Bank Reorganisation Act (*Gesetz zur Reorganisation von Kreditinstituten*, "**Bank Reorganisation Act**") or resolution measures under the German Recovery and Resolution Act (*Sanierungs- und Abwicklungsgesetz*, "**Resolution Act**") with respect to CRR Credit Institutions and Resolution Investment Firms[40] or group

38 *Haarmeyer* in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 21 no. 72; *Lüke* in Kübler/Prütting/Bork, InsO, 70th update (2017), § 94 no. 102 with the argument that section 96 no. 3 of the Insolvency Code is an adequate protection against unjustified set-off which does not leave room for any analogies as regards section 21 para 2 sent. 1 nos. 2 and 3 of the Insolvency Code.

39 *Lindemann* in: Boos/Fischer/Schulte-Mattler, KWG, 5th ed. (2016), § 46 nos. 118 *et seq.*

40 "**Resolution Investment Firms**" are CRR Investment Firms which need to have a minimum initial capital of EUR 730,000 as provided in section 33 para 1 sentence 1 no. 1 of the Banking Act.

companies[41] (CRR Credit Institutions and Resolution Investment Firms which may be subject to under the Resolution Act collectively, "**Resolution Firms**") under the Resolution Act, in order to avoid the insolvency of any such institution or company.[42]

In respect of insurance companies BaFin may institute measures pursuant to section 314 of the Insurance Supervisory Act. With respect to capital investment companies, section 42 of the Capital Investment Code enables BaFin to issue "appropriate and necessary" measures, in particular, if the investment management company fails to fulfil its obligations with respect to its creditors.[43]

If the Resolution Authority has already instituted a resolution order (*Abwicklungsanordnung*) under sections 136, 77 of the Resolution Act ("**Resolution Order**"), then measures under section 46 and section 46g of the Banking Act may only be instituted upon approval by the Resolution Authority (section 82 para 5 of the Resolution Act).

For purposes hereof, the procedures described in this Paragraph 5.1.1(d)(B) are collectively referred to as "**Regulatory Proceedings**".

Federal Moratorium

In respect of credit institutions, the German Federal Government (*Bundesregierung*) may, *inter alia*, if it determines that a credit institution is in economic difficulties which give rise to the assumption that the national economy, in particular payment transactions in general, are severely jeopardised, under section 46g of the Banking Act grant the credit institution a payment moratorium by the legal instrument of a regulation (*Rechtsverordnung*) and order that enforcement proceedings or Pre-Insolvency Proceedings against such credit institution or Insolvency Proceedings over its assets may not be

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41 By way of further background, group company means a parent undertaking or a subsidiary of a group (of companies), section 2 para 3 no. 30 of the Resolution and Recovery Act. In our view it is not entirely clear which affiliates of CRR Credit Institutions and Resolution Investment Firms can become subject to resolution action. The powers of the Resolution Authority generally relate to CRR Credit Institutions and Resolution Investment Firms as well as their group companies. However, section 64 of the Resolution and Recovery Act specifies the conditions for resolution only for certain subsidiaries (other than CRR Credit Institutions and Resolution Investment Firms), but does not refer to all group companies (see footnote 58~~57~~ below).

42 We do not opine on any proceedings etc. applicable on the basis of a consolidated supervision or on the consequences of a supervision as financial conglomerate or similar provisions.

43 *Kloyer* in: Moritz/Klebeck/Jesch, KAGB, 2016, § 42 no. 11 *et seqq*.

opened for as long as the moratorium continues. It may also order that credit institutions must be closed for business with customers and may neither make nor accept payments or remittances with customers; such order may be restricted to a limited number of credit institutions or types of banking activities.

Regulatory measures by the relevant competent authority

The relevant competent authority may take various regulatory measures in respect of credit institutions and financial services institutions ("**Institutions**"):

Under section 45 of the Banking Act the relevant competent authority may take measures for the reinforcement of an Institution's own funds and liquidity. In particular, the relevant competent authority is empowered to prohibit withdrawals by shareholders and the distribution of dividends, restrict or prohibit the granting of loans, order the Institution to take measures to reduce risks to the extent these risks result from certain types of transactions or products or the use of certain systems or order that the Institution implement measures laid down in its recovery plan (*Sanierungsplan*).

Under section 45c of the Banking Act, the relevant competent authority may appoint a special representative (*Sonderbeauftragter*), to assume certain functions within an Institution (including management functions) and would confer the requisite powers on such special representative.

Where the fulfilment of an Institution's obligations towards its creditors and, in particular, the security of the assets entrusted to it are jeopardised or if effective supervision is no longer possible, the relevant competent authority may take temporary measures under section 46 para 1 of the Banking Act, in particular:

(1) issue instructions for the management of the Institution's business;

(2) prohibit the acceptance of deposits or funds or securities from customers and the granting of loans;

(3) prohibit owners and managers from carrying out their activities or limit such activities;

(4) temporarily prohibit the disposition of assets or the making of any payments by such Institution (such prohibitions, which are different from those under a federal moratorium referred to in the preceding paragraph, are collectively referred to as a "**Moratorium**");

(5) close the Institution for ordinary business with customers and

(6) unless an applicable deposit or customer protection scheme ensures full satisfaction of the customers, prohibit the Institution from accepting payments except those made in respect of obligations owed to the Institution.

The relevant competent authority is also entitled to take crisis prevention measures (*Krisenpräventionsmaßnahmen*) as summarised in section 2 para 3 no. 37 of the Resolution Act, such as the exercise of powers to direct the removal of deficiencies or impediments for the recoverability (section 16 of the Resolution Act) or the reduction or the removal of impediments to the resolvability (sections 59, 60 of the Resolution Act), the application of an early intervention measure under sections 36 to 38 of the Resolution Act or the exercise of the power to write down or convert capital instruments (section 89 of the Resolution Act).

Legal effect of a Moratorium imposed in respect of an Institution

It has been suggested in a court decision that the imposition of a Moratorium has the effect of a payment deferral (*Stundung*), i.e. extension of the due date.[44] Accordingly, set-off of obligations would not be permissible in circumstances where a Moratorium is imposed in respect of assets of and payments by an Institution (as set off may not be effected where the claim against which it is to be effected is not due).

In its decision of 12 March 2013, the BGH has repealed the above-mentioned decision and confirmed that a Moratorium against an Institution under section 46 para 1 sent. 2 no. 4 of the Banking Act would not result in a payment deferral.[45] Rather, the Moratorium creates a temporary obstacle to specific performance and, if imposed on an Institution, would entitle such Institution to refuse specific performance vis-à-vis its counterparty for as long as the Moratorium continues to exist (based on an analogous application of section 275 para 1 of the German Civil Code).[46]

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44 See OLG Frankfurt, ZinsO 2013, 388 et seq. The judgment has been given in respect of the former section 46a para 1 sentence 1 no 1 of the Banking Act but the wording of section 46 para 1 sentence 2 no. 4 of the revised Banking Act is identical. This view has also been shared by the German legislator (BT-Drs. 7/4631, p. 8 and BT-Drs. 14/8017, p. 141).

45 BGH WM 2013, 742, 748.

46 In dismissing that a Moratorium results in a payment deferral, the BGH argues that, as an administrative act (*Verwaltungsakt*) directed against the relevant Institution, the Moratorium would have to be made known to the Institution to become effective against it (section 43 para 1 sentence 1 of the German Act on Administrative Proceedings (*Verwaltungsverfahrensgesetz*), but would not become effective *vis-à-vis* its creditors as a notification (*Bekanntgabe*) *vis-à-vis* the creditors is not provided for under applicable laws

While the BGH has left this question open, it has made obiter remarks indicating that a Moratorium does not prevent set-off. The BGH points out that the purpose of section 46 para 1 sent. 2 no. 4 of the Banking Act to secure the assets of the Institution concerned and prevent its insolvency would not prevent set-off. Even pre-insolvency measures by an insolvency court and the opening of Insolvency Proceedings would generally not prevent set-off and section 46 para 1 sent. 2 no. 4 of the Banking Act is not intended to impose restrictions beyond the restrictions Insolvency Proceedings entail.[47] While these remarks are, in our view, convincing, the BGH does, however, not address the question whether a temporary obstacle for the performance of a claim would still prevent set-off against such claim given that German statutory law allows for set-off only if the claim against which set-off is to be effected can be performed.

(C) Reorganisation Proceedings

Under the Bank Reorganisation Act the relevant credit institution may initiate restructuring proceedings (*Sanierungsverfahren*) or reorganisation proceedings (*Reorganisationsverfahren*)).

The measures under the Bank Reorganisation Act do not qualify as Insolvency Proceedings.

(D) Recovery and Resolution Proceedings

Additional regulatory proceedings may be instituted and measures may be taken by the Resolution Authority with respect to CRR Credit Institutions and Resolution Investment Firms or group companies under the Resolution Act in order to avoid the insolvency of any such institution or company.

In Germany, the Federal Agency for Financial Market Stabilisation (*Finanzmarktstabilisierungsanstalt,* "**FMSA**") is the competent national Resolution Authority (section 3 para 1 of the Resolution Act).

Since 1 January 2016, the Single Resolution Board ("**Board**") acting within the Single Resolution Mechanism ("**SRM**") has assumed certain resolution tasks and may take certain resolution actions or require the FMSA as the competent national resolution authority to implement a resolution scheme

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(BGH WM 2013, 742, 747). Moreover, the counterparty's set-off right which is a protected property right under the German Constitution (*Grundgesetz*) can, according to the BGH, not be restricted without a clearly defined legal basis; see BGH WM 2013, 742, 744.

47 BGH WM 2013, 742, 747.

designed by the Board although the details on the cooperation between the authorities are not entirely clear. Article 1 of 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 ("**SRMR**")[48] states that the uniform rules and the uniform procedure for the resolution of the entities referred to in Article 2 of the SRMR and established in the participating member states (such as Germany) are to be applied by the Board. Article 2 of the SRMR refers to CRR Credit Institutions established in a participating Member State, parent undertakings, including financial holding companies and mixed financial holding companies, established in a participating Member State, if they are subject to consolidated supervision carried out by the ECB in accordance with Article 4 para 1 lit (g) of Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions ("**SSMR**")[49] and investment firms and financial institutions established in a participating Member State, where they are covered by the consolidated supervision of the parent undertaking carried out by the ECB in accordance with Article 4 para 1 lit (g) of the SSMR.

The Board and the Resolution Authority are under a duty to cooperate and Article 7 para 2 of the SRMR clarifies that the Board shall be responsible for drawing up the resolution plans and adopting all decisions relating to resolution for: (a) the entities referred to in Article 2 of the SRMR that are not part of a group and for groups: (i) which are considered to be significant in accordance with Article 6 para 4 of the SSMR or (ii) in relation to which the ECB has decided in accordance with Article 6 para 5 lit (b) of the SSMR to exercise directly all of the relevant powers; and (b) other cross-border groups.[50] In relation to entities and groups other than those referred to in Article 7 para 2 of the SRMR the Resolution Authority is entitled to perform, and is responsible for, the resolution tasks enumerated in Article 7 para 3 of the SRMR.

48 OJ EU No L 225 of 30 July 2014, p. 1.

49 OJ EU No L 287 of 29 October 2013, p. 63.

50 Please also refer to http://srb.europa.eu/en/node/44.

Article 29 para 1 of the SRMR states that the national resolution authorities shall take the necessary action by taking the necessary measures in accordance with Article 35 or 72 of the BRRD and by ensuring that the safeguards provided for in the BRRD are complied with when implementing decisions under the SRM. Article 29 of the SRMR also clarifies that the national resolution authorities shall exercise their powers under national law transposing the BRRD and in accordance with the conditions laid down in national law. This means that to the extent the FMSA is the competent national resolution authority the FMSA would exercise its powers under the Resolution Act. Under Article 29 para 2 of the SRMR, where a national resolution authority has not applied or has not complied with a decision by the Board pursuant to the SRMR or has applied it in a way which poses a threat to any of the resolution objectives under Article 14 of the SRMR or to the efficient implementation of the resolution scheme, the Board may order an institution under resolution (a) in the event of an action pursuant to Article 18 of the SRMR, to transfer to another person specified rights, assets or liabilities of an institution under resolution, (b) in the event of an action pursuant to Article 18 of the SRMR, to require the conversion of any debt instruments which contain a contractual term for conversion in the circumstances provided for in Article 21 of the SRMR or (c) to adopt any other necessary action to comply with the decision in question.

Notwithstanding the provisions of Article 29 of the SRMR (and other relevant references throughout SRMR) the interaction between the SRMR and the Resolution Act is in our view not entirely clear. Therefore, to the extent a relevant entity is covered by the SRMR and subject to a resolution decision by the Board affected entities and their creditors might need to not only review the consequences under the Resolution Act following implementation of such decisions but also the requirements under the SRMR for making such decisions and to assess the potential application of powers under the SRMR (in particular, as the relevant provisions under the SRMR, the BRRD and the Resolution Act are not identical and they also may be subject to review by different courts). We are not aware of any court decision or any further guidance by the Board or the FMSA on this topic. Section 1 of the Resolution Act provides that as far as the SRMR is not applicable the Resolution Act applies. In the following, when referring to the Resolution Authority, we describe the powers of the FMSA under the Resolution Act but, as mentioned, the Board may require the FMSA to take resolution action based on the SRMR and the Board or the FMSA may under certain circumstances be entitled to exercise similar powers under the SRMR. In particular, the SRMR contains bail-in powers and powers to transfer assets and liabilities (Articles 24 *et seqq.* of the SRMR). In our view it cannot be excluded that powers under the Resolution Act and the SRMR differ.

Following this introduction in respect of Pre-Insolvency Proceedings and Regulatory Proceedings we will now answer your question set out in Paragraph 5.1.1(d) as to how creditor's rights may be affected depending on the nature of proceedings the relevant debtor is subject to:

(i) *The filing of proceedings seeking a judgment of insolvency;*

The time of filing of a petition for the opening of Insolvency Proceedings, or, if the debtor is a credit institution or a financial services institution and the BaFin has issued an order pursuant to section 46 para 1 of the Banking Act (please see Paragraph 5.1.1(d)(B), the time when such order is issued (section 46c of the Banking Act) is decisive for the calculation of insolvency challenge periods (section 139 para 1 sent. 1 of the Insolvency Code) (please see Paragraph 5.1.1(c) above).

(ii) *A bankruptcy court recognising the filing of proceedings seeking a judgment of insolvency*;

The recognition of the filing of proceedings seeking a judgment of insolvency does not qualify as a technical term under the Insolvency Code referring to a specific procedural step of Insolvency Proceedings. Section 26 of the Insolvency Code provides that the bankruptcy court rejects such filing in case the assets of the insolvent debtor are insufficient to compensate for the costs of the Insolvency Proceedings (*Abweisung mangels Masse*). However, such rejection has no impact on statutory netting or the enforceability of the contractual Netting Provisions.

(iii) *The date on which a bankruptcy court determines a party first becomes insolvent; and*

Upon the opening of Insolvency Proceedings, an insolvency court does not determine the date when the Insolvent Party has become insolvent. It rather determines that the Insolvent Party is insolvent at the point in time of issuing the order for the opening of the Insolvency Proceedings or, as the case may be, preliminary insolvency proceedings. The date when the Insolvent Party has become insolvent is only relevant to determine whether or not a legal act of an Insolvent Party can be challenged by an Insolvency Administrator (please see Paragraph 5.1.1(c)). In the following, we only refer to the point in time of the opening of the Insolvency Proceedings.

(iv) *Any other stage of the proceedings where a creditor's rights may be affected*

(1) Application for the opening of Insolvency Proceedings

Besides the filing for the opening of Insolvency Proceedings, the point in time in which, based on a valid application for the opening of Insolvency Proceedings, such opening of Insolvency Proceedings is to be seriously expected (*mit der Eröffnung eines Insolvenzverfahrens ernsthaft zu rechnen ist*) is relevant. According to the BGH,[51] this point in time is decisive for whether the Netting Provisions apply or whether such provisions are overridden by the statutory provisions of the Insolvency Code if termination is based on an insolvency related Termination Event (please see Paragraph 5.1.1(i)(ii) below).

(2) Actual opening of Insolvency Proceedings

In addition, the actual opening of the main Insolvency Proceedings is of relevance. Pursuant to section 81 of the Insolvency Code, any dispositions (*Verfügung*) of the Insolvent Party over its property made after the opening of Insolvency Proceedings are void unless the relevant court orders otherwise. However, dispositions over Financial Collateral affected after the actual opening of Insolvency Proceedings are valid, provided that such dispositions were effected on the day of the opening of Insolvency Proceedings and the other party proves that it did not know, nor should have known of the opening of the Insolvency Proceedings.

After the opening of Insolvency Proceedings rights in assets forming part of the insolvency estate cannot be acquired with legal effect even if such acquisition of rights is not based on a disposition by the insolvent party or effected by enforcement measures (section 91 para 1 of the Insolvency Code).

(3) Termination rights under the General Agreement following the opening of Reorganisation Proceedings

Termination rights under the General Agreement may be affected by restructuring measures under the Bank Reorganisation Act and the Banking Act applicable to credit

[51] BGH WM 2013, 274; BGH WM 2016, 1168.

institutions within the meaning of section 1 para 1 of the Banking Act which have their seat in Germany.

The Bank Reorganisation Act provides for restructuring proceedings involving the appointment of a restructuring advisor (*Sanierungsberater*) to implement a restructuring plan. Restructuring proceedings are initiated by the credit institution on a voluntary basis in close consultation with the BaFin and commenced by a court order of the OLG Frankfurt upon application. Restructuring proceedings may not affect creditors' rights.[52]

If restructuring proceedings have failed or are without prospect of success, reorganisation proceedings may be opened (section 7 of the Bank Reorganisation Act). Reorganisation proceedings are initiated by the credit institution itself, or, if restructuring proceedings have failed, by the restructuring advisor with the credit institution's consent, by notifying BaFin. The credit institution or the restructuring advisor must submit a reorganisation plan when notifying BaFin. Following the notification, reorganisation proceedings may be opened by the Higher Regional Court (*Oberlandesgericht*, "**OLG**") Frankfurt upon an application by BaFin if the conditions for a Resolution Order are met (as to which see Paragraph 5.1.1(d)(iv)(4) below). Reorganisation proceedings may involve measures that affect the rights of the credit institution's creditors and/or its shareholders.

Pursuant to section 12 of the Bank Reorganisation Act the reorganisation plan if approved by the OLG Frankfurt may provide that claims of creditors are partially reduced, deferred or modified in another way. The modification of claims that are protected by a statutory or voluntary deposit protection scheme is for example excluded. This right to reduce, defer or modify claims may also be extended to creditors' rights with respect to collateral provided as security interest if under such security interest the relevant creditors are entitled to separate satisfaction (*absonderungsberechtigt*) such as pledges over securities by applying section 223 of the Insolvency Code by analogy to the reorganisation proceeding. Section 9 of the Bank Reorganisation Act provides that claims of a creditor may be

52 Section 2 para 2 of the Bank Reorganisation Act provides that the restructuring plan may provide that certain loans granted in the context of the restructuring within the approved aggregate limit not exceeding 10 per cent. of the own capital of the relevant institution may rank superior to claims of all other insolvency creditors in case that insolvency proceedings are commenced within a period of three years following the commencement of the restructuring proceeding.

converted into equity ("debt-equity-swap"), however, this would be subject to the affected creditors' consent.

The measures proposed in the reorganisation plan are subject to a positive majority vote of the creditors and shareholders of the respective credit institution accepting such measures and final approval by the OLG Frankfurt. If the votes approve the reorganisation plan, the reorganisation is subject to the approval by the OLG Frankfurt, upon which it becomes effective (section 21 of the Banking Reorganisation Act).

Furthermore, the Bank Reorganisation Act provides for certain mandatory temporary limitations of the rights of counterparties to terminate contractual relationships with a credit institution that becomes subject to reorganisation proceedings (section 13 of the Bank Reorganisation Act). Contracts may not be terminated from the day on which the notification pursuant to section 7 para 1 of the Bank Reorganisation Act is filed with BaFin until the end of the following business day.[53] The effect of any termination events (for example in case of a payment default) occurring during this period is suspended until the expiration of that period. Contractual clauses that provide for the contrary (i.e. for an immediate termination) are invalid.[54]

Where the notification for the commencement of reorganisation proceedings is made less than two business days prior to termination upon the application of BaFin for the opening of Insolvency Proceedings, this suspensive effect would also hold true for (automatic) termination based on such event of default.

(4) Termination Rights under the General Agreement following the Resolution Order

The Resolution Act contains wide reaching powers for the Resolution Authority with respect to Resolution Firms and group companies under resolution that may affect their creditors, and result, *inter alia*, in a suspension of early termination rights and the conversion or write-down of liabilities.

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53 Section 13 of the Bank Reorganisation Act refers to the business day of a System as defined in section 1 para 16b of the Banking Act which comprises the usual business cycle of the System including day and night settlement.

54 Please refer to Paragraph 5.1.1(d)(E) with respect to the effects of such provision on agreements not governed by German law.

If the conditions for resolution are met, the Resolution Authority can take any action in accordance with the Resolution Act to achieve the resolution objectives. This includes the right to issue Resolution Orders under sections 77 para 1 no. 1, 136 of the Resolution Act and, together with or independent from a Resolution Order any other actions under sections 78 to 87 of the Resolution Act.[55] A Resolution Order may involve the application of the following resolution tools: write down or conversion of relevant capital instruments (section 89 of the Resolution Act), the bail-in tool (section 90 of the Resolution Act), the sale of business tool (section 107 para 1 no. 1 lit (a) of the Resolution Act), the bridge institution tool (section 107 para 1 no. 1 lit (b) of the Resolution Act) and the asset separation tool (section 107 para 1 no. 2 of the Resolution Act).[56]

The Resolution Authority may also, *inter alia*, order the modification (including any suspension) of the due date of any debt instruments issued or other eligible liabilities (*berücksichtigungsfähige Verbindlichkeiten*) incurred by a Resolution Firm and any group companies or of the amount of any interest payable or the date when such interest is payable (section 78 para 1 no. 3 of the Resolution Act).

Conditions for resolution

The conditions for the resolution (*Abwicklungsvoraussetzungen*) of Resolution Firms and Resolution Investment Firms are met if the ongoing existence of such entity is jeopardised (*Bestandsgefährdung*), the implementation of a resolution action (*Abwicklungsmaßnahme*) to achieve one or more resolution objectives (*Abwicklungsziele*) is necessary and proportionate (*erforderlich und verhältnismäßig*), and the situation cannot be remedied through measures other than resolution action with the same certainty regarding the time available (section 62 para 1 sent. 1 of the Resolution Act).[57] The ongoing existence of Resolution Firms is jeopardised if (1) the Resolution Firm infringes or there are objective elements to support the view that the Resolution Firm will, in the near

55 As regards the resolution objectives please refer to section 67 of the Resolution Act, as regards the general principles on resolution please refer to section 68 of the Resolution Act and as regards to the various valuation procedures please refer to sections 69 to 76 of the Resolution Act.

56 While we use the original terms of the English version of the BRRD this does not imply that the BRRD has been implemented on a one-by-one basis into German law.

57 Section 62 para 1 sentence 2 of the Resolution Act does not require that any crisis prevention measures or any other appropriate measures under the Banking Act are instituted before a resolution action.

future, infringe the requirements for holding a licence under section 32 of the Banking Act in a way that would justify the withdrawal of the licence by the competent authority, (2) the assets of the Resolution Firm are or there are objective elements to support the view that the assets of the Resolution Firm will, in the near future, be, less than its liabilities or (3) the Resolution Firm is, or there are objective elements to support the view that the institution will, in the near future, be, unable to pay its debts or other liabilities as they fall due unless there is a serious chance (*ernsthafte Aussicht*) that following the issuance of a state guarantee (*staatliche Garantie*) (as referred to in the next sentence) the Resolution Firm is in a position to meet its liabilities when they fall due; section 63 para 1 of the Resolution Act. The ongoing existence of a Resolution Firm is deemed to be jeopardised if extraordinary financial support is granted from public sources except when, in order to remedy a serious disturbance of the economy and preserve financial stability, the extraordinary public financial support takes any of the following forms: (1) a state guarantee to back liquidity facilities provided by central banks according to the central banks' conditions; (2) a state guarantee of newly issued liabilities; or (3) an injection of own funds or purchase of capital instruments at prices and on terms that do not confer an advantage upon the institution (for further details and exemptions refer to section 63 para 2 of the Resolution Act).[58]

Bail-in powers

With respect to the individual resolution tools, the bail-in tool (*Instrument der Gläubigerbeteiligung*) (section 90 of the Resolution Act) empowers the Resolution Authority to either convert eligible liabilities (*berücksichtigungsfähige Verbind-*

[58] Section 64 of the Resolution Act provides that the conditions for the resolution of a financial institution as defined in Article 4 para 1 no. 26 of the CRR (i.e. a subordinated undertaking of a parent undertaking subject to prudential supervision at a consolidated level) are met if the conditions for the resolution of the parent undertaking pursuant to section 62 of the Resolution Act are satisfied. In respect of financial holding companies (as defined in Article 4 para 1 no. 20 of the CRR) mixed financial holding companies (as defined in Article 4 para 1 no. 21 of the CRR), parent financial holding companies in a member state (as defined in Article 4 para 1 no. 30 of the CRR), EU parent financial holding companies (as defined in Article 4 para 1 no. 31 of the CRR), parent mixed financial holding companies in a member state (as defined in Article 4 para 1 no. 32 of the CRR) and EU parent mixed financial holding companies in a member state (as defined in Article 4 para 1 no. 34 of the CRR), the conditions are met if the conditions for resolution are met (a) both in respect of one such entity and in respect of at least one of its subordinated undertakings which qualifies as an Resolution Firm (or if a non-EU resolution has determined that a third country subordinated undertaking can be resolved in accordance with the laws of such non-EU country) or (b) if (1) the conditions for resolution are met in respect of at least one of its subordinated undertakings which qualify as Resolution Firms, (2) the jeopardy to the existence of the subordinated undertaking could result in the entire group's existence being jeopardised and (3) resolution action in respect of the holding company is necessary to resolve at least one of the subordinated undertakings or the group.

lichkeiten) of a Resolution Firm into shares or other Common Equity Tier 1 (for purposes of Article 28 of the CRR) items or partially or fully write down or cancel eligible liabilities. Liabilities are eligible for bail-in unless relevant liabilities are covered by one of the exemptions in section 91 of the Resolution Act or the Resolution Authority, exercising due discretion and having regard to the criteria in section 92 of the Resolution Act, decides to exempt liabilities from the application of section 90 of the Resolution Act in certain specified cases.

With respect to derivatives in general (as defined in section 2 para 3 no. 11 of the Resolution Act by reference to the definition of financial instruments under section 1 para 11 sent. 3 of the Banking Act) the bail-in tool may only be applied after or simultaneously with the "closing-out" (*Glattstellung*) of such derivatives (section 93 para 1 of the Resolution Act). Hence, only the relevant net settlement amount would be subject to bail-in. Pursuant to section 93 para 2 of the Resolution Act the Resolution Authority is empowered to terminate and close out derivatives transactions. If derivatives transactions have been entered into under an agreement qualifying as netting arrangement (*Saldierungsvereinbarung*) the Resolution Authority or an independent valuation expert is obliged to determine the net amount of the derivatives transactions and to simultaneously or subsequently apply the bail-in tool to the net claim (section 93 para 3 of the Resolution Act).

Pursuant to section 2 para 3 no. 43 of the Resolution Act, "netting arrangement" means an arrangement under which a number of claims or obligations can be converted into a single net claim, including (1) arrangements under which, upon the occurrence of an enforcement event the obligations of the parties are accelerated so as to become immediately due or are terminated, and in either case are converted into or replaced by a single net claim (close-out netting agreement), (2) set-offs based on a termination (close-out netting) as defined in Article 2 para 1 lit (n) of the FCD and (3) netting (*Aufrechnung*) as defined in Article 2 lit (k) of the Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on Settlement Finality in Payment and Securities Settlement Systems[59] as amended by Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives

[59] OJ No L 166 of 11 June 1998, p. 45.

98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 ("**Settlement Finality Directive**" or "**SFD**").[60]

We note that there is currently no guidance on the meaning of the definitions in section 2 para 3 no. 43 of the Resolution Act and any restrictions the Resolution Authority might apply in construing these terms. It is not entirely clear whether a competent court or a relevant competent authority would construe the term "netting arrangement" pursuant to section 2 para 3 no. 43 of the Resolution Act in the same way the BGH understands the term "netting agreement" (see Paragraph 5.1.1(i)(ii)(H) below)[61].

The Netting Provisions provide for the termination of mutual obligations between the Parties upon the occurrence of a Material Reason (Section 10.3 of the General Agreement) and the calculation of a single Termination Amount to replace the mutual obligations (Section 11.1 of the General Agreement). Therefore, the Netting Provisions qualify in our view as a netting arrangement as defined in the Resolution Act. Consequently, the Resolution Authority would be prevented from applying write-off or conversion powers to individual claims under such derivatives transactions covered by the Netting Provisions, but it would be entitled to close out the outstanding transactions, to calculate a net claim and to write off or convert such net claim pursuant to section 93 para 3 of the Resolution Act.[62] Please note the requirements under the Commission Delegated Regulation (EU) 2016/1401 of 23 May 2016 supplementing Directive 2014/59/EU of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms with regard to regulatory technical standards for

[60] In the English language version, both Article 2 para 1 lit (n) of the FCD and Article 2 lit (k) of the SFD refer to "close-out netting" or "netting" while the German language version refers to set-off (*Aufrechnung*).

[61] The SFD has most recently been amended by Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 ("**CSDR**"). In the English language version, both Article 2 para 1 lit (n) of the FCD and Article 2 lit (k) of the SFD refer to "close-out netting" or "netting" while the German language version refers to set-off (*Aufrechnung*).

[62] Separately, derivatives transactions may also be protected from bail-in under general exemptions such as the exemption for secured liabilities which is discussed in the next Paragraph; see also the European Banking Authority's ("**EBA**") Consultation paper "Draft Regulatory Technical Standards - On the valuation of derivatives pursuant to Article 49(4) of the Bank Recovery and Resolution Directive (BRRD)" dated 13 May 2015 as available at https://www.eba.europa.eu/documents/10180/1073039/EBA-CP-201-10+CP+on+RTS+on+derivatives+valuation.pdf on 21 October 2015.

methodologies and principles on the valuation of liabilities arising from derivatives.[63]

Pursuant to section 93 para 5 of the Resolution Act in conjunction with section 104 para 3 of the Insolvency Code, section 93 para 1 to para 4 of the Resolution Act apply *mutatis mutandis* to transactions pursuant to section 104 para 1 of the Insolvency Code, which are combined in a master agreement pursuant to section 104 para 3 of the Insolvency Code (in this respect see Paragraph 5.1.1(i)(ii)(H) below).

Secured liabilities within the meaning of section 91 para 2 no. 2 of the Resolution Act would not be subject to bail-in to the extent the secured liability is secured or covered by value of the secured collateral asset. In our view, the fact that in context of derivatives, generally margin is provided does not mean that derivatives in general qualify as secured liabilities. As we understand and construe section 91 para 2 no. 2 of the Resolution Act such exemption would only be available for derivatives if the relevant net settlement amount resulting from the application of close-out netting were to be secured separately. This is also in line with the fact that under section 93 of the Resolution Act only the net settlement amount would be subject to bail-in. The exemption under section 91 para 2 no. 2 of the Resolution Act does not apply to collateral which is enforced by way of close-out netting. We are not aware of any court decisions on this question.

We note that Article 27 of the SRMR does not provide for an exemption similar to section 93 of the Resolution Act (or Article 49 of the BRRD). It is therefore not entirely clear whether the Board when exercising any discretion under Article 27 para 1 of the SRMR will recognise any netting or whether section 93 of the Resolution Act can still be applied by the FMSA when implementing the Board's decision under Arcticle 29 of the SRMR.

Powers to transfer assets and liabilities

Shares or all or any assets including the liabilities of a Resolution Firm or group company in resolution may be transferred to a third party under the sale of business tool (section 107 para 1 no. 1 lit (a) of the Resolution Act) or to a bridge institution[64] under the bridge institution tool (section 107

[63] OJ EU No L 228 of 23 May 2016, p. 7

[64] "Bridge institution" (*Brückeninstitut*) means a legal entity which (1) is entirely held by the Resolution Authority or another public authority, (2) is controlled by the Resolution Authority on the basis of corporate

para 1 no. 1 lit (b) of the Resolution Act) if the Resolution Authority determines that the conditions for resolution of the Resolution Firm or group company are met.

Under the asset separation tool (section 107 para 1 no. 2 of the Resolution Act) all or any assets including the liabilities of a Resolution Firm or group company in resolution may be transferred to an asset management company. Secured assets and liabilities may not be separated from the relevant collateral assets serving as security as such assets or liabilities may only be transferred if they are transferred together with any relevant collateral assets and all collateral assets may only be transferred together with the relevant assets or liabilities which are secured by such collateral assets; section 110 para 1 of the Resolution Act. This prohibition of partial transfers is extended by section 110 para 3 of the Resolution Act to collateral assets securing liabilities included in a System, to netting arrangements (*Saldierungsvereinbarungen*) and set-off agreements (*Aufrechnungsvereinbarungen*). As mentioned, based on the definition of netting arrangements in the Resolution Act, the Netting Provision should in our view qualify as a netting arrangement.

There is no definition of "set-off agreements" in the Resolution Act. However, under Article 2 para 1 no 99 BRRD "set-off arrangement" means an arrangement under which two or more claims or obligations owed between the institution under resolution and a counterparty can be set off against each other. Based on this broad wording, the term "set-off agreement" seems to cover any agreement by which parties set off their liabilities. Thus, section 110 para 3 of the Resolution Act should have a broad scope of application. The Netting Provision would appear to contain sufficient elements of set-off to qualify as a set-off agreement.[65]

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law, contract law or public law powers to exercise influence and (3) has been established as a bridge institution for purposes of section 107 of the Resolution Act (section 128 of the Resolution Act).

65 However, EBA has concluded that rules preventing a separation of rights and liabilities should be applied in a restrictive manner (see technical advice by the European Banking Authority on classes of arrangements to be protected in a partial property transfer of 14 August 2015 (http://www.eba.europa.eu/documents/10180/983359/EBA-Op-2015-15+Opinion+on+protected+arrangements.pdf): "In any event, the protection should be limited to liabilities clearly identified in the set-off arrangement (at least by category). In addition, the delegated acts should specify precise criteria when such arrangements and liabilities qualify for this protection. Ideally the scope of the safeguard should be limited to certain qualifying arrangements and certain liabilities." Conversely, the EBA also notes that "qualifying arrangements could for example include only financial contracts as defined in point (100) of Article 2 (1), and the protection apply only to them (this term would need to include options, futures, swaps, forward rate agreements and any other derivative contracts)."

The Netting Provision should therefore qualify as a netting arrangement and should also qualify as a set-off agreement and accordingly, a partial transfer of transactions subject to it would not be permissible.

As long as the conditions for resolution are fulfilled, the asset transfer tools can be used multiple times and each transfer is valid (and the transfer of title is actually effected) upon the publication of the relevant Resolution Order (sections 114, 136 of the Resolution Act). Separately, section 79 para 2 of the Resolution Act empowers the Resolution Authority to modify or cancel (*ändern oder beseitigen*) the rights of third parties in respect of the Resolution Firm's assets.

Section 79 para 5 of the Resolution Act further empowers the Resolution Authority, in respect of a contract to which the Resolution Firm is a party, (i) to amend some or all provisions, (ii) to refuse performance or (iii) to replace the Resolution Firm with a transferee entity as the counterparty. The power pursuant to section 79 para 5 of the Resolution Act must not be exercised (i) in respect of Financial Collateral as well as netting and set-off agreements, (ii) so as to result in a cancellation of transfer orders for purposes of Article 5 of the SFD and or (iii) so as to affect the validity of transfer orders or set-offs in accordance with Articles 3 and 5 of the SFD, credit entries, securities or credit facilities for purposes of Article 4 of the SFD or rights *in rem* for purposes of Article 9 of the SFD (section 79 paras 6 and 7 of the Resolution Act).

Since the official heading of section 79 of the Resolution Act refers only to the use of transfer tools, these powers should only be available where the Resolution Authority makes use of a transfer tool although we also note that Article 64 para 1 lit (f) of the BRRD provides that national resolution authorities generally (not limited to situations where transfer powers are used) have the "ancillary power" to cancel or modify the terms of a contract to which the institution under resolution is a party or substitute a recipient as a party.

See Article 3 para 2 of the Commission Delegated Regulation (EU) 2017/867 of 7 February 2017 on classes of arrangements to be protected in a partial property transfer under Article 76 of the BRRD (OJ No 131 of 20 May 2017, p. 15) for further limitations on which set-off arrangements are protected and covered by Article 76 para 2 lit (c) of the BRRD.

Powers to temporarily suspend the enforcement of rights, claims and security interests and exemptions

The Resolution Authority is entitled under section 82 para 1 of the Resolution Act to suspend any payment or delivery obligations under any contract to which a Resolution Firm or group company under resolution is a party from the publication of a notice of the suspension in accordance with section 137 of the Resolution Act until the end of the business day following such publication. Such suspension may also affect payment and delivery obligations arising under an Individual Contract.

A payment or delivery obligation which would have been due during the suspension period becomes due immediately upon expiry of the suspension period. If the payment or delivery obligations of an institution under resolution under a contract are suspended, the payment or delivery obligations of such institution under resolution's counterparties under that contract are suspended for the same period of time.

The Resolution Authority has the power to temporarily prevent secured creditors of a Resolution Firm or group company under resolution from enforcing security interests in relation to any assets of that Resolution Firm or group company under resolution from the publication of a notice of the restriction in accordance with section 137 until the end of the business day following that publication (section 83 para 1 of the Resolution Act).

As mentioned, there is no definition of "secured liabilities" in the Resolution Act. However, Article 2 para 1 no 67 of the BRRD provides that secured liabilities include title transfer collateral arrangements and the term "secured liabilities" should in our view be construed accordingly for the purposes of the Resolution Act. Conversely, the Resolution Act as well as the BRRD address netting arrangements and security arrangements separately. Therefore, a competent authority or court would in our view likely not consider a netting arrangement as a form of security for purposes of the Resolution Act.

Under section 84 para 1 of the Resolution Act, the Resolution Authority is entitled to suspend the termination rights[66] of any party to a contract with a Resolution Firm or group company

66 Section 84 para 7 of the Resolution Act states that section 84 of the Resolution Act applies to all termination events arising under a contract with an institution or group company in resolution which, in our view, should also include automatic termination rights.

under resolution from the publication of such suspension pursuant to section 137 para 1 of the Resolution Act until the end of the business day following that publication. The Resolution Authority may also suspend the termination rights of any party to a contract with a group company forming part of the group of an institution under resolution from the publication of such suspension pursuant to section 137 para 1 of the Resolution Act until the end of the business day following that publication where (1) the obligations under that contract are guaranteed or are otherwise supported by the group company under resolution, (2) the termination rights under that contract are based solely on the insolvency or the conditions for resolution or the institution or implementation of resolution actions and (3) in the case of a transfer power that has been or may be exercised in relation to the institution or group company under resolution, (i) all rights and liabilities of the Resolution Firm or group company under resolution of the subsidiary relating to that contract have been or may be transferred to and assumed by the recipient or (ii) the Resolution Authority provides in any other way adequate protection for the rights of the other parties (section 84 para 2 of the Resolution Act).

A party may exercise a termination right under a contract before the end of the period referred to in paragraphs 1 or 2 of section 84 of the Resolution Act if that party receives notice from the Resolution Authority under section 84 para 5 of the Resolution Act that the rights and liabilities covered by the contract are (i) not to be transferred to another entity, (ii) not subject to write down and (iii) not subject to conversion upon the application of the bail-in tool. Subject to sections 82 and 144 of the Resolution Act, where no notice has been given pursuant to section 84 para 5 of the Resolution Act, a counterparty may exercise termination rights after the expiry of the period of suspension if, (1) in cases where the rights and liabilities covered by the contract have been transferred to a recipient entity, the contractual requirements for terminating the contract are still met after the transfer to the recipient entity (2) in cases where the rights and liabilities covered by the contract remain with the Resolution Firm or group company under resolution and the Resolution Authority has not applied the bail-in tool, the contractual requirements for terminating the contract are still met on the expiry of the suspension.

Exemptions from these restrictions apply for participants in Systems, System operators within the meaning of section 1 para

16 lit (a) of the Banking Act, central counterparties within the meaning of section 31 of the Banking Act and central banks.

Statutory safeguards

Pursuant to section 144 para 1 of the Resolution Act, a crisis prevention measure or a crisis management measure (*Krisenmanagementmaßnahme*), including the occurrence of any event directly linked to the application of such a measure, shall not in relation to the Resolution Firm or the group and all group companies be deemed to be an enforcement or termination event within the meaning of the FCD or as insolvency proceedings within the meaning of the SFD provided that the main obligations (*Hauptleistungspflichten*) under the contract, including payment and delivery obligations and the provision of collateral, continue to be performed.[67]

Under section 144 para 3 of the Resolution Act, a crisis prevention measure or crisis management measure, including the occurrence of any event directly linked to the application of such a measure, do not make it possible to (1) exercise any termination, suspension, modification, netting (*Verrechnung*) or set-off rights *vis-à-vis* a Resolution Firm or group company, (2) acquire title over any property of the Resolution Firm or group company, exercise control over it or enforce any rights under a security and (3) affect any contractual rights of the Resolution Firm or group company. This does only apply if the main obligations under the contract, including payment and delivery obligations, and provision of collateral, continue to be performed. A suspension or restriction under sections 82 to 84 of the Resolution Act is not regarded as non-performance of contractual main obligations.

Section 144 of the Resolution Act does not affect the right of a person to take an action referred to in section 144 para 3 of the Resolution Act where that right arises by virtue of an event other than the crisis prevention measure, the crisis management measure or the occurrence of any event directly linked to the application of such a measure. Section 144 para 5 of the Resolution Act provides that agreements violating sections 144 para 1 to 3 of the Resolution Act are not enforceable.[68]

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67 To the extent a resolution procedure of a third country state can be recognised under section 169 of the Resolution Act such procedure is deemed a crisis management measure for the purpose of section 144 of the Resolution Act.

68 Resolution Firms and group companies may only use standard agreements if they comply with the requirements, section 144 para 5 sent 2 of the Resolution Act.

"No creditors worse off" principle

Under section 146 of the Resolution Act the Resolution Authority must ensure that immediately after the resolution action or actions have been effected a valuation is carried out by an independent person (such valuation must be distinct from the valuation carried out under section 69 of the Resolution Act) to assess if and to what extent shareholders and creditors would have received better treatment if the institution under resolution had entered into normal insolvency proceedings. If such assessment shows that creditors are worse off than they would have been in insolvency proceedings, such creditors are entitled to seek compensation from the German bank restructuring fund (*Restrukturierungsfonds*) (section 147 of the Resolution Act).

This means that counterparties should at least receive compensation if the imposition of resolution measures results in a situation where they would be more detrimentally affected than in Insolvency Proceedings. In this respect, it should be assessed whether relevant transactions fall within the scope of section 104 of the Insolvency Code and, accordingly, would not be subject to a Selection Right by the Insolvency Administrator or if transactions qualify as mutual transactions which have not been completely fulfilled by one party and, therefore, are not protected by section 104 of the Insolvency Code (see Paragraphs 5.1.1(i)(ii)).

Legal remedies

A resolution action may be challenged before the Higher Administrative Court (*Verwaltungsgerichtshof*, "**VGH**") Kassel within one month upon their publication (section 150 of the Resolution Act). The law does not expressly foresee any appeal against any such judgment, although legal remedies may from time to time be available under generally applicable laws, including German constitutional law. The filing of a law suit does not suspend or otherwise affect the validity of the relevant resolution action.

Summary

To summarise, upon the imposition of crisis prevention measures or crisis management measures in respect of Resolution Firms and group companies under resolution contractual termination, set-off or netting rights as well as the enforcement of security may be temporarily suspended, excluded or otherwise restricted or affected, subject to applicable exemptions. Contractual rights and obligations may be subject to mandatory conversion or write off and may be transferred to another party and/or modified. If the relevant Resolution Firm and group companies under resolution subsequently becomes insolvent, this may (in particular in conjunction with the temporary suspension of enforcement, set-off or netting rights under the Resolution Act) result in a situation where the counterparty would continuously be prevented from exercising any termination, set-off or netting rights, first under the Resolution Act and subsequently under the Insolvency Code. However, this would only apply as a matter of German law and it is unclear whether the provisions of the Resolution Act would be given effect before any courts outside Germany, in particular before courts outside the EU.

For derivatives transactions, the bail-in tool may only be applied after or simultaneously with the "closing-out" of such derivatives.

(E) International scope of application of regulatory measures under the Banking Act, the Bank Reorganisation Act and the Resolution Act

In accordance with section 46d para 3 sent. 3 of the Banking Act, section 340 para 2 of the Insolvency Code, which provides for specific conflicts of law rules for "netting agreements" (*Schuldumwandlungsverträge und Aufrechnungsvereinbarungen*) (see Paragraph 5.2.1(d)(ii)(B) below) applies by analogy to reorganisation measures (*Sanierungsmaßnahmen*). Among such reorganisation measures are, in particular, measures taken under section 46 of the Banking Act which are intended to preserve or restore the financial status of a CRR Credit Institution and which may affect existing rights of third parties in a host member state of the EEA (section 46d para 3 sent. 1 of the Banking Act). The view of the German legislator appears to be that such "reorganisation measures" qualify as "reorganisation measures" as defined in Article 2 no. 7 of the Winding Up Directive because section 46d para 1 sent. 1 of the Banking Act requires BaFin to inform the competent authorities of host EEA member states when taking "reorganisation measures" under the Banking Act. However, the scope of section 46d para 3 of the Banking Act is not entirely clear as the term "reorganisation measure" is not used elsewhere in the Banking Act.[69]

[69] BT-Drs. 17/3024, p. 49. We note that Article 117 of the BRRD extended the scope of the Winding-Up Directive to also include CRR Investment Firms (previously only CRR Credit Institutions). However,

The same issue arises under section 7 para 5 sent. 2 of the Bank Reorganisation Act which provides that section 46d paras 1 to 4 of the Banking Act apply to reorganisation proceedings under the Bank Reorganisation Act. Whether restructuring proceedings (*Sanierungsverfahren*) or reorganisation proceedings (*Reorganisationsverfahren*) under the Bank Reorganisation Act are covered by the reference is in our view also not entirely clear, although, given the purpose of the Bank Reorganisation Act to stabilise credit institutions and to allow them to operate as going concerns, there is good reason to conclude that at least the measures under the Bank Reorganisation Act qualify as reorganisation measures for purposes of the Winding Up Directive and section 46d para 3 sent. 3 of the Banking Act. In such case, sections 338 and 340 of the Insolvency Code would be applicable and if a court were to follow our interpretation of sections 338 and 340 para 2 of the Insolvency Code, the effects of the regulatory measures and reorganisation proceedings on Individual Contracts would therefore have to be decided on the basis of English law if English law is governing the relevant General Agreement. However, absent any authoritative precedents from courts and at least a detailed analysis in legal literature, it is unclear whether a German court would also apply Article 9 of Regulation (EC) No 593/2008 of 17 June 2008 on the law applicable to contractual obligations (Rome I) ("**Rome I Regulation**") and, if so, in which way the court would resolve the conflict between section 340 of the Insolvency Code on the one hand and the direct application of overriding mandatory provisions of German law under Article 9 of the Rome I Regulation on the other hand.

There is no similar conflict of laws provision in the Resolution Act. Under German law, the termination restrictions under section 144 of the Resolution Act, which implements Article 68 of the BRRD, are considered to qualify as overriding mandatory provisions within the meaning of Article 9 para 1 of the Rome I Regulation. Thus, a German court would generally have to recognise the termination restrictions, irrespective of the law governing the transactions (Article 9 para 2 of the Rome I

section 46d of the Banking Act, which implemented Articles 3 to 6 and Article 8 of the Winding-Up Directive has not been amended. Accordingly the wording of section 46d of the Banking Act still only refers to CRR Credit Institutions. In contrast, section 46e of the Banking Act which implemented Articles 9, 13, 17 and 19 of the Winding-Up Directive has been amended to also include CRR Investment Firms (now simply referring to CRR Institutions). It is therefore not entirely clear whether the reference to CRR Credit Institutions in section 46d of the Banking Act is a mistake of the legislator and therefore section 46d of the Banking Act should be construed in accordance with section 46e of the Banking Act such that it should also include CRR Investment Firms.

Regulation). However, to the extent bound by the Rome I Regulation, a court outside Germany would have to consider applying such termination restrictions only if the obligations arising out of the transactions had to be or have been performed in Germany (Article 9 para 3 of the Rome I Regulation). In such case, effect may be given to the overriding mandatory provisions of German law, in so far as those overriding mandatory provisions render the performance of the contract unlawful. The fact that the termination restrictions under section 144 of the Resolution Act are from a German law perspective overriding mandatory provisions within the meaning of Article 9 para 1 of the Rome I Regulation, would not require a court outside Germany to apply the termination restrictions if obligations arising out of the transactions were not to be performed in Germany.

We are not aware of any guidance from BaFin, the ECB or the Resolution Authority or court decisions on the Bank Reorganisation Act, the Resolution Act and the aforementioned provisions of the Banking Act.

(e) *Opinion on whether the German insolvency law provides for a "safe harbour" for certain derivatives or other categories of transactions and whether the contract types listed in Annex would benefit from such provision(s).*

We understand that the term "safe harbour" refers to a provision pursuant to which the opening of Insolvency Proceedings would not affect the enforceability of claims under the relevant transaction. Such provisions do not exist under German law. However, section 104 of the Insolvency Code provides for an exception to the Insolvency Administrator's Selection Right (please see Paragraph 5.1.1(i)(ii) on) based on sections 103 and 119 of the Insolvency Code that would also render a contractually agreed insolvency related early termination invalid. For an overview of the contract types that could benefit from such exception, see Paragraph 5.1.1(i)(ii)(D) and in more detail in Annex 3.

German substantive insolvency law does not provide for an exception from the statutory provisions of challenging in insolvency (see Paragraph 5.1.1(c) above).

(f) *Opinion on whether there is publicly available information that would confirm any of the procedural steps mentioned above under (a) through (d) or other solvency related facts (e.g., financial statements, corporate actions, etc.).*

Pursuant to section 9 para 2 sent. 2 of the Insolvency Code in connection with section 2 of the Regulation on Public Announcements in Insolvency Proceedings via Internet (*Verordnung zu öffentlichen Bekanntmachungen in Insolvenzverfahren im Internet*), several procedural steps, including the court order on the opening of Insolvency Proceedings (*Eröffnungsbeschluss*) or the decision by a court not to open Insolvency Proceedings due to insufficient funds (*mangels Masse*) have to be published on the internet by the insolvency court. The relevant website is www.insolvenzbekanntmachungen.de. This website is updated several times a day. Thus, depending on the time when the opening of the Insolvency Proceedings is ordered, the announcement may be made on the same day or the day after the announcement. Additional publications may be made in print media.[70]

The filing for insolvency may also be made public by the relevant company itself. There is no general obligation on behalf of the insolvent party to publish the fact that it has submitted an insolvency filing. However, if a company qualifying as an issuer (as defined in Article 3 para 1 no. 21 of Regulation (EU) No. 596/2014 of April 2014 on market abuse ("**MAR**"))[71] who has requested or approved admission of its financial instruments to trading on a regulated market in a member state[72], is subject to the *ad hoc* requirements provided for in Article 17 of the MAR.

The *ad hoc* requirement applies to all information which, *inter alia*, is not known to the public and may, if it becomes public, have a significant effect on the price of the relevant financial instrument. Thus, the filing for the opening of Insolvency Proceedings and the insolvency court's order on the commencement of Insolvency Proceedings is likely subject to the *ad hoc* publication requirement. An *ad hoc* publication has to be made without undue delay (*unverzüglich*).[73]

Similarly, a market participant is obliged under Article 4 para 1 of the Regulation (EU) No 1227/2011 of the European Parliament and of the

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70 The information as published under www.insolvenzbekanntmachungen.de must also be published in the company register (*Unternehmensregister*) according to section 8b para 2 no. 11 of the German Commercial Code and is accessible via the electronic Federal Gazette (*elektronischer Bundesanzeiger*) under www.unternehmensregister.de.

71 OJ No C 173 of 12 Jne 2014, p. 1.

72 In the case of instruments only traded on a multilateral trading facility ("**MTF**") or on an organised trading facility ("**OTF**"), issuers who have approved trading of their financial instruments on an MTF or an OTF or have requested admission to trading of their financial instruments on an MTF in a member state.

73 Please refer to BaFin's FAQs on Article 17 of the MAR, p. 4 (https://www.bafin.de/SharedDocs/Downloads/DE/FAQ/dl_faq_mar_art_17_Ad-hoc.html)

Council of 25 October 2011 on wholesale energy market integrity and transparency ("**REMIT**") to publicly disclose in an effective and timely manner inside information which they possess in respect of business or facilities which the market participant concerned, or its parent undertaking or related undertaking, owns or controls or for whose operational matters that market participant or undertaking is responsible, either in whole or in part. REMIT applies to trading in wholesale energy products (Article 1 para 2 sent. 1 of the REMIT).

In case of an insolvency filing by the BaFin with respect to a credit institution, a financial services institution or an insurance company, the filing for insolvency is likely to be published on the BaFin's website (www.bafin.de).

In case of Insolvency Proceedings over the assets of a CRR Credit Institution or CRR Investment Firm, the announcement of Insolvency Proceedings is also published in the OJ of the EU and two nationwide newspapers (section 46e para 3 sent. 2 of the Banking Act). In case of Insolvency Proceedings over the assets of a German insurance company, the announcement of the Insolvency Proceedings is also published in the OJ (section 312 para 4 sent. 3 of the Insurance Supervisory Act).

(g) *A general description of limitations in German law, if any, applicable to set off of claims (both in an Early Termination scenario and otherwise):*

- *between Parties of claims arising* ***under*** *the General Agreement;*
- *between Parties of claims arising* ***outside*** *the General Agreement if contractually provided for in an amendment to the General Agreement; and*
- *between Affiliates or Credit Support Providers of Parties if contractually provided for in an amendment to the General Agreement.*

(i) General requirements for set-off

Under German statutory law, set-off (*Aufrechnung*) is understood as the mutual discharge of two corresponding obligations of the same nature. The rules relating to set off are contained in sections 387 *et seq.* of the German Civil Code. According to this provision, a party that demands payment – or of whom payment is demanded – is entitled to unilaterally declare that the debt is extinguished by a set-off provided that the legally defined set-off requirements are met. Set-off requires that (i) both parties have claims against each other (mutuality - *Gegenseitigkeit*), (ii) such claims are of similar nature (similarity - *Gleichartigkeit*), (iii) the claim against which set-off is to be effected is valid, due and enforceable (*Wirksamkeit, Fälligkeit und Durchsetzbarkeit der Gegenforderung*) and (iv) the other claim (against which set-off is to be effected) can be fulfilled (*Erfüllbarkeit der Hauptforderung*). Pursuant to section 388 para 1 of the German Civil Code, a set-off right is exercised by giving notice of set-off to the other party (*Aufrechnungserklärung*). The right to set off may only be exercised if set-off is neither excluded by law[74] nor by agreement.[75]

Pursuant to the principles of contractual freedom and party autonomy, contractual set-off agreements (*Aufrechnungsvertrag* or *Aufrechnungsvereinbarung*) are permissible. To the extent that the arrangements do not conflict with mandatory provisions of German law, the parties are allowed to deviate from the statutory requirements for set-off (such as the requirement that the claim with which set-off is to be effected is due and payable) by agreement. Such an agreement can modify the requirements for set-off or extend the right to set off (for example, by enabling the party to set off against a claim of a third party). Pursuant to section 94 of the Insolvency Code and subject to the challenging of transactions in Insolvency Proceedings, such a contractual agreement concerning set-off is generally enforceable, even in case of the insolvency of either or both parties. However, there is a view supporting a narrow interpretation of section 94 of the Insolvency Code to restrict the scope of permissible agreements concerning set-off in case of insolvency with a view to ensure an appropriate equal treatment of all creditors.[76]

(ii) Limitations on contractual set-off arrangements

Limitations on contractual set-off arrangements apply to agreements which deviate from the requirement of mutuality of the claims. Pursuant to the BGH section 96 para 1 no. 2 of the

[74] Set-off is generally subject to restrictions in specific circumstances pursuant to sections 392 *et seq*. of the German Civil Code, for example, if an obligation arises from a claim for compensation for an intentional tort (section 393 of the German Civil Code) or if one of the claims is not capable of being subject to attachment (section 394 of the German Civil Code). We do not opine on German corporate law where, in specific cases, statutory restrictions on set-off may apply (sections 19 of the Act on Limited Liability Companies and section 66 of the Stock Corporation Act, which restrict the right of a shareholder to set off against its obligation to provide equity contributions).

[75] For an overview see *Schlüter* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 387 nos. 56 *et seq*.

[76] *Schwahn,* NJW 2005, 473, 474.

Insolvency Code applies to agreements which provide for the right to set off claims of an affiliated company by another company against the claims of a third party (*Konzernverrechnungsklausel*).[77] The BGH took the view that after the opening of Insolvency Proceedings, a set-off with claims not owned by the offsetting party but by its affiliate is ineffective. This applies even if such "tri-party" set-off had been agreed upon by the three parties involved before the opening of Insolvency Proceedings as in the specific case the set-off declaration had been made only after the opening of Insolvency Proceedings and, accordingly, the preconditions of section 94 of the Insolvency Code had not been met.[78]

Typically, the mutuality that is required for set-off in liquidation does not exist in cross affiliate set-off and, as such, cross affiliate netting may not work in insolvency. Statutory provisions may also limit or prohibit set-off with respect to certain entities, including, for example, insurance companies and investment management companies:[79]

(A) Insurance companies

With respect to insurance companies, section 130 para 2 sent. 2 of the Insurance Supervisory Act limits the possibility of set-off against claims belonging to the "cover assets" (*Sicherungsvermögen*) of an insurance company.

(B) Investment management companies

Pursuant to section 93 para 5 sent. 1 of the Capital Investment Code, claims against the investment management company and claims which belong to the assets of a fund may not be set off against each other. This prohibition is framed broadly and should therefore apply to any set-off or netting agreements.

Pursuant to section 93 para 5 sent. 2 of the Capital Investment Code the prohibition of set-off does not apply[80] to master

77 BGH NJW 2004, 3185.

78 With respect to "tri-party" set-off, the BGH argued in its judgment that the situation entitling to a set-off (*Aufrechnungslage*) which is protected by section 94 of the Insolvency Code does not come into existence prior to the declaration of set-off.

79 Please also refer to Paragraph 6.1.9 with respect to the limitation of set-off against certain creditors established under public law.

80 Under German statutory law, set-off is restricted in an insolvency scenario if the claims to be set off are not mutual. While when entering into a master agreement, the investment management company is the debtor of contractual claims thereunder (section 93 para 2 of the Capital Investment Code), the claims arising out of the master agreement may either be claims of the investment management company acting as trustee for the

agreements or transactions pursuant to sections 197 para 1 sent. 1, 200, and 203 of the Capital Investment Code or which have been concluded with prime brokers for which it has been agreed that the claims arising from these transactions or master agreements which have been concluded for the account of a fund shall be netted automatically or upon the declaration of a party or that they shall be replaced by a single compensation claim in the event of the termination as a result of non-performance or insolvency.

Generally, German courts have taken the view that violations of regulatory law do not render contractual agreements void.[81] Where provisions of regulatory law serve the protection of the interests of a certain counterparty, such counterparty may, however, be entitled to claim damages in tort in order to be put in the position it would be in, if no violation of regulatory law had occurred.[82]

The restrictions laid down under section 93 para 5 of the Capital Investment Code may be applicable despite the choice of non-German law to govern the General Agreement and any Individual Contract, if a German court qualifies section 93 para 5 of the Capital Investment Code to constitute an overriding mandatory provision within the meaning of Article 9 para 1 of the Rome I Regulation. Since Article 9 para 2 of the Rome I Regulation provides that nothing in the Rome I Regulation restricts the application of the overriding mandatory provisions of German law section 93 para 5 of the Capital Investment

investors which are beneficial owners if the fund is established in the form of a trust structure (*Treuhandstruktur*), in which case mutuality would be questionable, or the claims arising out of the master agreement may be claims in the joint ownership of the investors in the fund if the fund is established in the form of joint ownership of its investors (*Miteigentumsstruktur*), in which case mutuality would not be given.

In our view, however, the explicit exemption from the prohibition of set-off contained in the Capital Investment Code should be construed to prevail over the limitations of set-off arising out of the legal form of a Fund as described above and this should also overcome missing mutuality under civil law aspects (*Anders,* in: Weitnauer/Boxberger/Anders, KAGB, 1st ed. (2014), § 93 no. 15 *et seq*., *Nietsch,* in: Emde/Dornseifer/Dreibusch/Hölscher, Investmentgesetz, 1st ed. (2013), §°31 no. 50 *et seq*.). This is supported by the reasoning to the German Capital Investment Company Act (*Gesetz über Kapitalanlagegesellschaften*, a predecessor of the Capital Investment Code) as the German legislator has explicitly mentioned that the provision shall enable the valid conclusion of close-out netting agreements in BT-Drs. 14/8601, p. 21, when implementing section 9 para 6 sentence 2 of the Capital Investment Company Act in the course of the Fourth Financial Markets Enhancement Act, and in BT-Drs. 1/8933, p. 105, with respect to section 8e of the Capital Investment Company Act. In our view, this reasoning applies accordingly to section 93 para 5 sentence 2 of the Capital Investment Code as the provision has been adopted in the Capital Investment Code without major change and without further reasoning. We are not aware of any court decision in this respect and a court may take a different view.

81 BGH NJW 2011, 3024, 3025; BGH NJW 1980, 1394; BGH WM 1978, 785.

82 BGH NJW 2005, 2703 *et seq*.; BGH NJW-RR 2006, 1713 *et seq.*

Code would be applicable to the General Agreement and any Individual Contract based on an interpretation of 93 para 5 of the Capital Investment Code as an overriding mandatory provision.

(h) *Opinion on whether German laws consider early termination, set-off and close-out netting as legally distinct and separate or similar rights, similar or related rights or whether they make no such distinctions between them.*

Under German law, "netting" technically does not constitute a legal term referring to a specific and clearly defined legal concept. Instead, the term "netting" may denote a variety of legal concepts such as payment or payment netting, netting by novation (*Schuldersetzung*), and close-out netting (*Liquidations-Netting*).[83]

In the context of master agreements for derivative transactions, the legal concept that is most relevant under German law is "close-out netting" which provides for a method of reducing the parties' exposure by terminating outstanding transactions, calculating their values and determining compensation payments for all outstanding transactions that are subsequently netted against each other.

This concept is distinct from the statutory concept of set-off as the corresponding obligations that are normally subject to close-out netting are neither of the same nature nor due at the same time. Rather, the parties contract to deviate from the statutory requirements for set-off, subject to certain restrictions due to mandatory provisions of German law (please see Paragraph 5.1.1(g) above).

(i) *Assuming the Parties have not specified that Automatic Termination applies, are the provisions of the General Agreement permitting the other Party (the "**Terminating Party**") to terminate the General Agreement (including all Individual Contracts) upon the occurrence of a Material Reason described in Section 10.5(c) of the General Agreement enforceable under German laws or is there a risk that (i) the entering into the General Agreement, (ii) the entering into Individual Contracts thereunder or (iii) the early termination by notice itself could be challenged by a liquidator, administrator, receiver or third party?*

[83] For an overview please refer to: European Financial Markets Lawyers Group, Protection for Bilateral Insolvency Set-off and Netting Agreements under EC Law, October 2004, Annex 6, p. 75.

(i) Enforceability of the termination rights under the General Agreement prior to the commencement of Insolvency Proceedings

Prior to the commencement of Insolvency Proceedings, the law applicable for termination under the General Agreement depends on the law governing the General Agreement.

(A) Enforceability of the termination rights if the General Agreement is governed by a law other than German law

From a German law perspective pursuant to Article 12 para 1 of the Rome I Regulation, the law applicable to a contract is generally decisive for its interpretation, the performance of the obligations created by it, within the limits of the powers conferred on the court by its procedural law, the consequences of a total or partial breach of obligations, including the assessment of damages in so far as it is governed by rules of law, the various kinds of extinguishing obligations, and prescription and limitation of actions and the consequences of the nullity of the contract.

Pursuant to Article 12 para 1 (d) of the Rome I Regulation and to the extent the Rome I Regulation applies, the validity of the termination of a transaction, which is not governed by German law, is determined under the law that governs such transaction. To the extent the termination is valid under the law governing the General Agreement, for example, English law, German law recognises the validity of such contractual early termination.

(B) Enforceability of the termination rights if the General Agreement is governed by German law

(1) Termination rights under the single agreement concept

According to the single agreement concept contained in Section 1.1 of the General Agreement, all Individual Contracts entered into under the General Agreement are governed by the terms of the General Agreement, and all Individual Contracts and the General Agreement form a single agreement between the parties and are referred to as the "Agreement".

Assuming the Individual Contracts are governed by German law and provided that the Individual Contracts refer to the General Agreement, such

Individual Contracts are included in the General Agreement irrespective of whether or not the relevant Individual Contract was concluded before or after the execution of the General Agreement, provided that the terms of the Individual Contract prevails over the terms of the General Agreement (Section 2.2 of the General Agreement).

Assuming the Individual Contracts are governed by a law other than German law, under German conflict of law rules, the laws governing the relevant Individual Contracts would also determine the circumstances under which such Individual Contracts may be included into the General Agreement. We do, however, not opine on the inclusion of transactions which are not governed by German law.

Therefore, the right to terminate the General Agreement and all Individual Contracts entered into thereunder for Material Reason would generally be enforceable, subject to our analysis in Paragraph 5.1.1(i)(ii) below.

(2) "Material Reason" in Section 10.5 of the General Agreement and termination for serious cause according to section 314 para 1 of the German Civil Code

If the General Agreement is governed by German law, the General Agreement may generally be terminated upon the occurrence of a serious cause (*wichtiger Grund*). Generally, section 314 para 1 of the German Civil Code provides for the termination of a contract for the performance of a continuing obligation on notice with immediate effect upon a serious cause. Serious cause exists if, after having regard to all circumstances of the specific case and balancing the interests of both parties, the terminating party cannot reasonably be expected to continue the contractual relationship until the agreed termination date or until the end of a notice period. Serious cause might consist in the infringement of a duty under the contract or a material change of circumstances.

Under the principles of contractual freedom and party autonomy, the parties to an agreement may agree on termination rights which specify or supplement the statutory termination rights for serious cause. Parties to an agreement may specify individual events giving rise to a termination right for serious cause by individual agreement (*Individualvereinbarung*).[84]

Therefore, the events specified as a "Material Reason" in Section 10.5 of the General Agreement will be construed as an agreement between the parties that such events qualify as a serious cause for purposes of section 314 para 1 of the German Civil Code.[85]

In case of a provision such as Section 10.5 of the General Agreement, in which the parties agree on a specific set of termination events which give rise to an early termination without any notice period, the terminating party only needs to prove the relevant facts giving rise to such termination event. No proof as to whether such termination event would actually qualify as serious cause needs to be presented by the terminating party since the parties have agreed already that such event qualifies as serious cause. In such case, the other party would explicitly have to establish that despite of the occurrence of such event which both parties explicitly agreed to qualify as serious cause, it is not unreasonable to continue the contractual relationship.[86]

84 BGH NJW-RR 1988, 1331, 1332.

85 Such enumeration would, however, not be capable of being construed as a conclusive enumeration of all events which may qualify as a serious cause under section 314 para 1 of the German Civil Code because this would then imply a contractual limitation of the right to terminate for serious cause and a limitation of the termination right for serious cause by standard terms and conditions would not be binding (BGH ZIP 1986, 919, 920; BGH NJW 2012, 1431). Furthermore, even by individual agreement the parties cannot entirely waive the termination right for serious cause (BGH BB 1973, 819).

86 Generally it depends on the individual circumstances whether an event constitutes a serious cause pursuant to section 314 para 1 of the German Civil Code and has to be determined on a case-by-case basis. Absent any contractual agreement between the parties to a contract, the terminating party would have to prove the existence of the facts that give rise to a serious cause and would also have to demonstrate that in balancing the interests of both parties it cannot reasonably be expected to continue the contractual relationship in case of a dispute over the validity of a termination pursuant to section 314 para 1 of the German Civil Code.

According to German court decisions, termination rights may not be exercised at an inappropriate point in time (*Kündigung zur Unzeit*), *i.e.* the terminating party must consider prior to any termination whether the point in time when the termination right is exercised would impose an additional significant burden on the other party to the contract that could be prevented by taking less severe steps.[87] Whether the point in time when the General Agreement and all Individual Contracts entered into thereunder are terminated may be regarded as inappropriate depends on the specific circumstances of the individual case. The party raising this argument would have to present conclusive evidence that its particular interest to defer the termination and continue the agreement is to be considered more justified than the interest of the terminating party to terminate the General Agreement and all Individual Contracts entered into thereunder *i.e.* that the other party has used its contractual right in an abusive manner (*rechtsmißbräuchlich*).

(ii) Enforceability of contractual Early Termination rights in case of insolvency

Under the Insolvency Code, following the opening of Insolvency Proceedings, mutual contracts[88] which have not or not (yet) fully been performed (*nicht oder nicht vollständig erfüllt*) by either party ("**Executory Contracts**") and which have not been effectively terminated prior to such opening of Insolvency Proceedings are, pursuant to section 103 of the Insolvency Code, subject to the Insolvency Administrator's Selection Right.[89]

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[87] LG Frankenthal ZIP 2006, 752; OLG München BB 1997, 435, 436; OLG Frankfurt WM 1992, 1018; BGH WM 1985, 1136; BGH DB 1959, 594. Whereas most courts have rejected the defence that a termination was exercised at an inappropriate point in time, LG Frankenthal considered the termination of a loan ineffective as the termination right was exercised by the terminating party "out of the blue" (*aus heiterem Himmel*) without considering less severe steps.

[88] Mutual contracts are contracts giving rise to mutual rights and obligations (*gegenseitige Verträge*) within the meaning of sections 320 et. seq. of the German Civil Code, whereby each of the parties only agrees to perform its obligations in exchange for the other party performing its obligation (*Huber* in: Münchener Kommentar InsO, 3rd ed. (2013), § 103 no. 55).

[89] The opening of Insolvency Proceedings does not trigger the (automatic) termination of the contractual obligation to perform. Rather, the opening of Insolvency Proceedings only affects the enforceability of the respective claims since both parties to a contract may raise the objection of non-performance of a contract

An English translation of section 103 of the Insolvency Code reads as follows:

"Section 103

Selection right by the insolvency administrator

(1) If a mutual contract was not or not fully performed by the debtor and the other party at the date when the insolvency proceedings were opened, the insolvency administrator may perform such contract in place of the debtor and claim performance by the other party.

(2) If the insolvency administrator refuses to perform such contract the other party is entitled to assert its claims for non-performance only as an insolvency creditor. If the other party requires the insolvency administrator to decide whether he chooses performance or non-performance, the insolvency administrator shall state his intention to claim performance without undue delay. If the insolvency administrator does not give his statement he may no longer insist on performance."

In the event that the Insolvency Administrator refuses to perform, a contract, such contract is terminated and the Solvent Party may assert claims arising from non-performance only as a creditor in the Insolvency Proceedings. Such claims rank *pari passu* with the claims of all other unsecured creditors.

(A) Protection of the Selection Right

Section 119 of the Insolvency Code provides that agreements excluding or limiting the application of sections 103 to 118 of the Insolvency Code in advance are invalid and therefore protects the Insolvency Administrator's Selection Right. As an early termination restricts the Selection Right an early termination under Section 10 of the General Agreement may be invalid if it violates sections 103, 119 of the Insolvency Code. In the following we will analyse the scope of sections 103, 119 of the Insolvency Code with respect to termination rights under the General Agreement and any potential exceptions.

(BGH ZIP 2002, 1093, 1095; BGH NJW 2005, 2231; BGH NJW 2006, 915; see also *Kreft*, in: Münchener Kommentar InsO, 3rd ed. (2013), § 103 nos. 11 *et seq.*). Therefore, neither the opening of Insolvency Proceedings nor the decision of the Insolvency Administrator results directly in a termination of a contractual agreement.

Based on its wording, section 119 of the Insolvency Code only applies after the opening of Insolvency Proceedings. However, based on the purpose of such section to protect the rights under sections 103 to 118 of the Insolvency Code, the BGH held in its judgement of 15 November 2012 that section 119 of the Insolvency Code applies from the point in time in which, based on a valid application for the opening of Insolvency Proceedings, such opening of Insolvency Proceedings is to be seriously expected (*mit der Eröffnung eines Insolvenzverfahrens ernsthaft zu rechnen ist*). [90] Any contractual early termination right based on insolvency related events is therefore void if the termination is triggered resulting from the occurrence of such event.[91]

According to the BGH, insolvency related termination provisions are provisions under which a contract may be terminated upon a stoppage of payment (*Zahlungseinstellung*), the filing of an application for the opening of Insolvency Proceedings (*Insolvenzantrag*) or the opening of Insolvency Proceedings (*Insolvenzeröffnung*). [92] This means that events specified as "Material Reason" in Section 10.5(c) of the General Agreement would be regarded as insolvency related termination provisions. Whereas, according to the BGH, "non-insolvency related" termination provisions are not intended to "erode" the Selection Right and therefore non-insolvency related termination provisions will generally not be covered by section 119 of the Insolvency Code, the validity of contractually stipulated termination rights that are based on insolvency related events depends on whether or not the respective agreement is deemed as an exclusion or limitation of the application of the Selection Right.[93] However, the BGH also confirmed that the Selection Right cannot be eroded where there is an exemption from the Selection Right (see Paragraph 5.1.1(i)(ii)(B) below).[94]

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[90] BGH WM 2013, 274, 276.

[91] BGH WM 2013, 274, 275 et seq. (relating to a contract for the supply of energy), confirmed by BGH WM 2016, 1168, 1173 also in respect of other contracts; see also *Obermüller*, ZInsO 2013, 476, 480 et seq.

[92] BGH WM 2013, 274.

[93] BGH WM 2013, 274, 275.

[94] BGH WM 2016, 1168, 1173.

(B) Exemption from the Insolvency Administrator's Selection Right

Section 104 of the Insolvency Code provides for an exemption from the Insolvency Administrator's Selection Right for fixed date transactions (*Fixgeschäfte*) and financial transactions (*Finanzleistungen*). To the extent section 104 of the Insolvency Code applies, it overrides the Insolvency Administrator's Selection Right under section 103 of the Insolvency Code.

Fixed date transactions and financial transactions falling within the scope of section 104 para 1 of the Insolvency Code are automatically terminated upon the opening of Insolvency Proceedings and the Parties may no longer demand performance of the relevant obligations but a claim for non-performance is calculated on the basis of the method stipulated in section 104 para 2 of the Insolvency Code. The Solvent Party may assert the claim for non-performance as an insolvency creditor, ranking *pari passu* with any other unsecured creditors (section 104 para 5 of the Insolvency Code). Section 104 of the Insolvency Code is therefore a statutory close-out netting provision. However, within the scope set out therein, section 104 para 4 of the Insolvency Code generally recognises contractual close-out netting (*vertragliches Liquidations-netting*).

The current version of section 104 of the Insolvency Code entered into force on 29 December 2016 and has been changed significantly compared to the previously applicable version. While these changes are, to some extent, intended to adapt the wording to market developments such as product innovation, they also have to be regarded as a response to the BGH decision of 15 November 2012 and, in particular to the BGH decision of 9 June 2016.[95] Understanding the purpose of the changes and the exemptions created thereby for contractual close-out netting arrangements is relevant for assessing to what extent the limits set by the BGH need still to be observed.

On 9 June 2016 the BGH did not explicitly decide whether or not an insolvency related contractual early termination right triggered upon the filing of an application for the opening of Insolvency Proceedings or any other relevant point in time before the opening of Insolvency Proceedings was void *per se*.[96] Rather, the BGH explained in its reasoning that the Selection

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95 BT-Drs. 18/9983, p. 8, 10.

96 With respect to the 2012 decision, please refer to *Obermüller*, ZinsO 2013, 476.

Right cannot be "eroded" by such contractual termination right as there is no Selection Right where section 104 of the Insolvency Code applies.[97] However, in its decision of 9 June 2016, the BGH went beyond this statement by holding that, if parties to a transaction governed by German law entered into a netting agreement (in the reasoning referred to as "*Abrechnungsvereinbarung*") for the event of an insolvency which is contradictory to section 104 of the Insolvency Code, (in the version applicable before 10 June 2016) the netting agreement is void in this respect and the provisions of section 104 of the Insolvency Code are directly applicable. The BGH has explicitly ruled that section 104 of the Insolvency Code prevails over contractual arrangements. On the basis of this ruling, a contractually agreed early termination of a transaction covered by section 104 of the Insolvency Code based on the filing for the opening of Insolvency Proceedings was held to be valid, as such early termination right per se does not modify the legal consequences under section 104 of the Insolvency Code, but the valuation method must not deviate from the method set forth in, and also the point in time relevant for the valuation must not deviate from, section 104 of the Insolvency Code.[98] If the contractually agreed valuation method or the timing of the valuation are not based on the method, and timing stipulated in the version of section 104 of the Insolvency Code in force before 10 June 2016 then such agreement is void under section 119 of the Insolvency Code.

Referring to the BGH decision of 9 June 2016, the legislative reasoning given for the amendments to section 104 of the Insolvency Code explains that a statutory provision would be required to clarify that contractual close-out netting provisions are enforceable in insolvency.[99] The legislative reasoning also clarifies that parties may enter into contractual agreements which deviate from the statutory netting mechanism. However, the relevant contractual agreement must not deviate from the fundamental principles of the statutory provision which is to remedy the uncertainties that would arise from the application of the Selection Right to transactions that fall within the scope of section 104 of the Insolvency Code.[100]

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97 BGH WM 2016, 1168, 1173.

98 BGH WM 2016, 1168, 1173 et seq.

99 BT-Drs. 18/9983, p. 8, 9, 10, 13.

100 BT-Drs. 18/9983, p. 14; for further detail please see Paragraph 5.1.1(i)(ii)(I).

While section 119 of the Insolvency Code was not amended, we construe the legislative reasoning to imply that section 119 of the Insolvency Code needs to be construed in light of the amendments. In any event, there is no scope for the Selection Right under section 103 of the Insolvency Code to the extent section 104 of the Insolvency Code applies and, hence, there is also no room for section 119 of the Insolvency Code in such case.

(C) Scope and analysis of section 104 of the Insolvency Code

Upon the opening of Insolvency Proceedings, section 104 of the Insolvency Code provides for a mandatory automatic termination of those transactions which fall within its scope. If the relevant date for early termination falls after the opening of Insolvency Proceedings the provisions of section 104 of the Insolvency Code would govern the close-out netting of those transactions which fall within its scope. Section 104 of the Insolvency Code would have no effect on those transactions which fall outside its scope and the analysis described above in Paragraph 5.1.1(i)(ii)(B) above would apply thereto, i.e. section 103 of the Insolvency Code would apply to Individual Contracts if they qualify as Executory Contracts and the Insolvency Administrator is entitled to exercise the Selection Right.

As mentioned, the currently applicable version of section 104 of the Insolvency Code entered into force on 29 December 2016 and applies pursuant to Article 5 para 1 of the Third Law Amending the Insolvency Code and the Introductory Act to the Code of Civil Procedure (*Drittes Gesetz zur Änderung der Insolvenzordnung und zur Änderung des Gesetzes betreffend die Einführung der Zivilprozessordnung,* "**Third Insolvency Code Amendment Act**")[101] to all Insolvency Proceedings opened on or after such date. For Insolvency Proceedings opened during the period from 10 June 2016 to 28 December 2016 a further version of section 104 of the Insolvency Code applies, as set out in Articles 1 and 5 para 2 of the Third Insolvency Code Amendment Act.[102]

[101] BGBl. 2016 I, p. 3147.

[102] An English convenience translation of section 104 of the Insolvency Code in the version applicable to Insolvency Proceedings opened during the period from 10 June 2016 to 28 December 2016 is attached as Annex 1 hereto. Immediately after the BGH decision of 9 June 2016, the BaFin issued a general decree (*Allgemeinverfügung*) based on section 4a of the German Securities Trading Act (*Wertpapierhandelsgesetz*) valid no longer than 31 December 2016 and clarifying that contractual netting arrangements in existing

An English convenience translation of Section 104 of the Insolvency Code in the version entered into force on 29 December 2016 is attached as Annex 2 hereto. All references in this Opinion to section 104 of the Insolvency Code are to such version, unless otherwise indicated.

Section 104 para 1 sent. 1 of the Insolvency Code covers fixed date transactions (*Fixgeschäfte*) on commodities (*Waren*) and section 104 para 1 sent. 2 of the Insolvency Code covers financial transactions, which are further defined in sentence 3. Section 104 para 2 of the Insolvency Code provides for a calculation method for the claim for non-performance following the early termination of transactions by section 104 of the Insolvency Code.[103]

Section 104 para 3 of the Insolvency Code expressly recognises "single agreement clauses" with respect to transactions which have been entered into under a master agreement (see Paragraph 5.1.1(i)(ii)(H) below). Section 104 para 4 sent. 1 of the Insolvency Code clarifies that parties to a contract may agree on terms deviating from the statutory netting provision as long as these are compatible with the fundamental principles applicable for the relevant statutory requirement which is being amended and sentence 2 gives examples of permitted deviations.

To summarise, any automatic termination by virtue of section 104 of the Insolvency Code results in a claim for non-performance calculated on the basis of market or exchange

master agreements should continue to be settled as agreed in order to ensure that master agreements would continue to be effective such as to allow recognition of netting arrangements contained therein for supervisory purposes. The version of section 104 of the Insolvency Code applying from 10 June 2016 to 28 December 2016 which entered into force retroactively is intended to replicate the contents of the general decree. According to the legislative reasoning, the retroactive effect is justified as, in view of the general decree, no reliance could be placed by market participants on the interpretation of section 104 of the Insolvency Code as made by the BGH in its 9 June 2016 decision; BT-Drs. 18/9983, p. 10.

103 It is unclear whether it is required that, given that section 104 of the Insolvency Code is a special rule to section 103 of the Insolvency Code, a transaction must qualify as an Executory Contract to fall within its scope (affirming this view with respect to section 104 of the Insolvency Code as in force prior to 10 June 2016, *Jahn/Fried* in: Münchener Kommentar InsO, 3rd ed. (2013), § 104 no. 34; *Bosch*, Kölner Schrift zur Insolvenzordnung, 2nd ed. (1999), p. 1018 no. 33). However, some of the transactions enumerated in section 104 para 1 sentence 3 of the Insolvency Code (such as financial collateral and contracts for difference) do not constitute Executory Contracts (some of them are not even mutual contracts) (see: *Balthasar*, in: Nerlich/Römermann, InsO, (as of July 2016), § 104 no. 31). According to the legislative reasoning to the version of section 104 of the Insolvency Code which entered into force on 29 December 2016, however, rather than the transaction fulfilling the formal requirement of an "Executory Contract", it should be decisive whether the market risks to which the transaction is subject should be captured by the scope of protection awarded by section 104 of the Insolvency Code to the parties, and, in particular, the Solvent Party (BT-Drs. 18/9983, p. 19).

prices subject to section 104 para 2 of the Insolvency Code. The claim for non-performance would, irrespective of the law governing the relevant transaction or agreement, be governed by German law and would generally rank *pari passu* with claims of all other unsecured creditors. The claim for non-performance is expressed in Euro and may be subject to set-off.[104]

(D) Fixed date transactions (*Fixgeschäfte*)

Pursuant to section 104 para 1 sent. 1 of the Insolvency Code, in the event that a defined fixed time or period was agreed exactly for the delivery of commodities (*Waren*) with a market or exchange price, and such time occurs or such period lapses after the opening of Insolvency Proceedings, specific performance may not be demanded, but rather only a claim for non-performance may be asserted. Section 104 para 1 sent. 1 of the Insolvency Code therefore covers fixed date transactions (*Fixgeschäfte*) on tangible commodities (*Waren*) with a market or exchange price only. Gas qualifies as commodity (*Ware*) under section 104 para 1 sent. 1 of the Insolvency Code.[105]

The wording with respect to fixed date transactions was not changed following the amendments made under the Third Insolvency Code Amendment Act to section 104 of the Insolvency Code and according to the legislative reasoning there was no intention to limit the scope of section 104 para 1

[104] Please note that section 104 of the Insolvency Code does in our view not include any set-off (in the legislative reasoning, it is stated that the claim for non-performance arising after termination may generally be set off in insolvency (BT-Drs. 18/9983, p. 21), which indicates that the set-off is not effected by section 104 of the Insolvency Code itself (see also *Ehricke*, ZIP 2003, 273, 277) but, by transforming the former payment and delivery claims into a Euro denominated payment claim, provides a basis for set-off (subject to the general set-off restrictions under contract and insolvency law, as applicable)).

[105] Gas is not expressly mentioned in Article 2 no. 6 of the Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of MiFID II (OJ No L 87 of 31 March 2017, p. 1, "**MiFID Delegated Regulation**") pursuant to which "commodity" means any goods of a fungible nature that are capable of being delivered, including metals and their ores and alloys, agricultural products, and energy such as electricity. See however *Von Wilmowsky* in: Kübler/Prütting/Bork, InsO, 71st update (2017), § 104 no. 57; *Liesenhoff* in: Horstmann/Cieslarczyk, Energiehandel, 1st ed. (2006), chapter 10 no. 89. In the context of derivatives, gas generally qualifies as product commodity (*Ware*) within the meaning of section 1 para. 11 sent. 4 no. 2 of the Banking Act (see (see BaFin, Hinweise zu Finanzinstrumenten nach § 1 Abs. 11 Satz 4 KWG (Derivate) (Stand: Mai 2012, zuletzt geändert am 22. Juli 2013) (Note on financial instruments pursuant to section 1 para 11 Sentence 4 KWG (derivatives), (as of May 2012, amended on 22 July 2013)), no. 2 a) bb)). In our view, the term "commodities" (*Ware*) as defined in section 104 para. 1 of the Insolvency Code includes "objects" (*Sachen*) as defined in section 90 of the German Civil Code (*Kroth* in: Braun, Insolvenzordnung, 7th ed. (2017), section 104 no. 3); gas qualifies as an object (*Stieper* in: Staudinger BGB (2017), § 90 no. 8.

of the Insolvency Code.[106] Hence the reasoning with respect to fixed date transactions based on the law as in force before 10 June 2016 should still be valid. From a German Civil Law perspective, fixed date transactions can be classified in "absolute" fixed date transactions (*absolute Fixgeschäfte*) and "relative" fixed date transactions (*relative Fixgeschäfte*).

Absolute fixed date transactions

Regarding absolute fixed date transactions, the agreed date of performance has such an importance to at least one of the contracting parties that, in case of failure to perform in time, subsequent performance to the performance date stipulated in the contract cannot be considered as a performance of the contractual obligation anymore.[107] Performance in time is the central point of the entire agreement (*die Leistung steht und fällt mit der Einhaltung der Leistungszeit*)[108] and a claim for performance subsequent to the agreed performance date is excluded by law according to section 275 para 1 of the German Civil Code because performance at a later point in time will be useless and will be treated as impossible for the debtor.[109] Delayed performance would not constitute performance in accordance with the agreement but a complete different performance instead.[110]

The question as to whether a transaction qualifies as an absolute fixed date transaction depends on the terms of the agreement, the interests and intention of the parties and the circumstances of the single case, also taking customary practice into consideration.[111] If the parties to an agreement did not provide for an explicit provision, the agreement has to be construed in good faith as to whether or not the parties wanted to attach the consequences of a fixed date transaction to the agreement. According to the BGH, however, any doubts

[106] BT-Drs. 18/9983, p. 18.

[107] *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 271 no. 17, *Krüger* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 271 no. 14; *Ekkenga/Kuntz* in: Soergel, BGB, 13th ed. (2014), § 275 no. 47 *et seqq*.

[108] BGHZ 110, 96; BGH NJW-RR 1989, 1373.

[109] BGH NJW 2009, 2743.

[110] *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 271 no. 17, *Krüger* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 271 no. 14; *Ekkenga/Kuntz* in: Soergel, BGB, 13th ed. (2014), § 275 no. 47 *et seqq*.

[111] Ibid.

concerning the intention of the parties to attach such meaning to the agreement excludes a fixed date transaction.[112]

Relative fixed date transactions

Regarding relative fixed date transactions, timely performance is crucial as well. Relative fixed date transactions are transactions where, due to the importance to receive performance in time, the creditor may no longer be interested in receiving performance by the other party if such performance has not been made on the agreed date. In contrast to absolute fixed date transactions, however, subsequent delivery (*Nachlieferung*) of performance is still possible and the purpose of the agreement can still be achieved. [113] As delayed performance will often not be in the interest of creditors, the German Civil Code provides for a revocation right for the non-defaulting party in such cases (section 323 para 2 no. 2 of the German Civil Code). Nevertheless, the non-defaulting party does not necessarily have to exercise its revocation right. It can also choose to claim for performance and claim damages, too, provided that the obligor is in payment or delivery default pursuant to section 286 of the German Civil Code.

By and large, German courts are reluctant to treat a transaction as a fixed date transaction merely because the agreement provides for a fixed performance or delivery date.[114] According to existing court decisions, an initial indication for the treatment of a transaction as a fixed date transaction is the wording of the agreement, in particular the use of terms such as "fix", "concise", "exactly", "prompt", etc. [115] In contrast, the exclusion of any grace period alone (i.e. the immediate liability for damages in case of default) does not necessarily entail the treatment as a fixed date transaction. [116]

Relative fixed date transactions fall under section 104 para 1 sent. 1 of the Insolvency Code. With regard to absolute fixed date transactions, however, this is disputed in legal literature[117]

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[112] BGH NJW-RR 1989, 1373.

[113] *Ernst* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 286 no. 41.

[114] *Ernst* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 323 no. 118 with further references.

[115] *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 323 no. 20.

[116] BGH NJW 1959, 933; *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 323 no. 20; *Ernst* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 323 no. 118.

[117] As mentioned, in line with BT-Drs. 18/9983, p. 17, 18, we hold the view that the reasoning for the version of section 104 of the Insolvency Code in force before 10 June 2016 is also valid for the versions enacted by the Third Insolvency Code Amendment Act and, accordingly, this dispute is still relevant: *Andres* in:

with the argument that the legislative material with regard to section 104 para 1 of the Insolvency Code in the version in force before 10 June 2016[118] explicitly refers to the former section 361 of the German Civil Code and section 376 of the Commercial Code which solely addresses relative fixed date transactions.[119] However, the wording of section 104 para 1 of the Insolvency Code itself does not give any further guidance and it is also mentioned in the legislative material, that the purpose of section 104 para 1 of the Insolvency Code is to minimise the Insolvency Administrator's ability to speculate.[120] Such purpose can only be achieved if section 104 para 1 of the Insolvency Code also applies to absolute fixed date transactions. In the absence of any court decisions, we would construe section 104 para 1 of the Insolvency Code to cover both, absolute and relative fixed date transactions.[121]

The question whether contracts concerning the delivery and acceptance of gas can be considered as fixed date transactions according to section 104 para 1 sent. 1 of the Insolvency Code depends largely on the characteristics of the contract and the intention of the parties.

With regard to the applicability of section 104 para 1 sent. 1 of the Insolvency Code to the General Agreement and the Individual Contracts thereunder, a German court would, in case of an insolvency, decide on the basis of the terms of the relevant contract whether or not and to which extent the contract constitutes a fixed date transaction, putting emphasis especially on the intention of the parties to such agreement. If

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Andres/Leithaus, Insolvenzordnung, 3rd ed. (2014), § 104 no. 3 and *von Wilmowsky* in: Kübler/Prütting/Bork, InsO, 70th update (2017), § 104 no. 64 argue that section 104 para 1 of the Insolvency Code covers absolute and relative fixed date transactions whereas according to *Lüer* in: Uhlenbruck, Insolvenzordnung, 14th ed. (2015) § 104 no. 6, section 104 para 1 of the Insolvency Code only covers relative fixed date transactions. We also note, however, that most legal commentators do not distinguish between absolute and relative fixed date transactions or at least do not address this issue; see: *Balthasar* in: Nerlich/Römermann, Insolvenzordnung, 30th update (2016), § 104 no. 16; *Jahn/Fried* in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 104 no. 37 *et seq.*; *Braun* in: Insolvenzordnung, 7th ed. (2017), § 104 no. 5; *Häsemayer*, Insolvenzrecht, 4th ed. (2007), p. 495 no. 20.34; with respect to the currently applicable version of section 104 of the Insolvency Code see *Berberich* in: Beck'scher Online-Kommentar InsO, 5th ed. 2017 (31 January 2017), § 104 no. 15 *et seqq*. This also holds true with respect to legal commentaries on the former Bankruptcy Code; see *Kilger* in: Karsten Schmidt, Konkursordnung, 16th ed. (1997), p. 126, 127; *Kuhn* in: Uhlenbruck, Konkursordnung, 11th ed. (1994), § 18 no. 3, 5.

118 Section 108 of the draft Insolvency Code of the Federal Government, BT-Drs. 12/2443, p. 145.

119 BT-Drs. 12/2443, p. 145; BT-Drs. 12/7302, note 69 to section 118 para 1, p. 167.

120 BT-Drs. 18/9983, p. 9, 13; see also BT-Drs. 12/2443, p. 145, as regards the version of section 104 of the Insolvency Code in force before 10 June 2016.

121 See also: *Fried* in: Schwintowski, Handbuch Energiehandel, 3rd ed. (2014), no. 701.

the parties have agreed with respect to an Individual Contract or a common intention can be inferred from the terms of the Individual Contract that a delayed delivery is (broadly speaking) better than no delivery at all and does not render the delivery virtually worthless to the other party but rather qualifies as complete although late fulfilment of the agreement, the transaction will not constitute a fixed date transaction. In these cases and to the extent not covered as financial transaction by section 104 para 1 sent. 2 and 3 of the Insolvency Code, the contract would fall under section 103 para 1 of the Insolvency Code and the Insolvency Administrator would then have the right to decide whether to assume or reject such contract. Such an interpretation is in our view especially appropriate when the agreement provides for a subsequent delivery (*Nachlieferung*).[122]

If the delivery dates are exactly defined by the parties and the party obliged to deliver is aware, due to the terms of the contract, special knowledge or knowledge of the relevant customary practice in the respective industry sector, that any delivery which is not made in time would render such delivery for the party to take delivery worthless, the agreement would qualify as a fixed date transaction, and, thus, would be

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[122] Insofar as contractual performances due to the parties are severable, and if the other party already had performed part of the services incumbent on it on the date when the Insolvency Proceedings were opened, section 105 of the Insolvency Code may be applicable.

An English translation of section 105 of the Insolvency Code reads as follows:

"Severable Contracts

If the contractual performances due to the parties are severable, and if the other party already had performed part of the services incumbent on it on the date when the insolvency proceedings were opened, such other party shall be deemed an insolvency creditor for the amount of its claim to consideration corresponding to the part of the services already performed by it, even if the insolvency administrator claims performance of the services not yet performed. The other party shall not be entitled to claim restitution for non-performance of its claim to the consideration of the part of services transferred to the debtor's assets before the insolvency proceedings were opened."

Severable contractual duties are, according to legislative materials (BT-Drs. 12/2443, p. 145 f.), in particular agreements providing for a successive obligation (*Sukzessivlieferungsverträge*) concerning energy and power supply which are necessary in order to continue business on a regular basis. If the Insolvency Administrator assumes its obligations under such contract according to section 103 para 1 of the Insolvency Code, only the claim regarding the time following the opening of Insolvency Proceedings would constitute a debt incumbent on the estate according to section 55 para 1 no. 2 of the Insolvency Code. With regard to the time previous to the opening of Insolvency Proceedings the non-defaulting party would be an insolvency creditor according to section 105 para 1 of the Insolvency Code (*Reinholz*, RdE 1999, p. 64 *et seq*., p. 73; *Binz/Hess*, Der Insolvenzverwalter, p. 271 no. 1811; *Grüneberg*, in: Palandt BGB, 76th ed. (2017), Überbl v § 311 nos. 28 and 30; *Andres*, in: Andres/Leithaus, Insolvenzordnung, 3rd ed. (2014), § 105 no. 4). Section 105 of the Insolvency Code presupposes the existence/applicability of the Selection Right whilst section 104 of the Insolvency Code excludes such Selection Right. Hence, section 105 of the Insolvency Code is not relevant for determining the scope of application of section 104 of the Insolvency Code.

terminated automatically by virtue of section 104 para 1 sent. 1 of the Insolvency Code. In our view, provisions supporting such interpretation are in particular contractual remedies for failure to deliver and accept delivery pursuant to which the defaulting party has to pay to the other party damages as compensation for non-delivery combined with an explicit exclusion of any subsequent delivery after the date agreed for delivery.[123] Under such provisions it becomes apparent that delivery at the due date is of such importance to the parties or at least one party that it is the central point of the transaction (*das Geschäft steht und fällt mit der Leistung*)[124] and that a delayed delivery will not be accepted. Other indicators for fixed date transactions would be contractual agreements according to which it is apparent to the defaulting party that the non-defaulting party, in the event of a failure to deliver, will directly and without any grace-period or prior notice accept delivery of a third party or delivery on account of a third party by a central delivery point instead of subsequent delivery by the defaulting contractual party. As a consequence, such transactions would fall under section 104 para 1 sent. 1 of the Insolvency Code and, thus, within the scope of a statutory exemption from the Selection Right, and the parties may agree on an insolvency related termination in respect of such transaction, provided that such termination is triggered prior to the opening of the Insolvency Proceedings (please refer to Paragraph 5.1.1(i)(ii)(A) above).

The Agreement (as defined in Section 1.1 of the General Agreement) may, in case no Automatic Termination applies, be terminated for Material Reason in accordance with Section 10.3 of the General Agreement. Such termination requires a notice of Early Termination and the designation of an Early Termination Date, such date not earlier than the day the notice is deemed to have been received not later than 20 days after such day. With respect to the definition of Material Reason in Section 10.5 of the General Agreement, in the event of a Non Performance a grace period of two Business Days or 10 Business Days is given and a Failure to Deliver or Accept will only constitute a Material Reason if such failure continues for

[123] With respect to the version of section 104 of the Insolvency Code in force before June 2016, please also refer to *Fried* in: Zerey, Finanzderivate, 4th ed. (2016), § 21 no. 52 *et seq.*; *Liesenhoff* in: Horstmann/Cieslarczyk, Energiehandel, 1st ed. (2006), chapter 10 no. 89; *Fried/Wulff*, Der EFET-Rahmenvertrag für Stromlieferungen in Recht und Praxis, ET 2003, p. 812 *et seq*., p. 814.

[124] With respect to the version of section 104 of the Insolvency Code in force before June 2016, please also refer to *Liesenhoff* in: Horstmann/Cieslarczyk, Energiehandel, 1st ed. (2006), chapter 10 no. 25 and 89, see above; *Tegethoff/Büdenbender/Klinger*, Das Recht der öffentlichen Energieversorgung, § 103 GWB no. 31; *Börner* in: Veröffentlichungen des Instituts für Energierecht (VEnerGR 30), p. 26.

more than 7 consecutive days or for more than 7 days in aggregate within a period of 60 days. The existence of such grace periods may result in the conclusion that Individual Contracts may not qualify as fixed date transactions. However, such conclusion would ignore the fact that Section 10 of the General Agreement refers to the Agreement and, thus, to the business relationship entered into under the Agreement. Section 10 of the General Agreement does not necessarily modify the terms of Individual Contracts and would not necessarily be decisive when analysing whether Individual Contracts may qualify as fixed dated transactions (section 104 para 1 sent. 1 of the Insolvency Code does not refer to master agreements but to individual transactions only).

More importantly, Section 8 of the General Agreement stipulates the remedies for failure to deliver and accept. Such section does not provide for any grace periods or notification requirements. Rather, any failure to deliver or to accept in accordance with the terms of the Individual Contract will result in a compensation claim for damages unless such failure is excused by an event of Force Majeure or the other Party's non-performance. As damages will become immediately payable, Section 8 of the General Agreement *per se* excludes any subsequent delivery and, therefore, shows together with the individually agreed delivery times the characteristics of a fixed date transaction. In the absence of any provision to the contrary in the relevant Individual Contract, we think that based on Section 8 of the General Agreement Parties should be able to argue that Individual Contracts fall within section 104 para 1 sent. 1 of the Insolvency Code.[125] With respect to any further details, please also refer to Annex 3 to this Opinion.

(E) Financial transactions within the meaning of section 104 para 1 sent. 2, 3 of the Insolvency Code

Section 104 para 1 sent. 2 of the Insolvency Code applies to financial transactions (*Finanzleistungen*) as further defined in section 104 para 1 sent. 3 of the Insolvency Code. Financial transactions are transactions which have a market or exchange price, and for which a particular time or period was agreed

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[125] With respect to the version of section 104 of the Insolvency Code in force before June 2016 please refer to *Liesenhoff* in: Horstmann/Cieslarczyk, Energiehandel, 1st ed. (2006), chapter 10 nos. 25 and 89; further *Tegethoff/Büdenbender/Klinger*, Das Recht der öffentlichen Energieversorgung, § 103 GWB no. 31; *Börner* in: Veröffentlichungen des Instituts für Energierecht (VEnerGR 30), p. 26.

which only occurs or expires after the opening of insolvency proceedings.[126]

Whereas section 104 of the Insolvency Code does not define what would constitute a market or exchange price, in our view, the interpretation of this requirement can be based on generally applicable principles of civil law such as section 385 of the German Civil Code.[127]

Section 104 para 1 sent. 3 of the Insolvency Code gives examples of financial transactions. The wording of section 104 para 1 sent. 3 of the Insolvency Code indicates that the enumeration of financial transactions is not conclusive (indicated by the words "in particular"). The legislative reasoning also shows that the words "in particular" are intended to address any future developments with respect to financial transactions.[128] Furthermore, based on the purpose of section 104 of the Insolvency Code, which is to limit the Insolvency Administrator's ability to speculate on price or market developments with respect to volatile instruments by not deciding whether to assume or reject any obligations subject to the Selection Right,[129] a court may accept that transactions showing comparable features to the enumerated financial transactions and in respect of which the same concerns may arise which the legislator has raised to justify the exemptions from the Selection Right under section 104 of the Insolvency Code, could be covered by section 104 para 1 sent. 2 of the Insolvency Code even if not explicitly mentioned.[130] In this

[126] Based on its wording, undated transactions (e.g. transactions which are due upon the giving of notice or transactions with an undetermined period of time) are outside the scope of application of section 104 para 1 sent. 1 of the Insolvency Code.

[127] According to section 385 of the German Civil Code, which is a provision of generally applicable civil law, a market or exchange price is given if at the relevant place the relevant assets are traded to an extent which allows the determination of a market or exchange price on the basis of the transactions which have taken place. A market price is available where based on the frequency of transactions an average price can be determined. According to the reasoning of the German legislator to the version of section 104 of the Insolvency Code applicable before 10 June 2016 (see BT-Drs. 12/7302, p. 168), the term "market or exchange price" within the meaning of section 104 para 2 sentence 1 of the Insolvency Code needs to be construed broadly. With respect to the version of section 104 of the Insolvency Code currently in force the references to market and exchange price in the legislative reasoning are focusing on the calculation methods under section 104 para 2 of the Insolvency Code. The BGH has referred to the possibility of entering into replacement transactions, BGH WM 2016, 1168, 1174.

[128] BT-Drs. 18/9983, p. 11, 18.

[129] BT-Drs. 18/9983, p. 9. This was already the case with respect to the version of section 104 of the Insolvency Code as applicable before 10 June 2016; BT-Drs. 12/2443, p. 145; BT-Drs. 12/7302, p. 167.

[130] With respect to the version of section 104 of the Insolvency Code applicable before 10 June 2016 see: *Jahn/Fried*, in: Münchener Kommentar InsO, 3rd ed. (2013), § 104 no. 52; *Balthasar*, in: Nerlich/Römermann, Insolvenzordnung, 30th update (2016), § 104 no. 40 et seq.; *Kroth*, in: Braun,

respect the legislative reasoning clarifies that interests of the Solvent Party and the interests of the insolvency estate need to be balanced.[131]

Financial transactions are transactions on the delivery of precious metals (no. 1), the delivery of financial instruments or comparable rights, except where there is an intention to acquire an interest in another enterprise with the aim of establishing a long-term relationship with that enterprise (no. 2), payments of money which are to be made in a foreign currency or in a mathematical unit, or the amounts of which are calculated, directly or indirectly by referencing to the exchange rate of a foreign currency or a unit of account, to the interest rate for borrowings or to the price of other goods (*Güter*) or services (no. 3), deliveries and payments from derivative financial instruments except where there is an intention to acquire an interest in another enterprise with the aim of establishing a long-term relationship with that enterprise (no. 4), options and other rights to demand delivery of commodities (*Waren*) or for delivery, payment or options and rights within the meaning of numbers 1 to 5 above (no. 5) and financial collateral within the meaning of section 1 para 17 of the Banking Act (no. 6). Pursuant to section 104 para 1 sent. 4 of the Insolvency Code financial instruments within the meaning of section 104 para 1 sent. 3 numbers 2 and 4 of the Insolvency Code are those instruments listed in Annex I Section C MiFID II, as last amended by Directive (EU) 2016/1034 (OJ No L 175 of 30 June 2016, p. 8).[132]

According to the legislative reasoning the newly enacted enumeration of financial transactions is not intended to exclude any financial transactions which were already covered by the version of section 104 of the Insolvency Code applicable prior to 10 June 2016. Rather, the changes are intended to simplify the definition of financial transactions.[133] Whether or not a transaction would be covered by section 104 para 1 sent. 3 no.

Insolvenzordnung, 7th ed. (2017), § 104 no. 6; *Lüer*, in: Uhlenbruck, InsO, 14th ed. (2015), § 104 no. 11. Even though the scope of financial transactions covered by section 104 of the Insolvency Code has been broadened by the amendments, the provisions before and after the amendments are based on the same principles.

131 BT-Drs. 18/9983, p. 10.

132 It is not entirely clear whether the reference to MiFID II is intended to be static or whether this also encompasses future amendments of MiFID II. Ultimately, this appears to be irrelevant, since the non-conclusive enumeration of covered financial transactions ensures that future developments in this respect can be captured.

133 BT-Drs. 18/9983, p. 18.

2 of the Insolvency Code depends on whether the transaction is aiming at the delivery of a financial instrument rather than whether the transaction giving rise to such entitlement is a financial instrument.[134] Options and other rights to demand delivery of commodities (*Waren*) covered by section 104 para 1 sent. 1 of the Insolvency Code as well as options and other rights to demand delivery or payment, option rights under section 104 para 1 sent. 3 numbers 1 to 5 of the Insolvency Code, including options on such options are covered, too.

With respect to the version of section 104 of the Insolvency Code applicable before 10 June 2016, the majority of German legal authors held the view that section 104 of the Insolvency Code may also apply to spot transactions which are settled in two or more days (*Kassageschäfte*).[135] Based on the wording of section 104 of the Insolvency Code and the legislative reasoning we believe that this view can still be followed but we are not aware of any court decisions on this matter. Where the qualification as a financial transaction within the meaning of section 104 of the Insolvency Code depends on the qualification as a derivative transaction within the meaning of MiFID II, spot transactions would not qualify as financial transactions within the meaning of section 104 of the Insolvency Code.[136]

Spot transactions are transactions with short term delivery or respectively, fulfilment dates which are not entered into at a futures or forward market. The participants in a spot transaction agree to buy and sell, respectively, at the present market value and to settle the transaction a few days later (usually few more or even less than two business days).[137] Spot transactions,

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[134] BT-Drs. 18/9983, p. 18. The legislative reasoning also clarifies that repurchase agreements and securities lending agreements fall within the scope of section 104 para 1 sent. 3 no 2 of the Insolvency Code.

[135] One of the arguments brought forward is that there may be a risk of loss in between signing of a contract and settlement due to market movements similar to forward transactions and which are covered by section 104 of the Insolvency Code. Furthermore, the wording of section 104 of the Insolvency Code only provides for a "specified time or a specified period agreed for the performance of financial transactions", i.e. requires a specified period or time to be agreed for performance of the obligations does, however, not stipulate a minimum period and therefore only excludes cash transactions. For more details please refer to: *Jahn/Fried*, in: Münchener Kommentar InsO, 3rd ed. (2013), § 104 nos. 88 *et seq*; *Jahn*, in: Schimansky/Bunte/Lwowski, Bankrechts-Handbuch, 4th ed. (2011), § 114 no. 140; *Wegener*, in: Frankfurter Kommentar InsO, 8th ed. (2015), § 104 no. 21; *Bosch*, Kölner Schrift zur Insolvenzordnung, 2nd ed. (1999), p. 1027 no. 72; for a different view see: *Meyer*, in: Smid, Insolvenzordnung, 2nd ed. (2001), § 104 no. 11.

[136] For further details see Annex 3 of this Opinion; See also Recital 8, Article 7 and Article 10 of MiFID Delegated Regulation.

[137] BGH NJW 2002, 892, 892; *Bosch*, Kölner Schrift zur Insolvenzordnung, 2nd ed. (1999), p. 1027 no. 72. The term spot transaction is also defined in Article 7 para 2 of the MiFID Delegated Regulation defining a

however, have to be distinguished from mere cash transactions (*Bargeschäfte*) which are settled same day and not covered by section 104 of the Insolvency Code.

(F) Financial collateral as financial transaction

Under section 104 para 1 sent. 3 no. 6 of the Insolvency Code, financial collateral within the meaning of section 1 para 17 of the Banking Act will also qualify as a financial transaction. According to the legislative reasoning this provision is intended to implement Article 7 of the Financial Collateral Directive by ensuring that Financial Collateral can also be enforced by set-off under a close-out netting agreement.[138] The wording of section 104 para 1 sent. 3 no. 6 of the Insolvency Code only refers to Financial Collateral, i.e. the asset constituting the Financial Collateral but it does not state that transactions which are secured by Financial Collateral will be within the scope of this provision. The legislative reasoning is not clear either as reference is made to the creation of Financial Collateral and that Financial Collateral, other than transactions covered by section 104 para 1 sent. 3 nos. 1 to 5 of the Insolvency Code, will not be the "main obligation" forming part of an Executory Contract. This appears to protect Financial Collateral as such from the Selection Right but it does not create an exemption for the transactions secured by Financial Collateral which themselves do not constitute financial transactions within the meaning of section 104 para 1 of the Insolvency Code. Article 7 of the Financial Collateral Directive provides that EU member states shall ensure that a close-out netting provision can take effect in accordance with its terms. To achieve the purpose of Article 7 of the Financial Collateral Directive there are good arguments to construe section 104 para 1 sent. 3 no. 6 of the Insolvency Code broadly. However, the definition of "close-out netting" under the Financial Collateral Directive[139] refers to financial collateral arrangements and such term again

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spot contract as a contract for the sale of a commodity, asset or right, under the terms of which delivery is scheduled to be made within the longer of the following periods: (a) two trading days; (b) the period generally accepted in the market for that commodity, asset or right as the standard delivery period.

[138] BT-Drs. 15/1853, p. 11, 12.

[139] Under Article 2 para 1 lit (n) of the Financial Collateral Directive "close-out netting provision" means 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.

refers in our view to the collateral as such but not to the secured obligation or any transaction to be secured. We would therefore construe section 104 para 1 sent. 3 no. 6 of the Insolvency Code such that, while also Financial Collateral may be included in the close-out netting (and, accordingly, would not be being subject to any Selection Right[140]), the mere collateralisation of a transaction normally not covered by section 104 para 1 sent. 3 of the Insolvency Code does not result in the application of section 104 para 1 sent. 3 of the Insolvency Code. However, as far as we are aware, no court decisions exist in respect of the interpretation of section 104 para 1 sent. 3 no. 6 of the Insolvency Code.

(G) Calculation of the amount of the claim for non-performance

Pursuant to section 104 para 2 sent. 1 of the Insolvency Code, the amount of any claim for non-performance is determined on the basis of the market or exchange value of the transaction.[141] Sent. 2 of section 104 para 2 of the Insolvency Code states that the market or exchange value is deemed to be the market or exchange price for a replacement transaction which is concluded without undue delay, but no later than on the fifth business day after the opening of insolvency proceedings (no. 1), or if no replacement transaction is entered into in accordance with no. 1, the market or exchange price for a replacement transaction, that could have been concluded on the second business day after the opening insolvency proceedings (no. 2).

To the extent that the market conditions do not allow for the conclusion of a replacement transaction pursuant to section 104 para 2 sent. 2 numbers 1 or 2 of the Insolvency Code, the market or exchange value is to be determined by way of methods and procedures allowing for an adequate assessment of the value of the transaction (section 104 para 2 sent. 3 of the Insolvency Code). This is the case if the relevant markets are inactive or if the prices available do not properly reflect the prices that would be determined under usual market conditions.[142]

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[140] With respect to the version of section 104 of the Insolvency Code applicable before 10 June 2016, see also *Jahn/Fried*, in: Münchener Kommentar InsO, 3rd ed. (2013), § 104 no. 27 and no. 75a.

[141] Please also refer to BT-Drs. 18/9983, p. 20.

[142] See the legislative reasoning in BT-Drs. 18/9983, p. 16, by reference to Article 16 of the Commission Delegated Regulation (EU) No 149/2013 of 19 December 2012 supplementing Regulation (EU) Nr.

(H) Section 104 of the Insolvency Code and master agreements

Section 104 para 3 sent. 1 of the Insolvency Code provides that where transactions pursuant to section 104 para 1 of the Insolvency Code are combined in a master agreement or the rules of a central counterparty within the meaning of section 1 para 31 of the Banking Act, which provides that the covered transactions may, upon the occurrence of certain events, only be terminated in their entirety, then the entirety of such covered transactions shall be deemed one single transaction within the meaning of section 104 para 1 of the Insolvency Code. This also applies if transactions are covered by such agreement or rules, which neither qualify as fixed date transactions nor as financial transactions. Such transactions would be subject to the general provisions (section 104 para 3 sent. 2 of the Insolvency Code).[143] By referring to the generally applicable provisions section 104 para 3 sent. 2 of the Insolvency Code refers also to the Selection Right. So if and to the extent Individual Contracts neither qualify as fixed date transactions nor as financial transactions such transactions would be subject to the Selection Right and, thus, to different treatment.

The Insolvency Code does not provide for a more detailed definition of the term "master agreement". Express precondition is only that the master agreement must provide for a termination of the entire agreement (including all transactions under the master agreement) where specified reasons allow for such termination.

Under Section 10.5 (c) (ii) of the General Agreement, upon a Party becoming insolvent or being unable to pay its debts, the Agreement may, in case no Automatic Termination applies, be terminated. By reference to the term "Agreement" Section 10.5 (c) (ii) of the General Agreement provides for a termination of all Individual Contracts and the General Agreement. This

648/2012 on OTC derivatives, central counterparties and trade repositories (OJ No L 52 of 23 February 2013, p. 11).

143 With respect to section 104 para 2 of the Insolvency Code as applicable prior to 10 June 2016, it was disputed among legal commentators whether (1) one non-qualifying transaction would also prevent the application of section 104 para 2 of the Insolvency Code for such transactions which would qualify as financial transactions, or (2) section 104 para 2 of the Insolvency Code applies to all transactions, even if only one or some of the transactions qualify as financial transactions or (3) only those transactions under the master agreement which qualify as financial transactions are covered by section 104 para 2 of the Insolvency Code, whereas such transactions which do not qualify as financial transactions remain outside its scope and are therefore individually subject to the Selection Right. This has now been clarified in section 104 para 3 sent. 2 of the Insolvency Code in favour of the third option.

implies that, accordingly, the General Agreement would in our view qualify as master agreement within the meaning of section 104 para 3 of the Insolvency Code.

(I) Contractual close-out netting

Transactions falling within the scope of section 104 para 1 of the Insolvency Code, which at the time of opening of Insolvency Proceedings have not been terminated (irrespective of whether or not entered into under a master agreement), terminate automatically and the claim for non-performance is calculated on the basis of the statutory netting provisions under section 104 para 2 of the Insolvency Code. Transactions not falling within the scope of section 104 para 1 of the Insolvency Code, which are Executory Contracts, are subject to the Selection Right. Contractual close-out netting provisions are recognised under German law and pursuant to section 104 para 4 sent. 1 of the Insolvency Code contractual parties may agree deviating provisions as long as these are compatible with the fundamental principles applicable to the relevant statutory provision which is to be amended.

Scope of contractual close-out netting

Pursuant to section 104 para 4 sent. 2 of the Insolvency Code parties may, in particular, agree that the effects of section 104 para 1 of the Insolvency Code may apply prior to the opening of Insolvency Proceedings, in particular upon the application by a party to the contract for the opening of Insolvency Proceedings over its assets or upon the existence of a reason for the opening for Insolvency Proceedings (contractual termination) (no. 1), that a contractual termination will encompass also such transactions pursuant to section 104 para 1 of the Insolvency Code in respect of which the claim for delivery of the commodities (*Waren*) or the performance of the financial transaction becomes due prior to the opening of Insolvency Proceedings, but after the point in time agreed for the contractual termination (no. 2), that for the purposes of the determination of the market or exchange value of the transaction the point in time of the contractual termination applies instead of the point in time of the opening of Insolvency Proceedings (no. 3 lit (a)), the entering into of the replacement transaction pursuant to section 104 para 2 sent. 2 no. 1 of the Insolvency Code may occur until the 20th business day after the contractual termination, if this is required to ensure that the unwinding of the transaction is performed in a manner that will maximise value (no. 3 lit (b)), or instead of the point in time specified in section 104 para 2 sent. 2 no. 2 of the Insolvency

Code a point in time or a period between the contractual termination and the expiry of the fifth business day following such termination shall apply (no. 3 lit (c)).

The reference to "in particular" indicates, as also stated in the legislative reasoning, that the above enumerated deviations are mere examples which are all guided by the principle that such deviations are permissible as long as these are compatible with the fundamental principles applicable to the relevant statutory requirement which is to be amended.[144] Hence, section 104 para 4 of the Insolvency Code limits contractual close-out netting provisions and prohibits that they contradict the purpose of the statutory close-out netting.[145] The legislative reasoning also mentions the valuation on the basis of an actual or hypothetical replacement transaction and that the relevant extended periods for valuations may only be used if and to the extent such time is necessary due to the complexity of the relevant portfolio.[146]

While we are not aware of any court decision or any further guidance in the legislative reasoning we hold the view that there is no need to explicitly refer to section 104 para 4 of the Insolvency Code when agreeing on any deviations from the statutory netting requirements, in particular from the timing and method of valuation set out under section 104 para 2 of the Insolvency Code.

As already mentioned above, while single agreement clauses are generally permissible in accordance with section 104 para 3 of the Insolvency Code, based on our understanding of section 104 para 4 of the Insolvency Code parties may not agree to extend section 104 of the Insolvency Code to such transactions which are not covered by section 104 para 1 of the Insolvency Code (however bearing into mind that with respect to financial transactions section 104 para 1 sent. 3 of the Insolvency Code is not conclusive but is intended to provide for examples of potentially covered transactions, see Paragraph 5.1.1(i)(ii)(E) above for more details).

Turning to the General Agreement, to the extent any of the Material Reasons stipulated in Section 10.5 of the General Agreement are insolvency related termination events (in particular Section 10.5 lit (c) of the General Agreement) the

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144 BT-Drs. 18/9983, p. 14.

145 BT-Drs. 18/9983, p. 1, 14.

146 BT-Drs. 18/9983, p. 22. As regards the time period relevant for valuation the legislative reasoning refers to Article 285 para 3 of the CRR.

restrictions under sections 119, 104 para 4 of the Insolvency Code need to be observed. Section 104 of the Insolvency Code does not limit the Parties' ability to agree on certain insolvency related termination events *per se*. Rather, the Parties may agree that an early termination may be effected prior to the opening of Insolvency Proceedings, in particular upon the application by a Party to the Master Agreement for the opening of Insolvency Proceedings over its assets or upon the existence of a reason for the opening for Insolvency Proceedings (contractual termination pursuant to section 104 para 4 sent. 2 no. 1 of the Insolvency Code). Pursuant to section 104 para 4 sent. 2 no. 2 of the Insolvency Code a contractual termination may also encompass such Individual Contracts in respect of which the claim for delivery of the commodities (*Waren*) or the performance of the financial transaction becomes due prior to the opening of Insolvency Proceedings, but after the point in time agreed for the contractual termination. In the absence of any additionally stipulated requirements we believe that the Parties do not need to make explicit reference to section 104 para 4 sent. 2 no. 2 of the Insolvency Code but all Individual Contracts qualifying under such provision would be captured automatically.

Section 10.4 of the General Agreement enables the Parties to agree on an Automatic Termination by making the relevant selection in the Election Sheet. The wording of section 104 para 4 of the Insolvency Code does not exclude an agreement on the automatic early termination. As regards the timing, any potentially available discretion with respect to the determination of the Early Termination Date (Section 10.3 lit (b) of the General Agreement) or with respect to the triggering of the payment of the Termination Amount (Section 10.3 lit (d) of the General Agreement) needs to be exercised in light of section 104 para 4 of the Insolvency Code. The references to the point in time when the relevant market or exchange value of the Individual Contracts needs to be determined (section 104 para 4 sent. 2 no. 3 lit (a) of the Insolvency Code) or the period in time which is relevant for the entering into any replacement transactions (section 104 para 4 sent. 2 no. 3 lit (b), para 2 sent. 2 no. 1 of the Insolvency Code) need also to be observed but to the extent the General Agreement is governed by and construed under German law we understand that the rights under the General Agreement can be exercised to comply with these requirements. If and to the extent the Parties would like to make use of the discretion available under section 104 para 4 sent. 2 no. 3 lit (c), para 2 sent. 2 no. 2 of the Insolvency Code the Parties would need to agree on a specific date but not later than on the fifth working day after the opening of Insolvency Proceedings or, as the case may be, after the occurrence of the contractual termination.

When calculating the relevant Settlement Amounts by determining the Gains and Losses as defined under Section 11.2 sent. 2 lit (b) and (c) of the General Agreement the relevant Terminating Party needs to calculate this on the basis of the relevant market or exchange price but as provided in sentence 3 of Section 11.2 of the General Agreement the Terminating Party may refrain from entering into a replacement transaction at its discretion (see section 104 para 2 sent. 2 no. 2 of the Insolvency Code). As regards the calculation of Costs as defined under Section 11.2 sent. 2 lit (a) of the General Agreement, such costs and expenses may in our view not be included in the calculation of the market or exchange price but they can be set off against any market or exchange price in line with generally applicable set-off rights in an insolvency (see Paragraph 5.1.1(o) below). As long as the restrictions for an insolvency set-off are observed we do not believe that the inclusion of Costs in the calculation of the Settlement Amounts would violate section 104 of the Insolvency Code and would thus be void under section 119 of the Insolvency Code. However, we are not aware of any specific guidance or court decision on this question.

Contractual close-out netting and section 119 of the Insolvency Code

Any contractual agreement excluding or limiting the application of the Insolvency Administrator's Selection Right under section 103 of the Insolvency Code in advance is void (section 119 of the Insolvency Code). As also mentioned, in its judgments of 15 November 2012 and 9 June 2016 the BGH has construed section 119 of the Insolvency Code widely to better protect the insolvency estate and the Selection Right. While it is not clear to what extent the BGH will follow such decisions in future, the BGH would need to consider the legislative reasoning on the amendment of section 104 of the Insolvency Code. Furthermore, the BGH has also ruled that there is no room for the Selection Right where section 104 of the Insolvency Code applies and, thus, there is also no room for protecting the Selection Right under section 119 of the Insolvency Code. Accordingly, as long as the General Agreement is in line with section 104 of the Insolvency Code, including any deviations from section 104 para 2 of the Insolvency Code as permitted by section 104 para 4 of the

Insolvency Code, the General Agreement should not be rendered void under section 119 of the Insolvency Code in Insolvency Proceedings.

If a court considered that a specific provision of the General Agreement violates section 119 of the Insolvency Code, it would, in a second step, have to consider whether any potential violation would render the relevant agreement void in whole or only in part or whether the agreement needs to be construed or applied in a way that it just meets applicable statutory requirements.[147] Generally the relevant contractual term which was void cannot be construed in a way that it continues to apply to the extent it would be valid (*Verbot der geltungserhaltenden Reduktion*). However, to the extent the relevant provision containing the wording which violates applicable law also contains wording which does not violate applicable law can be separated both from the perspective of the textual presentation and the contents then the wording which violates applicable law can be stricken off (also sometimes referred to as the "blue pencil test"). This would however mean that, after striking off the wording violating applicable law, the remaining text of the provision is in itself understandable without the need of any further interpretation or explanation.[148] We are not aware of any court decisions on this question but we hold the view that the relevant contractual provision would be void in its entirety and cannot be construed in a way that it can still be applied, even though to a limited extent only.

If the General Agreement is not governed by German law, outside Insolvency Proceedings, a German court would have to consider section 119 of the Insolvency Code an "overriding mandatory provision of German law" in accordance with Article 9 para 2 of the Rome I Regulation to hold any provisions of the Agreements invalid.[149] Mandatory provisions

[147] *Berberich* in: Beck'scher Online-Kommentar InsO, 5th ed. 2017 (31 January 2017), § 119 no. 37. The effects of a partial invalidity are also not addressed in section 104 para 3 sentence 2 of the Insolvency Code. By way of further background, the interpretation of section 119 of the Insolvency Code is a matter of German law only and not a matter of interpretation of the relevant contractual agreement which needs to be made under its respective governing law (see also Article 12 para 1 of the Rome I Regulation).

[148] See BGHZ 107, 185, 190 *et seq.;* BGHZ 145, 203, 212; *Basedow* in: Münchener Kommentar BGB, 7th ed. (2016), § 306 no. 18; *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 306 no. 7; *Roloff* in: Erman BGB, 14th ed. (2014), § 306 no. 11; *Schmidt* in: Ulmer/Brandner/Hensen AGB-Recht, 12 th ed. (2016), § 306 nos. 12 *et seqq*.

[149] According to a view expressed in legal literature (*Andres*, in: Andres/Leithaus/Dahl, Insolvenzordnung, 3rd ed. (2014), § 119 no. 3), section 119 of the Insolvency Code is a statutory prohibition (*Verbotsgesetz*) within the meaning of section 134 of the German Civil Code. Pursuant to section 134 of the German Civil Code and to the extent German law applies, any legal transaction (*Rechtsgeschäft*) which violates a statutory prohibition is void (i.e. the relevant insolvency related termination provision is regarded as not validly

within this meaning are provisions the observance of which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract under Rome I.

Should the Netting Provisions be regarded as not being in line with section 104 para 4 of the Insolvency Code and should a court conclude that in such case the Netting Provisions would be held void pursuant to section 119 of the Insolvency Code in Insolvency Proceedings, netting is still permissible under section 104 para 1 of the Insolvency Code if and to the extent the relevant Individual Contracts fall within the scope of section 104 para 1 of the Insolvency Code.

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agreed), unless a contrary intention appears from such statute. However, according to our view, section 119 of the Insolvency Code has to be construed narrowly as it limits the parties' freedom to contract. If section 119 of the Insolvency Code were to be construed as a statutory prohibition of agreements which exclude or limit the application of sections 103 to 118 of the Insolvency Code, the relevant termination right would be void pursuant to section 134 of the German Civil Code from the point in time such termination right has been agreed. Hence, there would be no room for the application of section 119 of the Insolvency Code, as the contemplated termination of the agreement would already be invalid pursuant to section 134 of the German Civil Code. Therefore, in our view section 119 of the Insolvency Code cannot be regarded as a statutory prohibition in the meaning of section 134 of the German Civil Code. The better arguments are therefore that section 119 of the Insolvency Code should be treated as procedural insolvency provision.

If a German court took a different view and considered section 119 of the Insolvency Code as a statutory prohibition under German law, the question arises whether a partial invalidity of the insolvency related termination provision would result in its invalidity as a whole. Under section 139 of the German Civil Code, if an agreement is partially void, the entire agreement is void, unless the parties would also have entered into the agreement without the part which is void. Section 139 of the German Civil Code is only a rule of interpretation which applies if the agreement does not contain a provision regarding the consequences of a partial invalidity. Section 23.4 of the General Agreement provides that a partial invalidity of a provision of the General Agreement does not affect or impair the legality, validity and enforceability of the other provisions of the General Agreement. Rather, the relevant provision is replaced by a provision "which comes as close as possible to the invalid provision as regards its economic intent". Thus, one could argue that in Section 23.4 of the General Agreement, the parties of the General Agreement have expressed their intention that even though the termination of those Individual Contracts which do not fall within the scope of section 104 of the Insolvency Code may not be valid, this does not affect the termination of the other Individual Contracts. In addition, one may argue that the replacing provision for purposes of Section 23.4 of the General Agreement, "which comes as close as possible to the invalid provision as regards its economic intent" would be a provision according to which at least those Individual Contracts falling within the scope of section 104 of the Insolvency Code are terminated. Whether or not an Individual Contract is included within the scope of the General Agreement is a factual matter that arises at the time such inclusion is made, and should therefore not invalidate the termination provision as such.

(iii) Challenging of the entering into the General Agreement, entering into the Individual Contracts thereunder and the early termination

The entering into the General Agreement, the entering into the Individual Contracts thereunder and the early termination may be challenged by the Insolvency Administrator under sections 129 *et seq.* of the Insolvency Code upon the opening of Insolvency Proceedings within the insolvency challenge periods as specified in Paragraph 5.1.1(c) above.

(j) *Assuming the Parties have elected Automatic Termination to apply, are the provisions of the General Agreement terminating the General Agreement (including all Individual Contracts) upon the occurrence of a Material Reason described in Section 10.5(c) of the General Agreement enforceable under the laws of Germany or is there a risk that the automatic termination could be challenged by a liquidator, administrator, receiver or third party?*

Our answers under Paragraph 5.1.1(c) apply *mutatis mutandis*.

(k) *Would you recommend to elect Automatic Termination to apply upon a Material Reason described in Section 10.5(c) of the General Agreement or upon other events not specified therein?*

Parties may only benefit from electing Automatic Termination upon a Material Reason described in Section 10.5(c) of the General Agreement to the extent that such termination provision does not violate section 119 of the Insolvency Code (please refer to Paragraph 5.1.1(i)(ii) above). However, a termination of Individual Contracts prior to the opening of Insolvency Proceedings would in our view not violate section 119 of the Insolvency Code if section 104 of the Insolvency Code applies. Since Individual Contracts falling within the scope of section 104 para 1 of the Insolvency Code will, upon the opening of Insolvency Proceedings, be terminated and valued pursuant to section 104 of the Insolvency Code if they have not been contractually terminated before, we recommend to elect Automatic Termination to prevent that a contractual termination by notice only becomes effective after the opening of Insolvency Proceedings. Parties may also make use of the discretion provided under section 104 para 4 of the Insolvency Code.

(l) *Would it be necessary or advisable to modify the scope of Automatic Termination (e.g. by (i) deleting or modifying some of the events listed in Section 10.5(c) of the General Agreement which would trigger the termination and/or (ii) by adding other Material Reasons upon the occurrence of which Automatic Termination should also apply and/or (iii) by limiting those insolvency events specified in Section 10.5(c) of* *the General Agreement which would trigger the Automatic Termination) or to specify, or to refrain from specifying, a certain grace period as contemplated in Section 10.5(c)(iv) of the General Agreement to provide for optimal timing of such termination under local law?*

As set out under Paragraph 5.1.1(i)(ii) above, an automatic termination based on non-insolvency related events or on a Party's application to commence Insolvency Proceedings against its assets and/or the existence of any material reason for such an application (such as over-indebtedness) is enforceable under German law, provided that the relevant Individual Contracts fall within the scope of section 104 of the Insolvency Code. A termination right directly based on an actual opening of Insolvency Proceedings is considered to be legally ineffective.

Subject to our answers given under Paragraph 5.1.1(o), if parties intend that the contractual provisions agreed under the General Agreement, rather than the German mandatory insolvency provisions (where applicable), continue to apply, the parties should agree on an Automatic Termination which triggers sufficiently early enough to prevent the application of mandatory insolvency provisions. For such purposes, Automatic Termination should be triggered upon an application filed for the commencement of Insolvency Proceedings or other bankruptcy proceedings against the assets of any Party as is provided for in Section 10.5 (c)(iv) of the General Agreement (see also section 104 para 4 sent. 2 no. 1 of the Insolvency Code). However, in order to avoid that Automatic Termination is triggered even if a third party has frivolously filed an application for the opening of Insolvency Proceedings, it is possible to refer to the adverse economic situation of the relevant Party which would either be evidenced if this Party has either filed the application itself or if reference were made to the Party being insolvent or otherwise in a situation which justifies the opening of such proceedings.[150]

In order to avoid that Automatic Termination is triggered by unsubstantiated or otherwise clearly frivolous petitions for the opening of Insolvency Proceedings, the following wording may be added to

[150] With respect to credit institutions, financial services institutions or insurance companies, parties may agree upon an Automatic Termination which is triggered on measures taken by the BaFin or any relevant other supervisory authority according to section 46 of the Banking Act or section 314 of the Insurance Supervisory Act if parties are of the view that such measures (in particular the imposition of a ban on payments under section 46 para 1 sent. 2 no. 4 of the Banking Act or section 314 para 1 of the Insurance Supervisory Act) may in fact create a risk to netting (taking into account that such measures are taken to stabilise the financial situation of the credit institution or financial services institution (sections 46d para 3 of the Banking Act)) In the legislative reasoning to the version of section 104 of the Insolvency Code currently in force reference was made to termination events triggered by the institution of a moratorium by a regulatory authority, see BT-Drs. 18/9983, p. 15.

Section 10.4 of the General Agreement: "*In situations described in Section 10.5 (c) (iv) of the General Agreement Automatic Termination shall be limited to situations where either this Party itself or where applicable the relevant supervisory authority has presented the petition, or such Party is insolvent or otherwise in a situation which justifies the opening of such proceedings.*" Alternatively, the following wording may be added to the definition of Section 10.5 (c) (iv) of the General Agreement: "*and either this Party itself or where applicable the relevant supervisory authority has presented the petition, or such Party is insolvent or otherwise in a situation which justifies the opening of such proceedings.*"

However, the restrictions on insolvency related termination provisions as set out in Paragraph 5.1.1(i)(ii) above would equally apply to an automatic termination, not only where a termination is exercised by notice.

(m) *If you are recommending that a grace period be made applicable in respect of Section 10.5(c)(iv) of the General Agreement, what, in your best estimation is the minimum reasonable period of time required by a party whose creditor(s) have instituted unsubstantiated or otherwise clearly frivolous involuntary bankruptcy proceedings against it in the insolvency courts of your jurisdiction to have these proceedings dismissed or otherwise terminated?*

We recommend not to provide for a grace period such as provided in Section 10.5 (c) (iv) of the General Agreement, because in such case, a termination (either on the basis of a contractual termination right or by way of Automatic Termination) could only become effective after the opening of insolvency proceedings and therefore, not the contractual provisions agreed under the General Agreement, but rather the German mandatory insolvency provisions (where applicable) would apply (please see Paragraph 5.1.1(i)(ii) above).

(n) *If you are recommending that Automatic Termination be made applicable in respect of parties subject to the insolvency laws of your jurisdiction, what is the optimal timing for that Automatic Termination to take effect? In this event, please supply specific recommended language for purposes of customizing Section 10.4 of the General Agreement to implement such optimal termination timing.*

As set out in Paragraph 5.1.1(l) above, the Automatic Termination should take effect at the time an application has been filed for the commencement of Insolvency Proceedings or other bankruptcy proceedings against the assets of a Party and this Party has either filed the application itself or is insolvent or otherwise in a situation which justifies the opening of such proceedings.

(o) *Are the provisions in Section 11 of the General Agreement providing for the netting of all positive and negative Settlement Amounts in determining the Termination Amount enforceable under the laws of Germany or is there a risk that such determination could be challenged by a liquidator, administrator, receiver or third party?*

With respect to the application of German law to the calculation of the Termination Amount for all Individual Contracts, we refer to Paragraph 5.1.1(i)(ii) above.

(i) *Enforceability of close-out netting*

German law recognises close-out netting in principle. Parties may specify certain events in an agreement upon the occurrence of which payments under such agreement become immediately due. Furthermore, under German statutory law, set-off (*Aufrechnung*) is understood as the mutual discharge of two corresponding obligations of the same nature. The rules relating to set off are contained in sections 387 *et seq.* of the German Civil Code. According to this provision, a party that demands payment – or of whom payment is demanded – is entitled to unilaterally declare that the debt is extinguished by a set-off provided that the legally defined set-off requirements are met (see Paragraph 5.1.1(g) above).

However, in case of the insolvency of a Party, the enforceability of contractual close-out netting depends on whether there is a statutory exemption from section 103 of the Insolvency Code, which qualifies as a "corresponding" statutory termination right as referred to in the judgements of the BGH of 15 November 2012 and of 9 June 2016[151] (please refer to Paragraph 5.1.1(i)(ii)(A) above). Even in such case, the enforceability of contractual close-out netting also depends on the point in time when the outstanding transactions are terminated. Even with respect to Individual Contracts falling within the scope of section 104 of the Insolvency Code (please refer to Paragraph 5.1.1(i)(ii) above), contractual close-out netting provisions are enforceable if the outstanding Individual Contracts are terminated and set off prior to the opening of Insolvency Proceedings. In contrast, the statutory close-out netting regime applies if termination of the outstanding Individual Contracts takes place at or after the opening of Insolvency Proceedings.

151 BGH WM 2013, 274; BGH WM 2016, 1168.

In Germany, the contractual provision of automatic aggregation and set-off of all existing mutual payment obligations of the Parties under the General Agreement, including payment obligations not yet due and payable at this time, upon occurrence of a Material Reason would be recognised if there is such "corresponding" statutory termination right and if such set-off was effected prior to the opening of Insolvency Proceedings even if Insolvency Proceedings are finally commenced against the assets of one of the Parties. Therefore, if an insolvency related Material Reason in relation to a Party occurred, which resulted in aggregation and set off according to the Netting Provisions, this would result in a single obligation equalling the balance of all of the mutual payment claims of the Parties.

The right of a Solvent Party to effect set-off after the opening of Insolvency Proceedings is governed by sections 94 through 96 of the Insolvency Code. The extent to which a set-off after the opening of Insolvency Proceedings is permissible mainly depends on the point in time when the situation entitling one party to the set-off comes into existence (*Entstehung der Aufrechnungslage*). This point in time is determined by German substantive civil law.

(A) Existence of a situation giving one party the right to set off at the time of the opening of Insolvency Proceedings

Pursuant to section 94 of the Insolvency Code and subject to the restrictions and prohibitions of set-off pursuant to sections 95 and 96 of the Insolvency Code, a right to set off a claim is preserved after the opening of Insolvency Proceedings if by force of law or on the basis of an agreement the Solvent Party was already entitled to set off the claim at the time the Insolvency Proceedings were opened irrespective of whether or not the declaration to set off the claim was made before or after the opening of such Insolvency Proceedings.

In contrast to the former German Bankruptcy Code (*Konkursordnung*), the Insolvency Code explicitly preserves rights to set off a claim under valid contractual agreements. With respect to the overall intention of the Insolvency Code in general and the purpose of section 94 of the Insolvency Code in particular, *i.e.* the aim to protect the legitimate expectations of the creditors of the Insolvent Party, the preservation of contractual rights to set off is criticised[152] since it enables the parties to extend the rights to set off to the detriment of creditors of the Insolvent Party as such agreements might reduce the assets available to (other) creditors in insolvency. Hence, the validity of contractual agreements concerning set-off is called into question by some legal authors[153] that advocate a restrictive interpretation of section 94 of the Insolvency Code according to which agreements concerning set-off may not override prohibitions of set-off that aim at protecting third parties' rights. According to these legal authors, such agreements also have to comply with sections 95 and 96 of the Insolvency Code and might be challenged pursuant to sections 129 *et seq*. of the Insolvency Code.

However, this restrictive approach particularly applies to agreements deviating from the requirement of mutuality of the claims[154] and should not affect the validity of the contractual provision of automatic aggregation and set-off of all existing mutual payment obligations of the Parties under the transactions where the relevant contractual provisions do not contain a contractual deviation from the requirement of mutuality of the claims.

(B) Statutory deviation from the requirement of similarity of the claims

Pursuant to section 95 para 2 of the Insolvency Code,[155] set-off is not excluded by claims being expressed in different currencies or mathematical units if these currencies or mathematical units are freely exchangeable at the place of payment of the claim against which the set-off is to be effected.[156] The claims have to be converted according to the exchange value

[152] *Kroth* in: Braun, Insolvenzordnung, 7th ed. (2017), § 95 no. 24. *Sinz* in: Uhlenbruck, InsO, 14th ed. (2015), § 94 nos. 8 et seq.

[153] Ibid.

[154] *Schwahn,* NJW 2005, 473, 475.

[155] This provision is generally understood to regulate a question of principle of German insolvency law and, hence, applies to both section 94 of the Insolvency Code and section 95 of the Insolvency Code (*Höhn/Kaufmann,* JuS 2003, 751, 753).

[156] However, absent any specific agreements between the parties, claims in different currencies are not of similar type and can, thus, not be set-off against each other in accordance with sections 387 of the German Civil Code (KG NJW 1988, 2181).

applicable to this place at the time of receipt of the declaration to set-off.

(C) Set-off with voidable claims

In the event an insolvency creditor acquired the right to set off its claim by a transaction which may be challenged as void, set-off is prohibited pursuant to section 96 para 1 no. 3 of the Insolvency Code. This prohibition applies irrespective of whether or not the Insolvency Administrator actually challenged the transaction.

(D) Emergence of a situation giving one party the right to set off after the opening of Insolvency Proceedings

In circumstances where the right to set off emerges after the opening of Insolvency Proceedings, set-off is only permissible if the mutual claims originated before the opening of Insolvency Proceedings. If on the date when Insolvency Proceedings are opened one or more of the claims to be set off against each other are conditional, not yet due or do not cover similar types of obligations, such set-off is not effected before such conditions are met (section 95 para 1 sent. 1 of the Insolvency Code). Pursuant to section 95 para 1 sent. 2 of the Insolvency Code, section 41 of the Insolvency Code concerning claims not yet due at the date when Insolvency Proceedings are opened and section 45 of the Insolvency Code concerning the conversion of certain claims do not apply.

(E) Statutory limitation of set-off

Set-off is excluded if the claim against which a set-off is to be effected becomes unconditional and matures before it can be set-off (section 95 para 1 sent. 3 of the Insolvency Code). With respect to set-off after the opening of Insolvency Proceedings, timing, therefore, is of fundamental importance. Set-off is permissible if the Solvent Party's claim is unconditional and matures prior to the Insolvent Party's claim or at the same time at the latest. Provided that the contractual close-out netting provision is structured in a way that ensures that claims arising thereunder come into existence at the same time, the statutory limitation pursuant to section 95 para 1 sent. 3 of the Insolvency Code would not apply.[157]

(F) Prohibition of set-off

Set-off is statutorily prohibited if (i) a creditor in the Insolvency Proceedings has become a debtor of the insolvency estate only after the opening of Insolvency Proceedings, (ii) a creditor in the Insolvency Proceedings acquired its claim from another creditor only after the opening of Insolvency Proceedings,[158] (iii) a creditor in the Insolvency Proceedings acquired the opportunity to set off its claim by a legal act subject to challenge[159] or (iv) a creditor with a claim to be satisfied from the debtor's free property is a debtor of the insolvency estate (section 96 para 1 of the Insolvency Code).

(G) Exceptions for Systems and the transfer of Financial Collateral

The prohibitions of set-off pursuant to section 95 para 1 sent. 3 of the Insolvency Code and section 96 para 1 of the Insolvency Code do neither apply to the transfer of Financial Collateral nor to the set-off of claims and benefits from transfer, payment or settlement agreements introduced into a System where set-off is effected at the latest on the day of opening of the Insolvency Proceedings.

The term System is defined in section 1 para 16 sent. 1 of the Banking Act pursuant to which a system within the meaning of section 24b of the Banking Act is a written agreement within the meaning of Article 2 lit (a) of the Settlement Finality Directive, including an

[157] Moreover, section 95 para 1 sent. 3 of the Insolvency Code has been interpreted restrictively by the BGH (BGH NJW 2005, 3574, 3575 *et seq.*). According to the BGH, section 95 para 1 sent. 3 of the Insolvency Code does not apply if the Insolvent Party's claim, against which set-off is declared, has become mature and unconditional before the Solvent Party's claim but at the same time was not enforceable due to a right to refuse performance by the Solvent Party against such claim.

[158] Accordingly, set-off would be generally permissible if a creditor in the Insolvency Proceedings acquired its claim from another creditor prior to the opening of Insolvency Proceedings. However, depending on the circumstances of the case, such acquisition of a claim prior to Insolvency Proceedings could itself be subject to challenge with the consequence that section 96 para 1 no. 3 of the Insolvency Code applied, i.e. the set-off were invalid (without the need to separately challenge it) as the claim were acquired by a legal act subject to challenge.

[159] This prohibition applies irrespective of whether or not the Insolvency Administrator actually challenged the Individual Contract (*Höhn/Kaufmann*, JuS 2003, 751, 753).

agreement between a participant and an indirectly participating Credit Institution which has been notified by Deutsche Bundesbank or a competent authority of a member state of the EEA to the European Securities and Markets Authority. Systems from third countries are treated similar as the systems referred to in the previous sentence if they largely correspond with the requirements enumerated in Article 2 lit (a) of the Settlement Finality Directive.

(ii) *Challenging the determination of the Termination Amount*

In order to be challenged by the Insolvency Administrator under sections 129 *et seqq.* of the Insolvency Code, the determination of the Termination Amount would have to be qualified as legal act (see also under Paragraph 5.1.1(c)).

The agreement on the automatic occurrence of the set-off is contractually agreed between the Parties at the time of entering into the General Agreement. Therefore, it may be argued that the determination of the Termination Amount merely constitutes a factual determination of an existing claim arising out of a set-off and could, thus, not be challenged separately. Accordingly, the Insolvency Administrator could merely deny the amount of the claim determined by the Solvent Party in accordance with section 176 of the Insolvency Code. However, as the determination of the Termination Amounts stipulates to what extent claims of either party have extinguished by way of set-off (*Tilgungswirkung der Aufrechnung*), one cannot fully exclude that such determination would be considered a legal act itself by an Insolvency Administrator and that an insolvency court will follow such view.

(p) *Do the laws of Germany recognise that the close-out netting provisions in Sections 10 and 11 of the General Agreement apply to all Individual Contracts? Would we need the single agreement concept in order to preserve the enforceability of the termination right and the ability to calculate a net amount? If the single agreement concept is particularly important in your jurisdiction, please give us your opinion on whether or not, and if so, the degree to which, provisions allowing or providing for the termination of some Individual Contracts but not all Individual Contracts under the General Agreement might impact termination and close out rights generally, as well as subsequent rights to terminate Individual Contracts remaining under the General Agreement following a previous Partial Close-Out.*

Regarding the applicability of German law to Sections 10 and 11 of the General Agreement, please refer to Paragraph 5.1.1(i)(i).

Assuming that the General Agreement and the Individual Contracts are subject to German substantial insolvency law, in particular sections 103 *et seqq.* of the Insolvency Code,[160] where a Material Reason has occurred in relation to a Party and the date of early termination falls before the opening of the Insolvency Proceedings or the point in time the BGH has considered decisive in its decision dated 15 November 2012,[161] by referring to the point in time when, based on a valid application for the opening of Insolvency Proceedings, such opening of Insolvency Proceedings is to be seriously expected (*mit der Eröffnung eines Insolvenzverfahrens ernsthaft zu rechnen ist*), the Parties may determine which Individual Contracts are subject to the Close-Out irrespective of whether or not the Parties have agreed to apply the single agreement concept as set forth in Section 1.1 of the General Agreement.

The early termination and, if applicable, close-out netting of some Individual Contracts would in our view not prevent the later termination of the General Agreement and the termination and close-out netting of the remaining Individual Contracts pursuant to mandatory insolvency laws.

(q) *Is the insolvent counterparty's obligation to pay the amount of any compensation claim in Euro, USD or GBP (as agreed between the parties in the Election Sheet) enforceable under the laws of Germany or could the calculation or demand of such amount in a foreign currency be challenged by a liquidator, administrator, receiver or third party?*

After the opening of Insolvency Proceedings, cash payment claims against an Insolvent Party in a currency other than Euro must be converted into Euro at an exchange rate applicable at the place of performance at the time of the opening of the Insolvency Proceedings (section 45 of the Insolvency Code).

According to the BGH, the official exchange rate applicable on the date of the opening of Insolvency Proceedings at the place of payment applies whereby the place of payment is the place where the Insolvency Proceedings have been opened.[162] With respect to enforcement proceedings, however, it is proposed that cash payment

[160] Whether or not substantial German insolvency laws are applicable in this context depends on the relevant conflict of law provisions, see in more detail in Paragraph 5.2.1.

[161] BGH WM 2013, 274, confirmed by BGH WM 2016, 1168.

[162] BGH NJW 1989, 3155 (on the KO); *Andres*, in: Nerlich/Römermann, Insolvenzordnung, 30th update (2016), § 45 no. 4; see, however, *Bitter*, in: Münchener Kommentar zur InsO, 3rd ed. (2013), § 45 no. 20.

claims in a currency other than Euro are converted at the official conversion rate on the date and at the place of payment.[163]

(r) *Please specify, if and as applicable, the degree to which termination and close-out rights in insolvency in your jurisdiction are dependent upon, or otherwise effected by, the status of one or more of the concerned parties falling within a particular category of classification of entity. Specifically, do these rights differ as the result of a party being a financial institution, ordinary corporate entity or any other categorization or regulatory or legal status?*

With respect to close-out netting, the Insolvency Code does generally not distinguish between different types of counterparties.

However, specific restrictions may apply to different types of counterparties under corporate and regulatory laws.

For example, pursuant to section 93 para 5 sent. 1 of the Capital Investment Code, claims against an investment management company and claims belonging to the separate assets (*Sondervermögen*, as defined in section 1 para 10 of the Capital Investment Code), cannot be set off against each other. However, pursuant to section 93 para 5 sent. 2 of the Capital Investment Code, this would not prohibit a set-off of claims under a master agreement as set out in Paragraph 5.1.1 (g)(ii)(B) above.

With respect to insurance companies, section 130 para 2 sent. 2 of the Insurance Supervisory Act limits the possibility of set-off against claims belonging to the "cover assets" *(Sicherungsvermögen)* of an Insurance Company.

5.1.2 Non-insolvency related Material Reasons

(a) *Please discuss and advise on the issues outlined above under 5.1.1(o), 5.1.1(p) and 5.1.1(q) in the context of non-insolvency related Material Reasons.*

Section 10.5 of the General Agreement provides for several Material Reasons which are not directly related to the insolvency of a Party. Such non-insolvency related Material Reasons are: Non Performance, Cross Default and Acceleration, Failure to Deliver or Accept, *Force Majeure* and breach of a Representation and Warranty.

With respect to the termination of the General Agreement due to such non-insolvency related Material Reasons, our opinion on the enforceability of Section 11 of the General Agreement set out under

163 *Bach*, in: Beck'scher Onlinekommentar ZPO, 23rd ed. (1 December 2016), § 722 no. 27.

Paragraph 5.1.1(o) above and Paragraph 5.1.1(p) above, as well as on the counterparty's obligation to pay the amount of any compensation claim in Euro, USD or GBP, as set out under Paragraph 5.1.1(q) also applies in the context of non-insolvency related Material Reasons.

(b) *Are the rights of the Terminating Party to terminate and close-out the General Agreement enforceable in accordance with the terms of the General Agreement, irrespective of the insolvency of Party A?*

Please refer to Paragraph 5.1.1(i) above.

5.2 Multibranch Parties

5.2.1 Overview of German International Insolvency Law

Whether or not German insolvency courts have jurisdiction for opening Insolvency Proceedings over the assets of a Party depends on the rules governing the relevant proceedings. The international scope of application of Insolvency Proceedings and any Provisional Insolvency Proceedings are governed by the EU Insolvency Regulation (or the Recast EU Insolvency Regulation, as applicable), Article 102 of the German Introductory Act to the Insolvency Code (*Einführungsgesetz zur Insolvenzordnung*), sections 3, 335 *et seqq.* of the Insolvency Code and sections 46d to 46f of the Banking Act.

(a) Scope of application of the EU Insolvency Regulation and the Recast EU Insolvency Regulation

The EU Insolvency Regulation and the Recast EU Insolvency Regulation apply to insolvency proceedings as specified in Article 1 para 1, Annex A of the EU Insolvency Regulation and of the Recast EU Insolvency Regulation. The EU Insolvency Regulation and the Recast EU Insolvency Regulation are not applicable, *inter alia*, to insolvency proceedings concerning insurance companies, credit institutions [164], investment undertakings/firms and other firms, institutions and undertakings to the extent that they are covered by the Winding-Up Directive [165] and collective investment undertakings [166] (Article 1 para 2 of the EU Insolvency Regulation and the Recast EU Insolvency Regulation).

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[164] In our view Article 1 para 2 of the EU Insolvency Regulation and of the Recast EU Insolvency Regulation refer to CRR Credit Institutions; see also footnotes 7 and 8 and *Nerlich* in: Nerlich/Römermann, InsO, (as of July 2016), Art. 1 EUInsVO no. 10; *Kindler* in: Münchener Kommentar BGB, 6th ed. (2015), Article 1 EUInsVO no. 15).

[165] Regarding the definitions of "investment undertaking" and "investment firms", please refer to footnote 11. The express reference to the Winding-Up Directive was introduced in the Recast EU Insolvency Regulation.

[166] Regarding the definition of "collective investment undertaking", please refer to footnote 12; see also *Virgós/Schmit*, Report on the Convention on Insolvency Proceedings, no. 56 et seq. and Article 2 no 2 of the Recast EU Insolvency Regulation.

The European Court of Justice ("**ECJ**") takes the view that the application of provisions of the EU Insolvency Regulation and the Recast EU Insolvency Regulation does not generally depend on the existence of a cross-border link (*grenzüberschreitender Bezug*) to another EU member state (other than Denmark) unless a relevant provision of the EU Insolvency Regulation and Recast EU Insolvency Regulation expressly requires such link.[167]

Within this scope of application, the courts of the EU member states (other than Denmark)[168] where the "centre of main interests" of a debtor is situated may open main insolvency proceedings (as specified in Annex A of the EU Insolvency Regulation and the Recast EU Insolvency Regulation). In case of a legal entity, the place of the registered office is deemed to be the centre of its main interests in the absence of proof to the contrary (Article 3 para 1 of the EU Insolvency Regulation and the Recast EU Insolvency Regulation). These proceedings are generally governed by the law of the EU member state where such proceedings are opened. They are, with regard to other EU member states, international in scope being effective in all EU member states unless secondary proceedings are opened in another EU member state. The only main insolvency proceedings permitted under Annex A of the EU Insolvency Regulation and the Recast Insolvency Regulation under the laws of Germany would be Insolvency Proceedings.

If the "centre of main interests" of a debtor is in an EU member state (other than Denmark), under Article 3 para 2 of the EU Insolvency Regulation and the Recast EU Insolvency Regulation, the courts of another EU member state (other than Denmark) may open "territorial proceedings" or, after the opening of main proceedings, "secondary proceedings" in the event that such debtor possesses an "establishment" within the territory of such other EU member state. The applicable law of such territorial or secondary insolvency proceedings is the law of that other EU member state. However, territorial or secondary insolvency proceedings are limited in scope to the debtor's assets located in that EU member state and will, thus, not extend beyond the EU member state where they are opened. Furthermore, under Article 3 para 3 of the EU Insolvency Regulation and the Recast EU Insolvency Regulation, secondary proceedings are limited to winding-up proceedings.

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167 ECJ NJW 2014, 610, 611 *et seq*. Several legal commentators have taken the view that the application of the EU Insolvency Regulation does not generally require a cross-border link. See *Kindler*, in : Münchener Kommentar BGB, 6th ed. (2015) , Article 1 EUInsVO no. 23; *Virgos/Schmit*, Report on the Convention on Insolvency Proceedings, no. 11. See also the overview given by *Reinhart*, in: Münchener Kommentar InsO, 3rd ed. (2016), Art 1 EUInsVO nos. 15 *et seq*.

168 As regards Denmark, the autonomous German international insolvency law provisions pursuant to sections 335 *et seq.* of the Insolvency Code apply.

As a result of the implementation of the Winding-Up Directive, the opening of secondary or territorial insolvency proceedings is excluded in respect of CRR Institutions (section 46e para 2 of the Banking Act). Insolvency Proceedings may only be opened by the competent authorities of the home state (*Herkunftsmitgliedsstaat*) of such CRR Institution.

(b) Jurisdiction of German insolvency courts within the scope of application of the EU Insolvency Regulation and the Recast EU Insolvency Regulation

As to the jurisdiction of German insolvency courts within the scope of application of the EU Insolvency Regulation and the Recast EU Insolvency Regulation the following distinctions have to be made:

(i) The centre of main interests of the Insolvent Party is in Germany

If the centre of main interests of the Insolvent Party is in Germany, Insolvency Proceedings are instituted in Germany with respect to the Insolvent Party irrespective of whether or not the relevant authorities in any other jurisdiction have initiated proceedings in respect of a branch office or any other assets of the Insolvent Party in such jurisdiction. An Insolvency Administrator appointed in Germany in relation to an Insolvent Party would include transactions (regardless of the branch from which they were entered into) in the calculation of amounts owed to and from the Insolvent Party and would recognise the Netting Provisions, subject to sections 103 and 104 of the Insolvency Code (see Paragraph 5.1.1(i)(ii) above).

(ii) The centre of main interests of the Insolvent Party is in an EU member state other than Germany or Denmark and the Insolvent Party has an establishment in Germany

Where the centre of main interests of the Insolvent Party is in an EU member state other than Germany or Denmark and the Insolvent Party has an establishment (within the meaning of the EU Insolvency Regulation and the Recast EU Insolvency Regulation) in Germany, the German insolvency courts have jurisdiction in respect of such assets of the Insolvent Party which are situated in Germany. An establishment is defined as any place of operations where the debtor carries out a non transitory economic activity with human means and goods (such term including branch offices) (Article 2 (h) of the EU Insolvency Regulation). Pursuant to Article 2 para 10 of the Recast EU Insolvency Regulation establishment means any place of operations where a debtor carries out or has carried out in the 3 month period prior to the request to open main insolvency proceedings a non-transitory economic activity with human means and assets.

(iii) The centre of main interests of the Insolvent Party is in an EU member state other than Germany or Denmark and the Insolvent Party has no establishment in Germany

Where the centre of main interests of the Insolvent Party is in an EU member state other than Germany or Denmark and the Insolvent Party has no establishment (within the meaning of the EU Insolvency Regulation or the Recast EU Insolvency Regulation) in Germany, the German insolvency courts will have no jurisdiction in respect of such Insolvent Party.

(iv) Situation of payment claims

Payment claims are deemed to be situated in the country in which the debtor of such claim has the centre of its main interests (Article 2 (g) of the EU Insolvency Regulation and Article 2 para 9 item (viii) of the Recast EU Insolvency Regulation). Therefore, if the centre of main interests of the Solvent Party is in another EU member state (other than Denmark), and there are secondary proceedings under the EU Insolvency Regulation in respect of the Insolvent Party in that EU member state, then the claims of such Insolvent Party against the Solvent Party would be deemed under the EU Insolvency Regulation to be situated outside of Germany. The Insolvency Administrator would be required to defer to the jurisdiction of the Insolvency Administrator appointed in such other EU member state in relation to such claims (to the extent they have not been extinguished at the time of opening of Insolvency Proceedings).

(c) Jurisdiction of German insolvency courts outside the scope of application of the EU Insolvency Regulation and the Recast EU Insolvency Regulation

As to the jurisdiction of German insolvency courts outside the scope of application of the EU Insolvency Regulation and the Recast EU Insolvency Regulation the following distinctions have to be made:

(i) The Insolvent Party is not a CRR Institution or a European insurance company

In case the Insolvent Party is not a CRR Institution or a European insurance company having its place of general jurisdiction in Germany, Insolvency Proceedings are opened in

Germany with respect to the Insolvent Party irrespective of whether or not the relevant authorities in any other jurisdiction have initiated proceedings in respect of a branch of the Insolvent Party in such jurisdiction. In case of a legal entity, the place of general jurisdiction is the registered seat. If the centre of that legal entity's independent business activity is located elsewhere (e.g. if the management is located at a place different to the registered seat) such place determines the competent insolvency court (section 3 of the Insolvency Code). Therefore, if the centre of an independent business activity of the Insolvent Party is located outside Germany, the German insolvency courts have no jurisdiction except for the opening of (separate) insolvency proceedings (which are limited in scope to the assets of the Insolvent Party situated in Germany).

(ii) The Insolvent Party is a CRR Institution or a European insurance company

In case the Insolvent Party is a CRR Institution or a European insurance company, the opening of secondary or territorial insolvency proceedings is excluded (section 46e of the Banking Act, section 312 para 3 of the Insurance Supervisory Act). Insolvency Proceedings may be opened in Germany only if Germany is considered to be the home member state, which is the case if the main office (*Hauptniederlassung*) is located in Germany (section 1 para 4 of the Banking Act (which implements Article 2 of the Winding-Up Directive in connection with Article 4 para 1 no. 43 of the CRR); section 10 para 1 of the Insurance Supervisory Act (which implements Article 1 sent. 1 lit (c) and Article 6 sent. 2 of Council Directive 92/49/EEC of 18 June 1992 on the coordination of laws, regulations and administrative provisions relating to direct insurance other than life assurance (third non-life insurance Directive) and Article 1 lit (e) and Article 4 of the Directive 2002/83/EC of the European Parliament and of the Council of 5 November 2002 concerning life assurance).[169]

(iii) Secondary or territorial insolvency proceedings

Secondary or territorial insolvency proceedings can be commenced in Germany under section 354 para 1 of the Insolvency Code if the debtor has an establishment in Germany

[169] Directives 92/49/EEC and 2002/83/EC were repealed with effect from 1 January 2016 by 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) ("**Solvency II**"). References to the repealed Directives shall be construed as references to Solvency II in accordance with Article 310 of Solvency II.

(with respect to the exception for CRR Institutions see the preceding Paragraph 5.2.1(c)(ii)). Where the Insolvent Party has no establishment in Germany, a sufficient basis for separate proceedings in Germany under the Insolvency Code is also provided in respect of assets located or deemed to be located in Germany upon request of a creditor, if such creditor provides evidence for its "special interest" in the opening of German territorial proceedings due to the fact that it would have worse prospects (*erheblich schlechter stehen*) for the settlement of its debt in the non-German proceedings (section 354 para 2 of the Insolvency Code).[170]

If territorial or secondary insolvency proceedings are opened in Germany, they take precedence over the non-German insolvency proceedings in relation to those assets of the Insolvent Party which are situated in Germany. Such territorial or secondary insolvency proceedings and, thus, the applicability of the German insolvency law rules set out above are, however, limited in scope to the debtor's assets in Germany.

(iv) Situation of payment claims

Payment obligations are assets deemed to be located in Germany if they are payable by the debtor out of Germany to the Insolvent Party. Therefore, only payment obligations which are payable by the Solvent Party out of Germany are assets deemed to be located in Germany and could provide a sufficient basis for separate Insolvency Proceedings in relation to such Insolvent Party.

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[170] See also *Wenner*, in: Mohrbutter/Ringstmeier, Handbuch der Insolvenzverwaltung, 9th ed. (2015), § 20 nos. 69 et seqq., 129; *Dahl*, in: Andres/Leithaus/Dahl, Insolvenzordnung, 3rd ed. (2014), § 354 no. 9.

(d) Netting under German international insolvency law

As to the netting under German international insolvency law the following distinctions have to be made:

(i) With respect to netting under German international insolvency law within the scope of the EU Insolvency Regulation the following applies:

(A) Scope of the *lex fori concursus* rule (Article 4 of the EU Insolvency Regulation and Article 7 of the Recast EU Insolvency Regulation)

When applicable, Article 4 of the EU Insolvency Regulation and Article 7 of the Recast EU Insolvency Regulation provide that the law applicable to insolvency proceedings and their effects are the law of the EU member state in which the proceedings are opened. Insolvency proceedings are opened in the jurisdiction where the centre of main interests of the Insolvent Party is located except where there is another, more specific, provision within the EU Insolvency Regulation or the Recast EU Insolvency Regulation itself – subject to any secondary proceedings. Secondary proceedings are governed by the law of the EU member state (other than Denmark) in which they are opened (Articles 3 para 2, 28 of the EU Insolvency Regulation or Articles 3 para 2, 35 of the Recast EU Insolvency Regulation).

Cases where rights may be immunised from the effects of insolvency law are, for example, "rights *in rem*" over assets outside the jurisdiction where the insolvency proceedings are conducted (Article 5 of the EU Insolvency Regulation or Article 8 of the Recast EU Insolvency Regulation) and rights of set-off permitted by the law applicable to the insolvent debtor's claim (Article 6 of the EU Insolvency Regulation or Article 9 of the Recast EU Insolvency Regulation). Insolvency law is subordinated to some other system of law where the rules of payment or settlement systems and financial markets (Article 9 of the EU Insolvency Regulation or Article 12 of the Recast EU Insolvency Regulation) apply.

(B) Conflict of law rule regarding insolvency set-off

Under the EU Insolvency Regulation and the Recast EU Insolvency Regulation set-off is permitted in each of the two following situations:

(1) if it is permitted under the insolvency[171] laws of the jurisdiction in which insolvency proceedings have been opened in relation to the insolvent debtor (Article 4 para 2 lit (d) of the EU Insolvency Regulation or Article 7 para 2 lit (d) of the Recast EU Insolvency Regulation) or

(2) if it is permitted by the law applicable to the insolvent debtor's claim (Article 6 para 1 of the EU Insolvency Regulation or Article 9 para 1 of the Recast EU Insolvency Regulation).

Article 6 para 1 of the EU Insolvency Regulation or Article 9 para 1 of the Recast EU Insolvency Regulation establish an insolvency conflict of law rule regarding insolvency set-off as an exception to the *lex fori concursus* rule as set forth by Article 4 para 1 of the EU Insolvency Regulation or Article 7 para 1 of the Recast EU Insolvency Regulation. In relation to (1), the laws of Germany would be applicable in the case of Insolvency Proceedings being opened by a court in Germany. In relation to the situation mentioned under (2), set-off will be allowed if it is permitted under the laws[172] governing the General Agreement and relevant Individual Contracts.

[171] According to many legal commentators in Germany (*Reinhart* in: Münchener Kommentar zur InsO 3rd ed. (2016), Article 4 EuInsVO no. 3; *Haß/Herweg* in: Haß *et al.*, EU-Insolvenzverordnung (2005), Article 4 no. 32; the EU Insolvency Regulation only concerns set-off restrictions that stem from the insolvency law of the jurisdiction in which insolvency proceedings have been opened. The scope of the *lex fori concursus* thus would be limited to such laws. The general legal requirements relating to set-off (e.g. in Germany sections 387 *et seq.* of the German Civil Code), however, are determined according to the usual conflict of law rules (e.g. the Rome I Regulation with respect to contracts entered into after 17 December 2009 or Article 32 para 1 no. 4 of the Introductory Code to the German Civil Code regarding claims having come into existence prior to such date, which are applicable as if there were no insolvency proceedings).

[172] This includes insolvency law, e.g. in Germany sections 94 *et seq.* of the Insolvency Code (see Paragraph 5.1.1(o)(i)) (*Kindler* in: Münchener Kommentar zum BGB, 6th ed. (2015), InsO § 340 no. 8, *Gruber* in: Haß *et al.*, EU-Insolvenzverordnung (2005), Article 6 no. 9; *Reinhart* in: Münchener Kommentar zur InsO, 3rd ed. (2016), Article 6 EuInsVO no. 9).

In our view, close-out netting arrangements do not fall within the scope of application of Article 6 para 1 of the EU Insolvency Regulation and Article 9 para 1 of the Recast EU Insolvency Regulation. The wording of Article 6 para 1 of the EU Insolvency Regulation and Article 9 para 1 of the Recast EU Insolvency Regulation supports this as the term "set-off" only covers one element of close-out netting but does not refer to other integral parts such as the early (closing-out) termination of transactions or the valuation and conversion of the terminated transactions into claims which are eligible for set-off.

While it has been argued that Article 6 para 1 of the EU Insolvency Regulation should be construed broadly to include close-out netting arrangements to enable financial market participants to choose the insolvency law applicable to close-out netting,[173] Recital 27 of the EU Insolvency Regulation and Recital 71 of the Recast EU Insolvency Regulation in connection with Article 9 of the EU Insolvency Regulation and Article 12 of the Recast EU Insolvency Regulation clarify that the European legislator distinguishes between set-off and netting agreements and that the later shall only be exempted from the *lex fori concursus* rule of Article 4 para 1 of the EU Insolvency Regulation and Article 7 para 1 of the Recast EU Insolvency Regulation if agreed in the context of a payment or securities settlement system. Moreover, the European legislator uses the terms set-off and netting agreements differently in other relevant European legal acts as well.[174] Therefore, we take the view that Article 6 para 1 of the EU Insolvency Regulation and Article 9 para 1 of the Recast

[173] See European Financial Markets Lawyers Group, Protection for Bilateral Insolvency Set-off and Netting Agreements under EC Law, A report by the European Financial Market Lawyers Group (EFMLG), October 2004, nos. 72 *et seq*.

[174] See also the proposal of the European Commission dated 12 December 2012 (COM(2012) 744 final), which intended to add Article 6a covering "netting arrangements". However, Article 6a has not been included in the final version of the Recast EU Insolvency Regulation.

EU Insolvency Regulation do not refer to close-out netting arrangements.

(C) Effects of Articles 6 para 2 and 4 para 2 lit (m) of the EU Insolvency Regulation and Article 9 para 2 of the Recast EU Insolvency Regulation

Pursuant to Article 4 para 2 lit (m) of the EU Insolvency Regulation and Article 7 para 2 lit (m) of the Recast EU Insolvency Regulation, the law of the member state opening the insolvency proceedings (*lex fori concursus*) determines the rules relating to the voidness, voidability or unenforceability of legal acts which are detrimental to all creditors. Article 6 para 2 of the EU Insolvency Regulation and Article 9 para 2 of the Recast EU Insolvency Regulation provide that the protection for set-off pursuant to Article 6 para 1 of the EU Insolvency Regulation and Article 9 para 1 of the Recast EU Insolvency Regulation do not preclude actions for voidness, voidability or unenforceability as referred to in Article 4 para 2 lit (m) of the EU Insolvency Regulation or Article 7 para 2 lit (m) of the Recast EU Insolvency Regulation. Consequently, Article 6 para 2 of the EU Insolvency Regulation and Article 9 para 2 of the Recast EU Insolvency Regulation preserve the ability of the *lex fori concursus* to declare the provision void despite the protection in Article 6 para 1 of the EU Insolvency Regulation and Article 9 para 2 of the Recast EU Insolvency Regulation.[175]

(D) Article 13 of the EU Insolvency Regulation and Article 16 of the Recast EU Insolvency Regulation

Pursuant to Article 13 of the EU Insolvency Regulation and Article 16 of the Recast EU Insolvency Regulation, the rules relating to voidness, voidability or unenforceability of the EU member state in which the proceedings have been opened would 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 an EU member state other than that of the EU member state of the opening of proceedings,

[175] Contrary to the explicit wording of Article 6 para 2 of the EU Insolvency Regulation, it is, however, argued that the set-off of claims has absolute protection under Article 6 para 1 of the EU Insolvency Regulation even where the agreement creating the right to set off was itself vulnerable as a preference (see European Financial Markets Lawyers Group, Protection for Bilateral Insolvency Set-off and Netting Agreements under EC Law, October 2004, pages 27 *et seq.* (nos. 84 *et seq.*)).

and (ii) that such law does not allow any means of challenging that act in the relevant case.

(ii) With respect to netting under German international insolvency law outside the scope of the EU Insolvency Regulation and Recast EU Insolvency Regulation the following applies:

(A) Principles of German international insolvency law

Under German international insolvency laws, section 335 of the Insolvency Code provides that insolvency proceedings and their effects are, in general, governed by the laws of the jurisdiction in which the proceedings have been opened. However, the Insolvency Code provides for some exceptions to this principle.

With respect to insolvency proceedings instituted in a jurisdiction other than Germany, section 351 of the Insolvency Code provides that rights *in rem* of creditors or third parties in assets of the insolvent estate will not be affected by the foreign proceedings provided that the relevant assets are situated in Germany at the time of the opening of the foreign proceedings and such right *in rem* entitles the creditor or, as the case may be, the third party to segregation of the relevant asset from the insolvency estate (*Aussonderung*) or separate satisfaction (*Absonderung*).

Section 338 of the Insolvency Code provides that any right to declare set-off is not affected by the opening of Insolvency Proceedings, provided that such right exists in accordance with the law governing the relevant claim of the Insolvent Party at the time the Insolvency Proceedings are instituted, and section 339 of the Insolvency Code provides that the validity of specific legal acts may be challenged if the requirements for doing this in insolvency proceedings are met in accordance with the law governing the insolvency proceedings, unless the party whose acts are to be challenged provides conclusive evidence that the relevant act is governed by the laws of another state and cannot be challenged thereunder.

(B) Effect of section 340 para 2 of the Insolvency Code on the Netting Provisions

Where the EU Insolvency Regulation and the Recast EU Insolvency Regulation do not apply, section 340 para 2 of the Insolvency Code provides that the effects of insolvency proceedings on "netting agreements" (*Schuldumwandlungsverträge und Aufrechnungsvereinbarungen*) are governed by the law applicable to such agreements, implementing Article 25 of the Winding-Up Directive into German law.[176]

Section 340 para 2 of the Insolvency Code refers to the substantive insolvency laws of the country the laws of which have been chosen by the parties to govern the relevant netting agreement given its wording, context and the legislator's intention to provide clarity on the applicable insolvency laws.[177]

Section 340 para 2 of the Insolvency Code provides for an insolvency conflict of laws rule for "netting agreements". In more detail, section 340 para 2 of the Insolvency Code provides for the effects of insolvency proceedings on netting agreements (*Schuldumwandlungsverträge und Aufrechnungsvereinbarungen*) to be governed by the law applicable to that agreement. Even though section 340 para 2 of the Insolvency Code does not provide any guidance on the interpretation of the term "netting agreement", the legislative history reveals that master agreements within the meaning of section 104 para 3 sent. 1 of the Insolvency Code fall within the scope of section 340 para 2 of the Insolvency Code.[178] Pursuant to the BGH, master agreements which contain

[176] Article 25 (addressing netting agreements (*Saldierungsvereinbarungen*)) of the Winding-Up Directive has been amended by Article 117 of the BRRD and should as from now be construed as referring to netting arrangements within the meaning of Article 2 para 1 no. 98 of the BRRD. Even though the wording of Article 25 of the Winding-Up Directive has been amended the wording of section 340 of the Insolvency Code was left unchanged but presumably was considered sufficient to address the change of the Winding-Up Directive. However, we construe the scope of section 340 of the Insolvency Code still on its wording rather than based on the changes made to Article 25 of the Winding-Up Directive.

[177] Before the 9 June 2016 decision, it was not entirely clear to which set of rules the wording "law of the country which governs such agreements" refers. Basically, section 340 para 2 of the Insolvency Code could refer to (i) the substantive insolvency laws of the jurisdiction that has been chosen by the parties to govern the relevant agreement (*Tashiro*, in: Braun, InsO, 7th ed. (2017) § 340 nos. 3 and 4; *Jahn/Fried*, in: Münchener Kommentar InsO, 3rd ed. (2014) § 340 no. 6 *et seq.*) (ii) the substantive contract law of the jurisdiction that has been chosen by the parties to govern the relevant agreement (*Kindler*, in: Münchener Kommentar BGB, 6th ed. (2015) § 340 InsO no. 5 (*lex causae*); *Stephan*, in: Heidelberger Kommentar InsO, 8th ed. (2016), § 340 nos. 6, 7).) or (iii) directly to the terms of the relevant agreement without any regard to the substantive insolvency or contract laws (this interpretation is supported by *Schneider*, in: Kohler/Obermüller/Wittig, Kapitalmarkt – Recht und Praxis, Gedächtnisschrift für Ulrich Bosch (2006), p. 211). This is now settled, as the BGH has applied substantive insolvency laws when referring to section 340 para 2 of the Insolvency Code (BGH WM 2016, 1168, 1172).

[178] BT-Drs. 15/16, p. 20; see also *Gottwald/Kolman*, in: Insolvenzrechtshandbuch, 5th ed. (2015), § 133 no. 86

netting agreements such as financial-market specific offsetting provisions (*finanzmarktspezifische Verrechnungsformen*), such as the German law governed Master Agreement for Financial Derivatives Transactions (*Rahmenvertrag für Finanztermingeschäfte*) fall within the scope of section 340 para 2 of the Insolvency Code.[179] When analysing what constitutes a netting agreement, the BGH emphasised the "balancing" or "netting" (*Saldierung*) of payment streams without referring to any other relevant features.[180]

Furthermore, as set out under Paragraph 5.1.1(i)(ii)(H) above, the General Agreement should qualify as a master agreement within the meaning of section 104 para 3 sent. 1 of the Insolvency Code. In addition, the Netting Provisions qualify as a netting agreement within the meaning of section 2 para 3 no. 43 of the Resolution Act (Paragraph 5.1.1(d)(D)(4) above).Thus, in our view, the General Agreement should also qualify as a netting agreement within the meaning of section 340 para 2 of the Insolvency Code. However, there are no court decisions beyond the decision of the BGH of 9 June 2016 as analysed above giving further guidance as to the scope and interpretation of this provision.

5.2.2 **German Multibranch Party**

(a) Additional assumptions

For the purposes of this Paragraph 5.2.2, we assume that one party to the General Agreement (Party A) has entered into Individual Contracts under the General Agreement through offices in Germany as well as through one or more branches located outside Germany. After entering into these Individual Contracts and prior to the maturity thereof, Party A becomes the subject of an Insolvency Proceeding.

(b) *Would there be any change in our conclusions reached under Paragraphs 5.1.1 or 5.1.2 above based upon the fact that Party A has conducted business under the General Agreement on a multibranch basis prior to its insolvency?*

If the main Insolvency Proceedings are opened in Germany, such main Insolvency Proceedings in Germany would be universal, which means that the Individual Contracts entered into by non-German branches of

[179] BGH WM 2016, 1168, 1172.

[180] BGH WM 2016, 1168, 1172.

Party A are included in the Insolvency Proceedings. Therefore, a single compensation claim is calculated in the main Insolvency Proceedings in Germany, provided, however, that German law cannot prevent that under the insolvency laws of another jurisdiction secondary insolvency proceedings are opened.

(i) Opening of main Insolvency Proceedings in Germany

(A) In case the EU Insolvency Regulation or the Recast EU Insolvency Regulation are applicable

If the EU Insolvency Regulation of the Recast EU Resolvency Regulation apply (please refer to Paragraph 5.2.1(a) above), Insolvency Proceedings are instituted in Germany with respect to Party A, because Party A has its centre of main interest in Germany (Paragraph 5.2.1(b)(i)).[181] This applies irrespective of whether or not the relevant authorities in any other jurisdiction have initiated proceedings in respect of a branch office or any other assets of the Insolvent Party in such jurisdiction. An Insolvency Administrator appointed in Germany in relation to Party A would include all transactions entered into under the General Agreement (regardless of the branch from which they were entered into) in the calculation of amounts owed to and from the Insolvent Party and would recognise the Netting Provisions and subject to sections 103, 104 and 119 of the Insolvency Code (see Paragraph 5.1.1(i)(ii) above).

(B) In case Party A is a CRR Institution or a German insurance company

In case Party A is a CRR Institution or a German insurance company, the main insolvency proceedings are also opened in Germany (please refer to Paragraphs 5.2.1(a) and 5.2.1(c)(ii)).

(C) In case neither the EU Insolvency Regulation nor the Recast EU Insolvency Regulation are applicable and Party A is not a European CRR Institution or a European insurance company

If neither EU Insolvency Regulation nor the Recast EU Insolvency Regulation apply and Party A is not a European CRR Institution or a European insurance company, insolvency proceedings are instituted with

[181] Please refer to the general assumption set out in Paragraph 4.1(a) above.

respect to Party A in the jurisdiction where Party A has its general place of jurisdiction. This applies irrespective of whether or not the relevant authorities in any other jurisdiction have initiated proceedings in respect of a branch office or any other assets of the Insolvent Party in such jurisdiction (please refer to Paragraph 5.2.1(c) above). In case of a legal entity, the place of general jurisdiction is the registered seat, except that if the centre of that legal entity's independent business activity is located elsewhere (for example, if the management is located at a place different to the registered seat) such place determines the competent insolvency court (section 3 para 1 sent. 2 of the Insolvency Code). Therefore, as the centre of main interest of Party A is in Germany (please refer to the assumption in Paragraph 4.1(a) above), the main insolvency proceedings will be opened in Germany.

(ii) Recognition of foreign secondary insolvency proceedings

If payment claims of Party A are deemed to be situated in a jurisdiction other than Germany (please refer to Paragraphs 5.2.1(b)(iv) and 5.2.1(c)(iv)) and secondary insolvency proceedings are opened in such jurisdiction, such secondary insolvency proceedings are recognised in Germany within the limits of section 343 para 1 sent. 2 of the Insolvency Code and Article 16 of the European Insolvency Regulation and Article 19 of the Recast European Insolvency Regulation, which require the recognition of such proceedings only if the relevant court had jurisdiction. If under the insolvency proceedings in such other jurisdiction, the Netting Provisions of the General Agreement are not enforceable, then, even if the General Agreement has been terminated prior to the opening of the main Insolvency Proceedings in Germany, the Insolvency Administrator will not enforce the payment claims that are situated in such other jurisdiction. The net payment claim of Party A under the General Agreement, if any, will be decreased accordingly.

(c) *Would the General Agreement be treated as a single unified agreement by the German receiver under the laws of Germany, regardless of the treatment of the General Agreement or Individual Contracts by an insolvency official in a country where close-out netting may be unenforceable?*

If claims under the Individual Contracts governed by the General Agreement become the subject of a secondary insolvency proceeding, and the single agreement concept is not recognised in such proceeding, the General Agreement would not be treated as a single unified agreement by the German Insolvency Administrator, to the extent such secondary insolvency proceedings are recognised in Germany. Rather, the separate treatment of Individual Contracts which are the subject of secondary insolvency proceedings would also be recognised in Germany.

5.2.3 **Foreign Multibranch Party**

(a) Additional assumptions

As instructed, we assume that a company, a credit institution, a financial services institution, an insurance company or any other similar financial institution covered by this Opinion ("**Party F**") incorporated, organised or having its centre of main interest in a country ("**Country H**") other than Germany has entered under the General Agreement into Individual Contracts both through its home office and through one or more branches located in other countries including in each case a branch of Party F located in and subject to the laws of Germany (the "**German Branch**").

After entering into these Individual Contracts and prior to the maturity thereof, Party F becomes the subject of voluntary or involuntary proceedings under the insolvency laws of Country H.

(b) *Would there be separate proceedings in Germany with respect to the assets and liabilities of the German Branch upon the start of insolvency proceedings for Party F in Country H? Or would the relevant authorities in Germany defer to the proceedings in Country H, so that the assets and liabilities of the German Branch would be handled as part of the proceedings for Party F in Country H?*

(i) In case the EU Insolvency Regulation or the Recast EU Insolvency Regulation are applicable

If the EU Insolvency Regulation or the Recast EU Insolvency Regulation are applicable to the insolvency of Party F (please refer to Paragraph 5.2.1(a)), the German Branch would qualify as an "establishment" of Party F in Germany (please refer to Paragraph 2.5. Hence, secondary insolvency proceedings (Article 3 para 3 of the EU Insolvency Regulation or Article 3 para 3 of the Recast EU Insolvency Regulation) may be opened by a German insolvency court after the opening of the main insolvency proceedings in Country H, or territorial insolvency proceedings may be opened absent main insolvency proceedings in Country H (Article 3 para 2 of the EU Insolvency Regulation or Article 3 para 2 of the Recast EU Insolvency Regulation). Such secondary insolvency or territorial insolvency proceedings would be limited to the assets of Party F which are situated in Germany (please refer to Paragraph 5.2.1(b)(ii)). Claims of Party F are deemed to be situated in Germany if the debtor of such claim has the centre of its main interests in Germany, as determined in Article 3 para 1 of the EU Insolvency Regulation or Article 3 para 1 of the Recast EU Insolvency Regulation. In case of a company or legal person, the place of the registered office is presumed to be the centre of its main interests in the absence of evidence to the contrary (please refer to Paragraph 5.2.1(a) above). This applies irrespective of whether or not such claims arise from transactions which were entered into by an establishment of Party F in Germany.

(ii) In case Party F is a European CRR Institution or a European insurance company

In case Party F is a European CRR Institution or a European insurance company, the EU Insolvency Regulation is not applicable (please refer to Paragraph 5.2.1(a)). Only the insolvency courts or other relevant authorities in the home member state of such European CRR Institution or European insurance company may open insolvency proceedings (section 46e para 1 sent. 1 of the Banking Act; please refer to Paragraph 5.2.1(c)(ii)). Therefore, even though Party F has an establishment in Germany, no secondary insolvency proceedings will take place in Germany.

(iii) In case neither the EU Insolvency Regulation nor the Recast EU Insolvency Regulation are applicable and Party F is not a European CRR Institution or a European insurance company

In case neither the EU Insolvency Regulation nor the Recast EU Insolvency Regulation are applicable and Party F is not a European CRR Institution or a European insurance company, sections 335 to 358 which provide for the conflicts of law rules of the Insolvency Code apply. German insolvency courts may open secondary insolvency proceedings (section 354 of the Insolvency Code) in addition to the insolvency proceedings in Country H or, absent such insolvency proceedings in Country H, territorial insolvency proceedings (section 354 para 1 of the Insolvency Code). Such secondary insolvency or territorial insolvency proceedings will be limited to the assets of Party F which are situated in Germany. Payment claims are deemed to be situated in Germany if Party F as debtor thereunder has its registered office in Germany (in case Party F is a corporation) or if Party F's place of residence is in Germany (please refer to Paragraph 5.2.1(c)(iv)).

(c) *If there were separate proceedings in Germany with respect to the assets and liabilities of the German Branch, would the receiver or liquidator in Germany and the German courts, based on the facts above, include Party F's position under the General Agreement, in whole or in part, among the assets of Germany and, if so, would the receiver or liquidator and the German courts recognise the close-out netting provisions of the General Agreement in accordance with their terms? The most significant problem arising would be if a German receiver, liquidator or court considering a single General Agreement were to require a counterparty of the German Branch of Party F to pay the mark-to-market value of Individual Contracts entered into with the German Branch to the liquidator or receiver of the German Branch, while at the same time forcing the counterparty to claim in the proceedings in Country H for its net value from other Individual Contracts with Party F under the same General Agreement. In considering this issue, please assume that close-out netting under the General Agreement would be enforced in accordance with its terms in the proceedings for Party F in Country H.*

If, according to the principles set out in Paragraph 5.2.3(b) above, separate Insolvency Proceedings are opened in Germany, such separate Insolvency Proceedings cover all assets of the debtor situated in Germany (for the situation of payment claims, please refer to Paragraphs 5.2.1(b)(iv) and 5.2.1(c)(iv)). Therefore, separate insolvency estates will be created, despite the single agreement concept provided for in Section 1.1 sent. 1 of the General Agreement.

Potentially, an Insolvency Administrator considering a single General Agreement might require a counterparty of the German Branch of Party F to pay the mark-to-market value of Individual Contracts entered into with the German Branch to the insolvency estate in Germany, while at the same time forcing the counterparty to claim in the proceedings in Country H for its net value from other Individual Contracts with Party F under the same General Agreement. However, this risk does not exist if at the time the secondary Insolvency Proceedings in Germany are opened, the General Agreement has been closed out already (and no claims under the Individual Contracts remain) and such close-out netting is recognised under German conflicts of law rules (please refer to Paragraph 5.2.1(d)).

(d) *Would it make any difference if Party F has no branch located in Germany, but has assets in Germany?*

If Party F does not have an establishment in Germany,[182] but has assets in Germany, secondary Insolvency Proceedings may be opened in

[182] For a discussion of the term "establishment" see *Reinhart* in: Münchener Kommentar zur InsO, 3rd ed. (2014), § 354 no. 7.

Germany, if a creditor has a particular interest in the opening of such Insolvency Proceeding, in particular, if such creditor would be in a substantially worse position if no secondary Insolvency Proceedings were opened. The opening of secondary Insolvency Proceedings in Germany on the basis of assets of the debtor in Germany has been controversially discussed.[183] However, the mere fact that a claim is situated in Germany may already allow the opening of secondary Insolvency Proceedings in Germany.

5.3 Collateral under the Credit Support Annex

5.3.1 Additional Assumptions

In this Paragraph 5.3, as instructed we assume that at least one of the counterparties entering into the General Agreement is incorporated or organised or has its centre of main interest in Germany ("**Party A**"). Although the Credit Support Annex is a bilateral form in that it contemplates that each party may be required to post collateral to the other, we assume that (i) Party A is at all times the transferor (the "**Transferor**") and Party B the transferee (the "**Transferee**") under the Credit Support Annex and (ii) that under the Credit Support Annex, the collateral is owned by Party A or that Party A is authorised and empowered to transfer ownership in the collateral.

The counterparties agree that Eligible Credit Support includes Cash and Letters of Credit (as defined in the Credit Support Annex). Cash is denominated in a freely convertible currency (specified as "Base Currency" or "Eligible Currency" in Section 14.10 or Section 14.11 of the Credit Support Annex) and is held in an account under the control of Party B.[184]

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[183] Neither the EU Insolvency Regulation nor the Recast EU Insolvency Regulation provide for jurisdiction based on the situation of assets. However, section 354 para 2 of the Insolvency Code recognises that secondary Insolvency Proceedings may be opened in Germany due to the location of assets in Germany (*Wenner* in: Mohrbutter/Ringstmeier, Handbuch der Insolvenzordnung, 9th ed. (2015), § 20 no. 71.)

[184] The Financial Collateral Directive provides in Article 2 para 2 that "References in this Directive to financial collateral being "provided", or to the "provision" of financial collateral, are to the financial collateral being delivered, transferred, held, registered or otherwise designated so as to be in the possession or under the control of the collateral taker or of a person acting on the collateral taker's behalf. Any right of substitution or to withdraw excess financial collateral in favour of the collateral provider or, in the case of credit claims, right to collect the proceeds thereof until further notice, shall not prejudice the financial collateral having been provided to the collateral taker as mentioned in this Directive." In a recent decision (C-156/15 of 10 November 2016), the ECJ, dealing with the question what "control" means with respect to collateral in respect of monies deposited in a bank account, has ruled that "the taker of collateral… in the form of monies lodged in an ordinary bank account may be regarded as having acquired 'possession or control' of the monies only if the collateral provider is prevented from disposing of them." There is no express reference in section 1 para 17 of the Banking Act to "control", but we are of the view that the term "provide" in that section would need to be interpreted in conformity with European Union law. To the extent that the security provider is entitled to dispose over the Cash being collateralised (at least in cases which do not relate to a right to substitution or withdrawal of excess collateral), there would be a risk that a court could take the view that the qualification as Financial Collateral is endangered.

5.3.2 Questions to be opined on

(a) *Under the laws of Germany, what law governs the transfer of ownership in the various forms of Eligible Credit Support deliverable under the Credit Support Annex?*

Under German conflict of law rules regarding the transfer of Cash, one has to distinguish between Cash held in a bank account and Cash in the form of money bills or coins: Where the ownership in Cash is transferred or where a security interest is created in Cash and such Cash is held in a bank account, German conflict of law rules refer to the law governing the account relationship between the bank and the payee (in this event the Cash is represented by the payee's claim against the bank maintaining its account in regard of the Cash transferred).

Last but not least, the assignment of claims for the payment of money and the creation of a security interest in such claims, as well as the effects of such assignment or creation, are governed by the law which governs such claims.

(b) *Would the laws of Germany characterise each transfer of collateral as effecting an unconditional transfer of ownership in the assets transferred? Is there any risk that any such transfer would be re-characterized as creating a security interest? If so, is there any way to minimize such risk? What would be the consequences of such a re-characterisation?*

In the case of a Letter of Credit, no assets are transferred. Therefore, the following paragraphs consider the situation where Cash is given as Eligible Credit Support. For Cash, we assume that the Eligible Credit Support is paid to the Transferee and not to any third party.

It should be noted that the Credit Support Annex provides only for an obligation to transfer the title but not for the actual transfer of title. Therefore, when granting or substituting Eligible Credit Support, both Parties need to ensure that all necessary steps will be taken separately so that the title in the relevant assets will pass. The transfer of title itself is subject to mandatory conflict of law provisions (see the respective German conflict of law provisions outlined in Paragraph 5.3.2(a) above).

Pursuant to Section 3 of the Credit Support Annex, the Transferor (as defined in Section 3 para 1 of the Credit Support Annex) is obliged to transfer cash into the account of the Transferee (as defined in Section 3 para 1 of the Credit Support Annex) specified in Section 13 of the Credit Support Annex and any Excess Credit Support (as defined in section 4 of the Credit Support Annex) must be retransferred by the

Transferee to the Transferor in accordance with Section 4 of the Credit Support Annex. Section 7 para 1 of the Credit Support Annex provides that all right, title and interest in and to any Eligible Credit Support must be transferred from the Transferor to the Transferee.

Cash credited to an account is represented by the repayment claim of the relevant account holder against the entity maintaining the account, such as a bank or a custodian. Hence, under German law, a security interest over cash credited to an account is established by creating a security interest in the relevant repayment claim of the account holder against the relevant account bank. However, where the account is held in the name of the secured party, any transfer of cash made into such account *prima facie* constitutes an asset of the secured party and it would not be necessary to create a security interest over such account. In other words, where the cash is transferred into an account opened in the name of the secured party it is treated as a transfer of "ownership" (*Vollrechtsübertragung*),[185] rather than as a security interest (*Sicherheit* or *beschränkt dingliches Recht*).

Where the cash is booked in an account held in the name of the security provider, a security interest over such account needs to be created.[186]

Generally under German law, different types of security over assets can be created, such as a security interest in the Cash balance on an account such as a pledge (*Pfandrecht*), [187] a transfer for security purposes (*Sicherungsabtretung*) and a transfer of ownership.

Article 14 of the Rome I Regulation contains the relevant conflict of laws provisions for security over contractual claims. Article 14 para 1 of the Rome I Regulation provides that the relationship between

[185] Transfer of ownership arrangements as a security have been recognised by German statutory law (section 1 para 17 of the Banking Act) following the implementation of the Financial Collateral Directive.

[186] Where an account is held in the name of the account holder but for the account of another person, for example a fiduciary account (*Treuhandkonto*), the secured party should verify whether the account holder may dispose of such account and validly create a security interest over such account and, as the case may be, the relevant beneficiary under such account has approved the creation of the security interest. If the secured party is aware that the account is a fiduciary account (*offenes Treuhandkonto*), the secured party cannot in good faith acquire a security interest in the assets booked into the account. If the secured party is not aware that the account is a fiduciary account (*verdecktes Treuhandkonto*), the secured party can acquire a security interest in the account. However, when a secured party later becomes aware the relevant account is a fiduciary account, it must not enforce a security interest acquired in such account or exercise any set-off rights (BGH WM 1990, 1954, 1955; BGH WM 1996, 249, 251; *Hadding/Häuser*, in: Schimansky/Bunte/Lwowski, Bankrechts-Handbuch, 4th ed. (2011), § 37 nos. 43 *et seq.*). This means that even if a security interest has been validly created over a fiduciary account because it was created without the awareness of the secured party, this can subsequently be frustrated by making a person that has taken such security subsequently aware of the fiduciary nature of the account.

[187] Pledges of rights are subject to sections 1273 *et seq.* of the German Civil Code.

assignor and assignee is governed by the law that applies to the contract between the assignor and assignee under the Rome I Regulation, i.e. the parties may choose the governing law under Article 3 para 1 of the Rome I Regulation. Recital 38 of the Rome I Regulation makes it clear that this also covers the property aspects of the assignment in countries such as Germany where these aspects are legally separate from the law of obligations. The same applies in respect of pledgor and pledgee in case a claim is pledged (Article 14 para 3 of the Rome I Regulation). The law governing the pledged claim is relevant in determining whether the claim can be pledged, the relationship between the pledgee and the pledgor, the conditions under which the pledge can be invoked against the pledgor and whether the pledgor's obligations have been discharged (Article 14 para 2 of the Rome I Regulation)

Section 7 of the Credit Support Annex indicates that the parties have no intention of establishing a pledge, but to transfer Cash balances by way of "outright transfer" to a Transferee's account. Thus, the payment of Cash by the Transferor into an account of the Transferee under the Credit Support Annex should neither qualify as a pledge nor as a transfer for security purposes but as a "transfer of ownership" in the Cash.

In the unlikely event that the courts of Germany would re-characterise the transfer of Cash under the Credit Support Annex as a creation of a security right other than a transfer of "ownership" the transfer of the Cash would not be void due to a lack of registration since there is no such requirement under German law. However, if the account to which the Cash has been transferred is maintained in a jurisdiction other than Germany, the laws of that other jurisdiction should be checked to ensure that the transfer would not be re-characterised with possibly adverse effects.

(c) *Assuming that the counterparty receives absolute ownership in the collateral, will it need to take any action thereafter to ensure that its title therein continues? Are there any requirements in Germany necessary or advisable, including any filing, registration, notification, stamping, notarisation or any other action or the obtaining of any governmental, judicial, regulatory or other order, consent or approval? Are there any other procedures that must be followed or consents or other governmental or regulatory approvals that must be obtained or established, to enforce, or continue such ownership interest?*

Under the laws of Germany, no further action such as, for instance, filing a registration, a notification, stamping, or notarisation is required to enforce or continue such ownership.

However, if the account to which the Cash has been transferred is maintained in another jurisdiction the laws of that jurisdiction should be checked to verify that there are no procedures that must be followed to enforce or continue such ownership interest.

(d) *What is the effect, if any, under the laws of Germany of the right to substitute collateral pursuant to Section 6 of the Credit Support Annex? Does the presence or absence of consent to substitution by the counterparty have any bearing on this question?*

Subject to the approval of the Transferee, under Section 6 of the Credit Support Annex the Transferor is entitled to replace, in whole or in part, any Eligible Credit Support provided under the Credit Support Annex by other Eligible Credit Support of the same or higher value. Under German law, the contractual obligation or right to the re-transfer of title has to be distinguished from the actual re-transfer of such title. The right of the Transferor to exchange Eligible Credit Support (for example, by swapping Euros for United States Dollars) pursuant to Section 6 of the Credit Support Annex is a contractual right only.

Where the transfer of Eligible Credit Support itself is governed by German law, in order to effect an valid *in rem* transfer (*dingliche Übertragung*) for a substitution, an additional agreement on the re-transfer of the relevant assets to be replaced by the Transferee to the Transferor and an additional agreement on the transfer of the assets newly provided as Eligible Credit Support by the Transferor to the Transferee is required because each of such transfers needs to be made in compliance with the applicable German law requirements to validly transfer title to such asset (including any additional activities such as transfer of possession or a book entry). Thus, if the Transferee refuses to actually re-transfer the respective assets to the Transferor, the title to the relevant assets remains with the Transferee, even if the Transferee is under a contractual obligation pursuant to Section 6 of the Credit Support Annex to re-transfer such asset.

(e) *Party B's right in relation to the transferred collateral upon termination of the relevant master agreement will be governed by Section 11 of the General Agreement together with Section 11 of the Credit Support Annex. Assuming that Section 11 of the General Agreement is valid and enforceable in Germany insofar as it relates to the determination of a net amount payable by either party on the termination of Individual Contracts, is Section 11 of the Credit Support Annex also valid to the extent that it provides for the value of the collateral provided and not yet transferred to be included in the calculation of a net amount payable under Section 11 of the General Agreement as "other amounts payable"?*

According to Sections 11 and 12 of the Credit Support Annex, the value of all Eligible Credit Support provided under the Credit Support Annex must be included in the Termination Amount to be determined pursuant to Section 11 of the General Agreement as part of "other amounts payable" by the Transferee. The inclusion of such Eligible Credit Support in the calculation of the net amount payable under Section 11 and 12 of the Credit Support Annex as "*other amounts payable*" upon early termination should in our view be recognised. Section 104 para 2 of the Insolvency Code refers to replacement transactions (whether or not actually entered into) but not to what extent any collateral is included in the calculation of the market or exchange value of the relevant fixed date or financial transaction. When giving examples of permissible contractual agreements deviating from the principles otherwise stipulated in section 104 of the Insolvency Code section 104 para 4 of the Insolvency Code does not refer to any collateral arrangements. However, Financial Collateral qualifies as financial transaction under section 104 para 1 sent. 3 no. 6 of the Insolvency Code. So to the extent the collateral qualifies as Financial Collateral it would in our view ultimately not matter whether the collateral is included in the valuation of any replacement transaction in case in can be argued that the replacement transaction needs to fully reflect the terms of the relevant transaction, including any collateral provided, or, which in our view is the better view, collateral would be treated and valued separately as a financial transaction covered by section 104 para 1 sent. 3 no. 6 of the Insolvency Code. We are not aware of any court decisions or any further guidance on this question.

Eligible Credit Support in form of Cash may generally qualify as Financial Collateral if the relevant legal requirements are met, in particular if both Parties are covered by section 1 para 17 of the Banking Act or in case the security provider is a person or business undertaking named in Article 1 para 2 lit (e) of the Financial Collateral Directive the collateral secures obligations arising under agreements or the procurement of agreements which serve towards (a) the acquisition and sale of financial instruments, (b) sale and repurchase, lending or similar transactions on financial instruments or, (c) loans to finance the acquisition of financial instruments (see Paragraph 5.8.1(f) below. Letters of Credit, however, do not qualify as Financial Collateral.

The provision of Section 11 of the Credit Support Annex, pursuant to which Eligible Credit Support is applied to a Settlement Amount by way of contractual set-off, would recognised, subject to restrictions to the right to set off after the opening of Insolvency Proceedings; see Paragraph 5.1.1(o)(i) above.

(f) *Are the rights of Party B enforceable in accordance with the terms of the General Agreement and the Credit Support Annex, irrespective of the insolvency of Party A?*

If Party A has provided cash collateral in the form of a full title transfer prior to the commencement of Insolvency Proceedings, Party B is regarded as the person entitled to such cash collateral. As set out above, it is unlikely that the courts of Germany would re-characterise the transfer of Cash under the Credit Support Annex as a creation of a security right other than a transfer of "ownership" (please refer to Paragraph 5.3.2(b)).

However, such transfers of cash collateral are generally subject to the challenge under insolvency rules, subject to an exception for margin collateral (please refer to Paragraph 5.1.1(c)).

Upon the opening of the Insolvency Proceedings the Insolvency Administrator is vested with Party A's right to manage and transfer the insolvency estate (section 80 para 1 of the Insolvency Code). Therefore, if following the commencement of Insolvency Proceedings, Party A transfers an object forming part of the insolvency estate, such transfer is legally invalid (section 81 para 1 sent. 1 of the Insolvency Code).

If the debtor transferred an object forming part of the insolvency estate on the day on which the Insolvency Proceedings were opened, such transfer is presumed to have been effected after the opening of the Insolvency Proceedings. However, provided that at least Party B qualifies as a credit or financial services institution, including (without limitation) financial institutions within the meaning of Article 1 para 2 lit (d) of the Financial Collateral Directive, any transfer by the debtor in respect of Financial Collateral within the meaning of section 1 para 17 of the Banking Act (please refer to footnote 14) following the opening of Insolvency Proceedings is, subject to generally applicable insolvency challenge rules (please refer to Paragraph 5.1.1(c)), legally valid if it occurred on the day of the opening and the other party proves that he was neither aware of nor had to be aware of the opening of the proceedings (section 81 para 3 of the Insolvency Code).

(g) *Will Party A (or its receiver or other similar official) be able to recover any transfer of collateral provided to the counterparty during a certain "suspect period" preceding the date of the insolvency? If so, how long before the insolvency does the suspect period begin? If such a period exists, does the substitution of collateral by a counterparty during this period invalidate an otherwise valid transfer, assuming the substitute assets are of no greater value than the assets they are replacing? Is the transfer of additional collateral pursuant to the* *mark-to-market provisions of the Credit Support Annex during the suspect period subject to avoidance, either because it was considered to relate to an antecedent or pre-existing obligation or for some other reason?*

Following the commencement of Insolvency Proceedings, any transfer of Cash collateral is invalid, subject to an exception applicable to Financial Collateral which is transferred on the day on which the Insolvency Proceedings are opened (please refer to Paragraph 5.3.2(f)).

As further set out in Paragraph 5.3.2(f), the transfer of Cash collateral prior to the commencement of Insolvency Proceedings is subject to the general applicable challenge in insolvency rules as the transfer is a legal act, subject to an exception for margin collateral. Thus, transfer of Eligible Credit Support under the provisions of the Credit Support Annex could be challenged by an Insolvency Administrator during insolvency challenge periods (please see Paragraph 5.1.1(c) for a discussion of the relevant insolvency challenge periods and for an exception for margin collateral).

Under German law, substitution of collateral whereby the collateral provider can re-claim particular securities and replace them with other securities of equivalent value is considered as a transaction consisting of various legal acts based on the declared intention of the security provider such as the conclusion of the collateral agreement providing for collateral substitution, each withdrawal of particular securities and each replacement of securities with other securities of equivalent value each of which is principally subject to challenge in insolvency under German insolvency law. Hence, each substitution is deemed to consist of two transfers that need to be made in compliance with the applicable requirements to validly transfer title to such asset and principally is subject to new insolvency challenge periods.

(h) *Is the EFET Credit Support Annex in an appropriate form to create the intended outright transfer of ownership in the collateral to Party B? Are there any other requirements to be observed in Germany in order to ensure validity of such transfer in each type of Eligible Credit Support created by Party A under the Credit Support Annex? For example, are there any other requirements such as those mentioned under Paragraph 5.3.2(b)?*

As set out in Paragraph 5.3.1 above5.3.2(a), we understand that under the terms of the Credit Support Annex, only Cash or Letters of Credit qualify as Eligible Security.

In the case of a Letter of Credit, no assets will be transferred.

In case of the transfer of cash collateral, the EFET Credit Support Annex is in an appropriate form to provide the basis for a legal obligation for a transfer of "ownership" (please refer to Paragraph 5.3.2(b)). To actually transfer the ownership in certain assets additional requirements may need to be fulfilled (such as the transfer of possession or any book entries).

(i) *Do you have other specific recommendations on the subject of collateral that you would like the EFET members to consider?*

We do not have other specific recommendations on the subject of collateral but we are happy to discuss any topics related to collateral not yet covered by this Opinion to develop further issues to be addressed.

5.4 **General Enforceability**

For the purposes of the following analysis of this Paragraph 5 we assume that the General Agreement and Annexes are governed by German law. Where the General Agreement and Annexes are governed by English law, please see our comments in Paragraph 5.4.1(d)(ii) below.

5.4.1 *Is the General Agreement and any of the above Annexes (including the Credit Support Annex) enforceable under the laws of Germany in accordance with its own terms? We would like you to specifically discuss the provisions on (a) non-performance due to Force Majeure (Section 7 of the General Agreement); (b) remedies for non-performance (Section 8 of the General Agreement); (c) limitation of liability (Section 12 of the General Agreement); and (d) any other provisions which need to be commented on according to the law of Germany, including whether these provisions could be further expanded or strengthened under the laws of your jurisdiction.*

We are especially interested in provisions that you may believe infringe upon the ordre public in Germany and that may be challenged by the courts in Germany irrespective of the law that governs the General Agreement.

(a) Enforceability of non-performance due to Force Majeure (Section 7 of the General Agreement)

Under German statutory law, the occurrence of an event described as *Force Majeure* in Section 7 of the General Agreement may give rise to a termination right.

By way of background, such event may also qualify as a material reason pursuant to section 314 of the German Civil Code and may give rise to a termination right if, after having regard to all circumstances of the specific case and balancing the interests of both parties, the terminating party cannot reasonably be expected to continue the contractual relationship until the agreed termination date or until the end of a notice period. The parties to an agreement may also agree on additional termination rights which specify or supplement the statutory termination rights for serious cause (please refer to Paragraph 5.1.1(i)(i) above).

In addition to the circumstances described as *Force Majeure* in Section 7 of the General Agreement, a party to the General Agreement is discharged from performing an obligation if such performance is impossible for the debtor or for anyone else (section 275 of the German Civil Code).

Furthermore, section 313 of the German Civil Code codifies the German law doctrine of "*Wegfall der Geschäftsgrundlage*" which provides for a right to adjust or terminate contracts in circumstances which, having been beyond the control of the parties and unforeseeable when entering into the contract, render the performance under the agreed terms unreasonable.[188] If an adjustment of the contract is not possible or is unreasonable to one of the parties, the disadvantaged party may withdraw from the contract, and in case of contracts providing for continuous obligations, terminate the contract.[189]

In our view sections 313, 314 of the German Civil Code generally do not prohibit clauses which provide for a non-performance due to *Force Majeure*. To the extent sections 305 to 310 of the German Civil Code, as further set out in Paragraph 6.3.15 below, do not provide otherwise, Section 7 of the General Agreement would be enforceable.

(b) Enforceability of remedies for non-performance (Section 8 of the General Agreement)

Section 8 of the General Agreement provides that if the party obliged to deliver natural gas (the "**Delivering Party**") fails to perform its obligations for reasons other than *Force Majeure* or the other party's non-performance, the Delivering Party is obliged to pay damages. Section 8 of the General Agreement does not provide for any grace period or warning notice to be observed or delivered by the other party. With respect to the calculation of the amount of damages, Section 8 of the General Agreement provides that such amount must be calculated on the basis of the difference between the price agreed between the parties and the price at which the party entitled to damages, acting in a reasonable manner, is or would be able to purchase or otherwise acquire in the market the quantity of undelivered natural gas.

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[188] This doctrine has been developed in court decisions and is now explicitly included in section 313 of the German Civil Code. See BGH NJW 2001, 1204, 1205; BGHZ 129, 236, 252; BGHZ 129, 297, 309; BGHZ 131, 209, 214; BGHZ 135, 333, 338.

[189] *Finkenauer* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 313 no. 117.

(i) Termination right in case of fixed date transactions

For the purposes of the analysis, relative fixed date transactions and absolute fixed date transactions must be distinguished.

(A) Relative fixed date transactions

Section 376 para 1 of the Commercial Code entitles the creditor to damages in case the other party does not deliver in time and is in default pursuant to section 286 of the German Civil Code. Section 376 para 1 of the Commercial Code only applies to natural gas delivery contracts if at least one party to such contract is a merchant (section 345 of the Commercial Code). In addition, the natural gas delivery contract has to be a fixed date transaction. Under the German Civil Code and Commercial Code fixed date transactions are transactions where due to the importance to receive performance in time the creditor is no longer interested in performance by the other party if such performance has not been made on the agreed date; see section 323 para 2 no. 2 of the German Civil Code. Section 376 para 1 of the Commercial Code only applies to relative fixed date transactions according to which, in contrast to absolute fixed date transactions, subsequent delivery of performance is still possible and the purpose of the agreement can still be achieved[190] (please also refer to Paragraph 5.1.1(i)(ii)(D) above).

If a natural gas delivery contract under the General Agreement qualifies as a relative fixed date transaction and if a party is entitled to damages pursuant to section 376 para 1 of the Commercial Code and the commodities (*Waren*) which have not been delivered have a market or exchange price, the damages which the creditor is entitled to may be calculated on the basis of such market or exchange price. The creditor does not have to actually purchase the commodities (*Waren*) on the market or exchange, but may calculate and claim damages on the basis of the difference between the price agreed with the non-performing party and the market or exchange price at the time of non-

[190] *Hopt* in: Baumbach/Hopt, Handelsgesetzbuch, 37th ed. (2016), § 376 no. 4; *Grunewald* in: Münchener Kommentar zum HGB, 3rd ed. (2013), § 376 no. 11; *Roth* in: Koller/Kindler/Roth/Morck, HGB, 8th ed. (2015), § 376 no. 1. In case of an absolute fixed date transaction, delayed delivery is not considered performance anymore and accordingly, upon non-performance the provisions of impossibility (*Unmöglichkeit*) in accordance with sections 275, 283, 326 of the German Civil Code).

performance by the non-performing party. If the creditor makes a replacement purchase, the damages are calculated on the basis of the difference between the price agreed with the non-performing party and the price actually paid for the replacement purchase, provided, however, that such replacement purchase has to be made immediately after the time at which the delivery by the other party would have been due (section 376 para 3 sent. 1 of the Commercial Code). Therefore, if the replacement purchase is not made immediately after the time the performance was due by the non-performing party, any additional costs incurred by the creditor due to a rise in the market or exchange price may not be claimed for as damages.

Presuming that the natural gas delivery contract qualifies as a relative fixed date transaction, the non-performing party is in default pursuant to section 286 of the German Civil Code, and the replacement purchase is made immediately after the time agreed in the natural gas delivery contract between the creditor and the non-performing party, Section 8 of the General Agreement would in our view be enforceable to the extent sections 305 to 310 of the German Civil Code, as further set out in Paragraph 6.3.15 below, do not provide otherwise.

(B) Absolute fixed date transactions

Section 283 of the German Civil Code entitles the creditor to damages in case the other party is no longer obliged to perform pursuant to section 275 para 1 to 3 of the German Civil Code and the requirements of section 280 para 1 of the German Civil Code are satisfied. Section 283 of the German Civil Code does not provide for any grace period or warning notice to be observed or delivered by the other party. As set out in Paragraph 5.1.1(i)(ii)(D) above regarding absolute fixed date transactions, a claim for performance subsequent to the agreed performance date is excluded by law pursuant to section 275 para 1 of the German Civil Code because performance at a later point in time will be useless and will be treated as impossible for the debtor. Delayed performance would not constitute performance in accordance with the agreement but a completely different performance instead.

With respect to the calculation of the amount of damages section 249 of the German Civil Code provides that damages must restore the position that would exist if the circumstance obliging the party in default to pay damages had not occurred (*Natural-restitution*). If it is impossible for the debtor to restore the position, section 251 of the German Civil Code provides for compensation in money which is to be calculated on the basis of a market price or on the basis of a replacement purchase value.

If a natural gas delivery contract under the General Agreement qualifies as an absolute fixed date transaction and if a party is entitled to damages pursuant to sections 280, 283 of the German Civil Code and the creditor makes a replacement purchase, the damages are calculated on the basis of the difference between the price agreed with the non-performing party and the price actually paid for the replacement purchase.

If the natural gas delivery contract qualifies as an absolute fixed date transaction and the non-performing party is in default pursuant to section 283 of the German Civil Code, Section 8 of the General Agreement would in our view be enforceable to the extent sections 305 to 310 of the German Civil Code, as further set out in Paragraph 6.3.15 below, do not provide otherwise.

(ii) Requirement of a grace period pursuant to section 281 of the German Civil Code

(A) Statutory provisions

If the natural gas delivery contract does not qualify as a fixed date transaction, the creditor has to grant a reasonable grace period for the delivery before claiming damages (section 281 para 1 sent. 1 of the German Civil Code), and the creditor may only demand damages after the lapse of such grace period. The requirement to grant such grace period is only waived if the debtor has made it clear that the debtor will not perform the obligation to deliver, or, if special circumstances exist which, taking into account the interests of both parties, justify the immediate assertion of damages, without granting a grace period (section 281 para 2 of the German Civil Code). The latter exemption is to be construed narrowly and is only applicable if the purpose for which the creditor requested the performance cannot be fulfilled anymore in case of a performance at a later point in time.[191]

Whether this applies to a natural gas delivery contract under the General Agreement depends on the circumstances of the individual case. However, due to the narrow interpretation of this exemption, this exemption may not always apply. In such case, Section 8 of the General Agreement would deviate from the statutory provisions. It is questionable whether such a deviation is enforceable.

(B) Application of rules on standard business conditions (*Allgemeine Geschäftsbedingungen*)

The aforementioned deviation has to comply with sections 305 to 310 of the German Civil Code.

As further set out in Paragraph 6.3.15 below, sections 305 to 310 of the German Civil Code apply to contractual terms which have not been negotiated individually but are applied by one of the contracting parties as standard business conditions. The term "**standard business conditions**" means pre-formulated contractual conditions imposed by one party on another. In general terms, the restrictive statutory provisions on the use of standard business conditions would apply if one party incorporates general terms and conditions which have not been negotiated, for example, where one party uses standardised contracts such as the General Agreement.

However, if both parties respectively use the same master agreement, for example the General Agreement, as their respective standard terms, the risk that the provisions of the German Civil Code on standard business conditions are applicable is significantly reduced. The majority of commentators in legal literature holds that if both parties to an agreement mutually refer to the same standard business conditions and mutually request their introduction into the contract, sections 305 to 310 of the German Civil Code should

[191] BGH NJW-RR 1997, 622, 623 *et seq.*; *Ernst* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 281 no. 62 and § 323 nos. 128 *et seq.*

not apply to such terms and conditions.[192] Although we generally share this view, it is also important to note that there is some uncertainty on whether the courts will follow this argument with regard to the General Agreement as well, because there are not many court decisions regarding this question,[193] and because some legal commentators suggest that sections 305 to 310 of the German Civil Code also apply to standard business conditions which are commonly used by both parties to a contract.[194] In particular where the counterparty to a master agreement is a new and inexperienced market participant, it is not entirely clear whether German courts would share this view and rule accordingly that such party deserves protection under sections 305 to 310 of the German Civil Code.

Notwithstanding the aforementioned exemption, to the extent that agreements will only be concluded with a person pursuing its commercial or independent professional activities as entrepreneur (*Unternehmer*) within the meaning of section 14 of the German Civil Code or with private or public law legal entities, sections 305 to 310 of the German Civil Code apply to a limited extent. If the General Agreement is entered into with one of the aforementioned type of counterparties, sections 308 and 309 of the German Civil Code specifying certain generally prohibited clauses will not apply. Nevertheless, the agreement must not alter substantial principles of German law or lead to consequences that are either surprising, overly disadvantageous or expressed in an unclear way (sections 305c and 307 of the German Civil Code).[195] In this respect, the legal principles expressed in the prohibition of certain clauses according to sections 308 and 309 of the German Civil Code must still be taken into account. If the relatively strict requirements of such

[192] *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 305 no. 13; *Ulmer/Habersack* in: Ulmer/Brandner/Hensen, AGB-Recht, 12th ed. (2016), § 305 no. 29; *Wolf* in: Wolf/Lindacher/Pfeiffer, AGB-Gesetz, 6th ed. (2013), § 305 no. 32.

[193] The *OLG Düsseldorf* subscribes to the majority view in legal literature, OLG Düsseldorf NJW 1994, 59.

[194] This has been discussed in particular with regard to standard business conditions in the construction business, but the same reasoning might be applied to master agreements such as the General Agreement. Please refer to: *Schlosser* in: Staudinger BGB (2006) § 305 no. 31 (*Schlosser* in: Staudinger BGB (2013) §°305 no. 31 has revised its view); *Schlechtriem* in: Festschrift für Konrad Duden (1977), p. 576 *et seq.*; *Sonnenschein,* NJW 1980, 1489, 1491 *et seq.*

[195] BGH NJW 2007, 3774; BGHZ 89, 363; BGHZ 90, 273.

provisions are not met, the standard business conditions concerned are null and void and the rules of statutory law apply. A severability clause replacing the invalid contractual provision with a contractual provision achieving an effect coming as close a legally possible to the effect of the invalid provision would be equally void.

The BGH has considered a provision according to which a transaction was specified as a fixed date transaction to be surprising and therefore invalid, even if it is used between entrepreneurs.[196] However, the decision of the BGH concerned a type of business in which fixed date transactions are unusual. The BGH explicitly leaves open the question whether the same would apply to fields of business where fixed date transaction are common.

Therefore, where the transactions entered into under the General Agreement do not qualify as fixed date transactions, Section 8 of the General Agreement would not be enforceable to the extent that the purchaser is entitled to damages without granting a grace period to the non-performing party.

(c) Enforceability of limitation of liability (Section 12 of the General Agreement),

(i) General Enforceability of Exclusion of Liability (Section 12.2 of the General Agreement)

Section 12.2 of the General Agreement limits the liability of each Party to gross negligence, intentional default or fraud of a Party or its employees, officers, contractors and/or agents used by such Party in performing its obligations under the General Agreement.

Section 12.2 of the General Agreement deviates from the statutory provisions of sections 276 and 278 of the German Civil Code, pursuant to which a party to a contract is liable for any negligence (not only gross negligence) or wilful act of

[196] BGHZ 110, 88, 97 = NJW 1990, 2065, 2067; BGH NJW 1986, 842, 843 *et seq.*; *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 309 no. 23; *Wurmnest* in: Münchener Kommentar zum BGB, 7th ed. (2016), § 309 N. 4 no. 14; *Schäfer* in: Ulmer/Brandner/Hensen, AGB-Recht, 12th ed. (2016), § 309 Nr. 4 no. 11; *von Westphalen* in: Löwe/Graf v. Westphalen/Trinkner, AGB-Gesetz, 2nd ed. (1983), § 11 Nr. 4 nos. 25, 26; *Dammann* in: Wolf/Lindacher/Pfeiffer, AGB-Recht, 6th ed. (2013), § 309 Nr. 4 no. 62.

itself, its agents and other persons used by such party in performing its obligations under a contract.

A limitation of liability is generally permissible. However, the exclusion of liability in Sections 12.2 and 12.3 of the General Agreement has to comply with sections 305 to 310 of the German Civil Code if the General Agreement qualifies as standard business conditions within the meaning of those provisions. Please refer to Paragraph 6.3.15 below for a general discussion of the application of German requirements on standard business conditions.

Presuming the applicability of sections 305 *et seq.* of the German Civil Code with respect to the General Agreement, the limitation of liability in Section 12.2 of the General Agreement would, in principle, meet the above-mentioned requirements and would therefore be enforceable as, according to Section 12.4 of the General Agreement, such limitation of liability does not apply to the violation of a Party's fundamental contractual obligations (*Kardinalpflichten*).[197]

(ii) Enforceability of limitation of consequential damages and similar types of liabilities (Section 12.3 and Section 12.4 of the General Agreement)

The limitation of consequential damages as set forth in Section 12.3(a) of the General Agreement would be considered as overly disadvantageous within the meaning of section 307 of the German Civil Code and therefore be void. According to German court decisions and legal literature, any exclusion of liability violates section 307 of the German Civil Code where such exclusion also covers damages from the violation of obligations which are typical for the contractual relationship or which are predictable.[198]

As Section 12.3(a) of the General Agreement covers all indirect and/or consequential damages irrespective whether or not such damages are typical for the contractual relationship or predictable, Section 12.3(a) of the General Agreement would not comply with section 307 of the German Civil Code and would be void.

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[197] BGHZ 89, 367; BGHZ 93, 29, 48; BGH NJW 1993, 335; *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 307 no. 33.

[198] BGH NJW-RR 2001, 342; BGH NJW 1993, 335; BGH NJW 2001, 292, 295; BGHZ 138, 118, 133; *Grüneberg* in: Palandt BGB, 76th ed. (2017), § 309 no. 48.

The limitation of liability to an amount equal to the amounts payable for electricity supplied or to be supplied by a Party as set forth in Section 12.3(b) of the General Agreement may be void for similar reasons.

(iii) Enforceability of Duty to Mitigate (Section 12.5 of the General Agreement)

The duty to mitigate damages corresponds to a similar concept of German civil law (section 254 para 2 of the German Civil Code) and insofar does not alter substantial principles of German law (for details regarding the enforceability of Exclusion of Liability please see our answer to Paragraphs 5.4.1(c)(i) and 5.4.1(c)(ii) above).

(iv) Could the limitations and exclusions under this provision be further expanded or strengthened under the law of your jurisdiction?

Please see our answers under Paragraphs 5.4.1(c)(i) and 5.4.1(c)(ii) above.

(d) Any other provisions which need to be commented on according to the law of Germany, including whether these provisions could be further expanded or strengthened under the laws of your jurisdiction.

(i) There is a general risk that that these provisions may qualify as standard business conditions and may be invalidated (see Paragraph 5.4.1(b)(ii)(B) above). However, such risk generally exists with respect to clauses qualifying as standard business conditions and it is not uncommon to see such or comparable provisions applied by parties.

(ii) In any proceedings taken in Germany for the enforcement of the obligations under the General Agreement, the German courts would recognise the choice of English law to govern the General Agreement, Annexes and Individual Contracts, subject in each case to the provisions of the Rome I Regulation.[199]

Where the result of the application of a foreign law contradicts the fundamental idea of the corresponding German legal provisions and the understanding of righteousness of the German public in a way that the application of such foreign law

[199] With respect to agreements entered into prior to 17 December 2009 the 1980 Rome Convention applies which contains a conflict of law rule (Article 7 section 2 of the 1980 Rome Convention) that corresponds to that set forth in Article 9 para 3 of the Rome I Regulation.

is to be considered unbearable, a German court would not apply such foreign law contravening the German *ordre public*.[200] The application of *ordre public* is, however, subject to strict rules [201] and, if governed by a law different from German law, Sections 7, 8, and 12 of the General Agreement should not contravene the German *ordre public*.

However, whether or not the *ordre public* is infringed depends on the circumstances of the specific case with a view to all aspects of the relevant foreign law, the application of which is to be considered.

5.4.2 *Do you have other recommendations going to the topic of general legal enforceability that you would like EFET members to consider?*

We recommend to conduct authority and capacity checks for each counterparty to ensure that the counterparty has obtained all authorisations required to enter into the relevant transaction (for example, board resolutions) and that the signatory is authorised to sign the relevant transaction on behalf of the counterparty. If an advisory relationship exists with the relevant counterparty, it is necessary to observe the general regulatory requirements applicable to investment advice and the obligations applicable in case of an advisory relationship (*anleger- und objektgerechte Beratung*). Payment of provisions, fees etc. may be subject to disclosure requirements or other restrictions.

5.5 Confirmation Practice

5.5.1 Additional Assumptions

In this Paragraph 5.5 as instructed, we furthermore assume that as far as the confirmation practice is concerned, when entering into an Individual Contract, the counterparties in each case (i) make oral reference to the General Agreement when concluding the relevant Individual Contract over the phone and (ii) refer to the General Agreement when subsequently exchanging confirmations or similar electronic, written or non-verbal means of entering into or confirming Individual Contracts (in whichever form, including telex, telefax, SWIFT, electronic confirmation or position matching service or other means of electronic transmission).

Parties may or may not (i) use the EFET Electronic Confirmation Matching System (EFET eCM) to electronically match and exchange Confirmations or (ii) enter into the EFET Electronic Confirmation Agreement. We do not opine on any related regulatory obligations.

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200 BGHZ 50, 370, 375; BGH ZIP 1992, 1256, 1264.

201 See for example OLG Köln VersR 2007, 553 *et seq.* on an exclusion of liability under the laws of Taiwan even for cases of gross negligence not contravening the German *ordre public*.

5.5.2 Binding Individual Contract

(a) *Does the formation of a legally binding and enforceable Individual Contract require any formal act (e.g., execution in writing, signature, registration or notarisation)?*

If governed by German law despite the provision of Section 23.3 of the General Agreement, Individual Contracts may be concluded orally in accordance with Section 3.1 of the General Agreement unless otherwise agreed between the Parties. Under German law, no specific formal requirements, such as a notarisation requirement, do generally apply.

Pursuant to Section 3.2 of the General Agreement, a written confirmation of the Parties' understanding of the agreed terms of an Individual Contract that is not concluded in written form qualifies as Confirmation.

According to our interpretation of Section 3.2 of the General Agreement, the Parties have agreed on producing a written document for merely evidentiary purposes. The Confirmation sets out in writing the contents of an Individual Contract that has already (i.e. prior to the drafting of the Confirmation) been concluded orally. For merely evidentiary purposes, however, any conceivable text version that is suitable for documentary evidence and that can be permanently stored – including e-mails and telefaxes would suffice.

We understand that the EFET Electronic Confirmation Matching System (EFET ECM) is an electronic system by which confirmations can be matched electronically. We further understand that for this purpose, EFET has provided communication standards which are to be used in such matching process. According to our interpretation of Section 3.2 of the General Agreement, the parties may agree on the use of certain communication standards to be used for the electronic matching of confirmations by signing the EFET Electronic Confirmation Agreement.

Unless otherwise agreed between the Parties, there is no general requirement under German civil law to execute documents in written form. However, in case a Party is a German entity established under public law, such party may be obliged under applicable law, to enter into the General Agreement or any Confirmation thereunder in written form.

If the Parties to the General Agreement do not concur with our interpretation of Section 3.2 of the General Agreement and, instead, would only be satisfied with a Confirmation that complies with the more stringent written signature requirements, it would be recommendable to specify the agreed-upon formal requirements in more detail and, in particular, to include an explicit reference to a (handwritten) signature. It is further recommendable to include in Section 3.2 of the General Agreement a reference to the EFET Electronic Confirmation Matching System and the EFET Electronic Confirmation Agreement as a means of confirming a transaction.

(b) *At what point in time does an Individual Contract agreed upon orally become legally binding or enforceable?*

An Individual Contract is legally enforceable once agreed upon orally. However, the Parties may be required to provide documents in writing following the conclusion of the contract for evidential purposes (see our answer under Paragraph 5.5.2(c) below).

(c) *Does failure to object to incorrect terms in a received Confirmation constitute "acceptance" of those terms? If so, is there a relevant time period?*

Since the Parties will have entered into the Confirmation already orally, a written Confirmation pursuant to Section 3.2 of the General Agreement sent to either counterparty after the oral conclusion of the agreement in principle does not alter or amend such agreement and would merely be of declaratory nature.

However, pursuant to the German law doctrine of a commercial letter of confirmation *(kaufmännisches Bestätigungsschreiben)* – which, in the absence of a deviating agreement between the Parties or a different commercial practice in gas trading, would most likely also apply here – the terms stipulated in such commercial letter of confirmation will prevail. The Confirmation pursuant to Section 3.2 of the General Agreement will qualify as a commercial letter of confirmation if it states that an agreement has been reached orally and that the terms of such agreement are confirmed in such letter.

If such Confirmation qualifies as a commercial letter of confirmation and its terms deviate from the content of the terms agreed orally, the provisions contained in the Confirmation will generally prevail if the recipient remains silent,[202] *i.e.* does not object immediately.

This may apply even if the party which sends the Confirmation requests the recipient to countersign, because the sender of the Confirmation may request the countersignature only for evidentiary purposes.[203]

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202 BGHZ 7, 187, 189; BGH WM 2007, 303, 305.

203 BGH WM 2007, 303, 305; BGH NJW 1964, 1269, 1270.

Thus, the terms of the Confirmation are deemed to be accepted, unless the recipient objects immediately, that is without undue delay (*unverzüglich*) within the meaning of section 121 of the German Civil Code. The time frame allowed thereunder depends on the usual time in which a counterparty can be expected to review and react to a confirmation. General court decisions – which, however, do not specifically deal with commodity contracts in natural gas trading – allow for one to three business days;[204] however, an objection within an even shorter period of time might be required in the specific context of commodity trading, in particular where performance under the contract must commence within a short period of time.

The aforementioned principles do not apply if the party sending the Confirmation knows that the Confirmation is incorrect,[205] or if the Confirmation deviates from the orally agreed terms to such an extent that the silence on behalf of the recipient cannot reasonably be construed as a consent to such terms.[206]

(d) *Is the reference to the relevant General Agreement sufficient for the inclusion of the Individual Contract in the General Agreement?*

In the event the Parties to the General Agreement enter into an Individual Contract orally (such as over the telephone), or otherwise (e.g., through an electronic trading or matching system), and make reference to it being an Individual Contract for the purpose of the General Agreement between the Parties and assuming that the Individual Contract and the General Agreement are governed by German law, such Individual Contract would be validly included in the General Agreement as we understand that the Parties intend to include such Individual Contract under the General Agreement and the Parties' corresponding agreement should prevail over the terms of the General Agreement.

Assuming the Individual Contract is not governed by German law, under German conflict of law rules, the law governing the relevant Individual Contract and the General Agreement would also determine the circumstances under which such Individual Contract may be included in the General Agreement.

Subject to the above an Individual Contract is also validly included in the General Agreement if the Parties orally enter into such Individual

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[204] BGH NJW 1962, 246, 247; BGHZ 70, 232, 234.

[205] *Schmidt* in: Münchener Kommentar zum HGB, 3rd ed. (2013), § 346 no. 162; BGH WM 1955, 1284.

[206] *Schmidt* in: Münchener Kommentar zum HGB, 3rd ed. (2013), § 346 no. 163; BGH NJW 1954, 105, 105; BGHZ 40, 42, 45; BGHZ 101, 357, 365 = NJW 1988, 55, 57; BGH NJW-RR 2001, 680, 681; BGH NJW 1994, 1288.

Contract without any reference to the General Agreement between them, but subsequently confirm the Individual Contract in writing, via telex, facsimile, SWIFT, or other means of electronic transmission by using one of the sample Confirmations attached to the General Agreement as Annex 2a to 2d or by otherwise referring to the Individual Contract as a Individual Contract for the purposes of the General Agreement between the Parties.

5.5.3 **Means of Evidence**

Assuming there is a dispute with respect to the existence or the terms or conditions of an Individual Contract, would any or all of the following be eligible for rendering or otherwise properly introducing evidence of the agreed terms of the Individual Contract in court: (i) taped recording; (ii) witness' statement; (iii) e-mail or other electronic message or transaction entry system; and/or (iv) facsimile? Are there any local requirements or other considerations that are relevant to each form of evidence?

(a) Taped recording

Under German law, the recording of telephone conversations is generally not permissible without the consent of the all participants of the conversation. According to section 201 para 1 of the German Criminal Code (*Strafgesetzbuch*), it is a criminal offence to unlawfully record conversations, to use such recordings or to make such recordings available to third parties. This offence is punishable by imprisonment not exceeding three years or a fine. Furthermore, such recordings may also breach contractual obligations and duties and may also constitute a breach of the obligations assumed as an employer *vis-à-vis* the employees who have not consented to the recording. Subject to narrow exceptions, recordings which have been illegally obtained without the consent of the participants of the conversation may not be produced as evidence in civil actions.[207]

However, it is permissible to seek and obtain consent prior to the recording of telephone conversations. For this purpose, each participant of the conversation (*i.e.* the employee and the external customer) has to consent to the recording as well as to its use for evidentiary purposes and its disclosure to third parties. The recording Party may submit that its employees have given their consent[208] and

[207] BGHZ 27, 284; BGH NJW 1982, 277, 278; BGH NJW 1988, 1016; OLG Hamm NJW-RR 1996, 735. Similar principles have been developed in connection with witness evidence of third persons who listened to telephone conversations as requested by one participant without disclosing their attendance to the other participants, BVerfG NJW 2002, 3619, 3622 *et seq.*; BGH NJW 2003, 1727, 1729.

[208] The German Central Credit Committee (*Zentraler Kreditausschuss*) has agreed with the BaFin, the *Deutsche Bundesbank* and the German Association of Employers in the Private Banking Industry (*Arbeitgeberverband des privaten Bankgewerbes*) on a concept which serves as a framework for the recording of telephone conversation in the interbank trading business. Based on this concept, the

generally rely on such representation. In this context, it is of high importance to obtain the consent in writing, as section 4a para 1 sent. 3 of the Federal Data Protection Act (*Bundesdatenschutzgesetz*) allows other forms of consent only if warranted by special circumstances.

From a technical point of view, in order to comply with the restrictions under German law, *i.e.* to record only those conversations for which consent has been given, a specific telephone system would be required. This system would have to identify incoming calls and to route them depending on whether the caller is identified as having consented to the recording of its conversations or not. In the first alternative, the conversation can be recorded (and later submitted in court), whereas recording is not allowed in the second alternative due to the absence of consent.

(b) Witness statement; e-mail or other electronic message or transaction entry system; facsimile

Witness statements, e-mails or other messages derived from electronic message or transaction entry systems and facsimiles are eligible for rendering or otherwise properly introducing evidence of the agreed terms of the Individual Contract in court.

As far as electronic communication of employees is concerned, employers should ask their employees to consent in writing to the monitoring of their business e-mails and – if necessary – to their use as forensic evidence (subject to compliance with specific data protection requirements). Thus, the risk that German law enforcement authorities raise allegations in connection with sections 43 and 44 Federal Data Protection Act (unlawful violations of provisions of the Federal Data Protection Act) can be mitigated.

Under the German Code of Civil Procedure (*Zivilprozessordnung*), all forms of admissible evidence are of equal rank.[209] The court has to assess, based on the entire content of the court proceedings and all evidence submitted, whether a Party's submission (*e.g.* regarding the agreed terms of the Individual Contract) is proven or not.

Grundsatzvereinbarung dated February/March 1993 for interbank business on the recording of telephone conversations relating to cash, foreign exchange, securities and derivatives trading has been signed. Under this *Grundsatzvereinbarung*, German credit institutions, on the one hand, have obliged themselves to inform their counterparties about the intended recording and, on the other hand, to obtain consent from all employees of their trading departments. After such consent has been given, telephone conversations can be recorded. This *Grundsatzvereinbarung* is, however, limited in its scope. It applies only to the banks which are members of the said associations. So far, it has not been extended in scope by an agreement with other counterparties. Furthermore, it applies only to telephone conversations in the trading area of a bank.

[209] *Prütting* in: Münchener Kommentar zur ZPO, 5th ed. (2016), § 286 no. 13.

Regarding this assessment, the German courts are not limited to prescribed methodologies or types of evidence (*Grundsatz der freien Beweiswürdigung*) pursuant to section 286 of the German Code of Civil Procedure.

However, if a piece of evidence was obtained unlawfully, it may not be admissible in court. This applies usually and subject to only few exceptions in connection with violations of privacy. In this case, the right of privacy is violated not only by taking the evidence unlawfully, but also by presenting it in court and thus additionally disclosing the sensitive information to third parties.

5.6 Core Provisions

5.6.1 *Would any of the elections contemplated by the General Agreement or any of the above Annexes (including the Credit Support Annex) change the substance of your conclusions reached under Paragraph* 5.1 *and Paragraph* 5.2.? *As far as the Credit Support Annex is concerned, you should in particular discuss the effect of electing to allow substitution with or without consent.*

In the Election Sheet to the General Agreement the parties to the General Agreement may agree on a customisation of provisions in the General Agreement and include additional provisions to the General Agreement. If the General Agreement is governed by German law (please refer to Paragraph 5.2.1), whether such elections and additional provisions change the substance of our conclusions reached under Paragraph 5.1.1 and Paragraph 5.1.2, depends on the contents of such elections and additional provisions. Generally, such elections and additional provisions should not affect the conclusions reached under Paragraph 5.1.1 and Paragraph 5.1.2 regarding the enforceability of close-out netting provided that such inclusion would not have the effect of modifying or affecting the operation or implementation of any Core Provision (as defined in Paragraph 5.6.2).

Clause 6 of the Credit Support Annex provides that "Subject to the approval of the Transferee (not unreasonably to be withheld), the Transferor may replace, in whole or in part, any Eligible Credit Support provided under this Annex by Eligible Credit Support of the same or higher Value. The Transferee has no obligation to transfer the Eligible Credit Support which it holds until it has received the replacement Eligible Credit Support."

If the parties agree to modify this provision and to allow an exchange of Eligible Credit Support without the approval of the Transferee (such modification may be implemented in section 14.12 (Additional Provisions) of the Credit Support Annex), the substance of our conclusions reached under Paragraph 5.1 and Paragraph 5.2 would not change. However, we refer to our comments on the validity of *in rem* transfers in Paragraph 5.3.2(d) above.

5.6.2 *Considering your conclusions reached under Paragraph* 5.1.1 *and Paragraph* 5.1.2, *what are the provisions of the General Agreement that you regard as so essential that a material alteration thereof could affect the conclusions reached in that Paragraph* 5.1.1 *and Paragraph* 5.1.2 *(each such provision a "**Core Provision**")?*

We understand that "**Core Provisions**" are such provisions of the General Agreement which are so essential that a material alteration thereof could affect the enforceability of the contractual close-out netting as achieved by the Netting Provisions.

Following such understanding and subject to the opinions given in Paragraph 5.1.1 above, the assumptions set out under Paragraph 4 and the reservations set out under Paragraph 6, we identify the following provisions of the General Agreement as Core Provisions:

(a) Section 1.1 (*Subject of the Agreement*) of the General Agreement;

(b) Section 8 (*Remedies for Failure to Deliver and Accept*) of the General Agreement;

(c) Section 10.3 (*Termination for Material Reason*) of the General Agreement;

(d) Section 10.5 (c)(*Winding-Up/Insolvency/Attachment*) sub-clause (iv) of the General Agreement;

(e) Section 11 (*Calculation of the Termination Amount*) of the General Agreement; and

(f) all defined terms relevant for these provisions, in particular contained in Annex 1 to the General Agreement and related to the Sections of the General Agreement as set out under Paragraph 5.6.2(a) through (e) above.

A modification to any provision of the General Agreement that is not a Core Provision would generally not affect the conclusions reached in Paragraph 5.1.1 above5.1.1(c) regarding the enforceability of close-out netting provided that such modification would not have the effect of modifying or affecting the operation or implementation of any Core Provision.

An inclusion of Additional Provisions in the Election Sheet to the General Agreement should not affect the conclusions reached in Paragraph 5.1.1 above regarding the enforceability of close-out netting provided that such inclusion would not have the effect of modifying or affecting the operation or implementation of any Core Provision.

5.6.3 *Would the inclusion of the General Agreement in the EFET Cross Product Payment Netting Agreement or in the CPMA Cross-Product Master*

*Agreement (as amended by the EFET/IECA Commodities Schedule to the Cross-Product Master Agreement) (the "**CPMA**") change the substance of your conclusions reached under Part C.I or C.II such as, but without limitation, by invalidating the netting provisions in the EFET General Agreement due to its inclusion under the broader netting provisions of the CPMA?*

As set out in our opinion issued in connection with the Master Netting Agreement published by EFET in June 2010 and the Bond Market Association's Cross Product Master Agreement as modified by the EFET/IECA European Commodities Schedule and the Cross Product Credit Support Annex thereto, dated 29 April 2015, in particular in paragraphs 5.5.2 thereof, the General Agreement can be validly included. For more details please refer to our afore-mentioned opinion.

5.7 Governing Law, Arbitration and Jurisdiction

5.7.1 *Would the Parties' agreement on the governing law, submission to arbitration or jurisdiction (Section 22 of the General Agreement) be upheld in Germany, and what would be the consequence if it were not?*

(a) Governing law

The choice of German or English law to govern the General Agreement (Section 22.1 of the General Agreement) would, as a matter of contract law, be recognised under the laws of this jurisdiction, even if the Parties are not incorporated, domiciled or established in this jurisdiction, in accordance with Article 3 para 1 of the Rome I Regulation.[210]

Regarding the Parties' agreement on the governing law, see further Paragraph 5.1.1(i)(i).

(b) Recognition of arbitral award

An arbitral award on a civil matter rendered on the basis of the arbitration clause contained in the General Agreement will be recognised by a German court in accordance with sections 1059 *et seq.* of the German Code of Civil Procedure. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked,

[210] Rome I applies to contracts concluded on or after 17 December 2009 (Article 28 of Rome I as amended by the corrigendum published in OJ No L 309 of 24 November 2009, p. 87).

in case of a German domestic arbitral award only if that party furnishes proof that

(i) the parties to the respective contract were, under the applicable law, under some incapacity, or the arbitration clause under the respective contract was not valid under the law to which the parties have subjected it, or, failing any indication thereof, under German law; or

(ii) the party against whom the award is invoked was not given proper notice of the appointment of the arbitral tribunal or of the arbitration proceedings or was otherwise unable to present its case; or

(iii) the award is about a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognised and enforced; or

(iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the arbitration clause under the respective contract, or, failing such agreement, was not in accordance with German law, and it can be assumed that such deficiency influenced the award;

or if the German court finds that

(v) the subject matter of the dispute is not capable of settlement by arbitration under German law; or

(vi) the recognition or enforcement of the award would be contrary to the German *ordre public*;

or, in case of a foreign arbitral award, any grounds for refusal of recognition and enforcement under the United Nations Convention on Recognition and Enforcement of Foreign Arbitral Awards apply.

An order for the enforcement of a foreign arbitral award on a civil matter will be issued by a German court provided that the aforementioned requirements for recognition are met and provided further that the party interested in the enforcement has filed for enforcement of the arbitral award with the competent court in Germany in compliance with applicable legal requirements for such filings, including but not limited to the submission of the relevant documentation.

5.8 Regulatory Regime

5.8.1 *Are there any exchange control laws or licence requirements (under, e.g., any banking, securities trading or energy law) that may affect the enforceability of the relevant General Agreement or of the Individual Contracts?*

(a) Any currency or exchange control laws which may affect the General Agreement

Any transfer of rights or payment in respect, or other performance~~,~~ of an obligation under the General Agreement involving the government of any country which is currently the subject of United Nations or European Union sanctions, any person or body resident in, incorporated in or constituted under the laws of any such country or exercising public functions in any such country or any person or body controlled by any foregoing or by any person acting on behalf of any of the foregoing may be subject to restrictions pursuant to such sanctions as implemented or applicable in Germany. In exceptional cases restrictions may also be imposed by the EU member states, in Germany by the Federal Ministry for Economic Affairs and Energy (*Bundesministerium für Wirtschaft und Energie*).

In respect of cross-border cash payments the notification requirements under the German Foreign Trade Act (*Außenwirtschaftsgesetz*) and the German Foreign Trade Regulation (*Außenwirtschaftsverordnung*) need to be observed. Any transfer of more than EUR 12,500 or the equivalent amount in other currency must be notified to the *Servicezentrum Außenwirtschaftsstatistik* in Mainz, which is the competent federal office of *Deutsche Bundesbank* (the German Central Bank) for such notifications in Germany. A failure to do so would, however, not endanger the validity of the respective transaction.

(b) Energy law licence requirements

(i) Wholesale trading of natural gas

REMIT provides for a registration requirement for all market participants which are obliged to report trade information. The reporting obligations are laid down in Article 8 of the REMIT and specified in the Implementing Regulation (EU) No 1348/2014 of 17 December 2014 on data reporting ("**Implementing Regulation**"). The Implementing Regulation contains a list of reportable contracts that have to be reported since 7 October 2015, partly as from 7 April 2016 (Article 3 of Implementing Regulation).

The registration and reporting requirements apply to all market participants defined as any person, including transmission system operators, who enters into transactions, including the placing of orders to trade, in one or more wholesale energy markets qualifies as a "market participant" (Article 2 para 7 of the REMIT). "Wholesale energy markets" include any market within the EU on which wholesale energy products are traded (Article 2 para 6 of the REMIT). "Wholesale energy products" means the following contracts and derivatives, irrespective of where and how they are traded:

- contracts for the supply of electricity or natural gas where delivery is in the EU;
- derivatives relating to electricity or natural gas produced, traded or delivered in the EU;
- contracts relating to the transportation of electricity or natural gas in the EU; and
- derivatives relating to the transportation of electricity or natural gas in the EU.

Contracts for the supply and distribution of electricity or natural gas for the use of final customers are not wholesale energy products. However, contracts for the supply and distribution of electricity or natural gas to final customers with a consumption capacity greater than 600 GWh per year (Article 2 paras. 4 and 5 of the REMIT) are treated as wholesale energy products.

The registration has to be made with the national regulatory authority in the EU member state in which the respective market participants are established or resident or, if they are not established or resident in the EU, in a member state in which they are active. In Germany, the Federal Network Agency (*Bundesnetzagentur*, "**BNetzA**") is the competent national regulatory authority for registration purposes.

In December 2012, the German Parliament (*Bundestag*) passed a Law on the Establishment of a Market Transparency Unit for the Wholesale of Gas and Electricity (*Gesetz zur Einrichtung einer Markttransparenzstelle für den Großhandel mit Strom und Gas*). This law, *inter alia*, provides for an obligation to report trade information for all market participants. It also introduced penalties and fines for violating REMIT.

(ii) Transportation of natural gas

With respect to the German Energy Industry Act (*Energiewirtschaftsgesetz*), only a grid operator would need a licence if it, for the first time, intends to commence operating a grid. In addition, the Energy Industry Act provides for a certification procedure for transmission system operators (four in Germany). Already these regulations show that the Energy Industry Act in the first place contains obligations respectively provisions with respect to grid operators.

(iii) Supply of natural gas to household customers

However, pursuant to section 5 sent. 1 of the Energy Industry Act, energy supply companies who – for the first time – intend to supply household customers with energy (electricity or gas) or terminate such a supply need to notify their activities to the regulatory authority (*Lieferantenanzeige*). According to section 3 no. 22 of the Energy Industry Act household customers are end customers who use the energy supplied for their own purposes within their own households or for the purpose of commercial use provided that the yearly overall consumption does not exceed 10,000 KWh. Only in cases where the above-mentioned prerequisites are met, a notification has to be issued. Thus, wholesale traders – defined in section 3 no. 21 of the Energy Industry Act as natural or legal persons buying energy for resale purposes excluding grid operators – do not have to file a notification.

The BNetzA is the responsible regulatory authority pursuant to section 54 para 1 and 2 of the Energy Industry Act. The BNetzA will publish a list of such undertakings on its website providing the name and address of the single companies that have notified the delivery of energy in accordance with section 5 sent. 1 of the Energy Industry Act. When notifying the business, a company is required to give proof of the personal, technical and economical capability and the reliability of its management (section 5 sent. 3 of the Energy Industry Act). The BNetzA is entitled to prohibit the activity if it deems that the personal, technical and economic capability of the undertaking or the reliability of its management is not guaranteed (section 5 sent. 4 of the Energy Industry Act). However, section 5 sent. 3 and 4 of the Energy Industry Act do not apply in case the energy supply company holds a supply permit granted by another Member State of the European Union (section 5 sent. 5 of the Energy Industry Act).

(iv) Registration and submission of information to the BNetzA for the market master data register (*Marktstammdatenregister*)

From 1 July 2017 onwards, participants to the German energy market, inter alia those market participants within the scope of Article 8 of the REMIT (see Paragraph 5.8.1(i) above) which file a REMIT registration with the BNetzA are also obliged to registration at the market master data register administered by the BNetzA. The information to be submitted with the registration is listed in an annex to the Ordinance on the Registration of Energy Industry Data (*Verordnung über die Registrierung energiewirtschaftlicher Daten*) comprising, inter alia, general information about the market participant (e.g. name, address, legal form as well as start and end date of the market activity) as well as information with regard to the relevant gas supply locations (e.g. name of the gas grid connection point (if applicable) as well as the relevant market area).

(c) Other permits and requirements

Persons who have their corporate seat in Germany and want to (i) deliver natural gas, (ii) use natural gas in Germany which has been produced by themselves or (iii) procure natural gas from providers domiciled outside Germany for use inside Germany have to notify the respective intent to the competent main customs office (*Hauptzollamt*) pursuant to section 38 para. 3 of the German Energy Tax Act (*Energiesteuergesetz*).

Energy trading activities are not subject to any permit requirements under trade law. It is merely stipulated in section 14 para 1 sent. 1 of the Trade Code (Gewerbeordnung) that a notice of commencement of trade (Gewerbeanzeige) must be filed, i.e., that the relevant trade or business must be registered. in the event that the relevant trade or business is established within Germany

(d) Licence requirements under the Greenhouse Gas Act[211]

With respect to Emissions Trading no licence or permit is required under the Greenhouse Gas Act (*Treibhausgas-Emissionshandels-gesetz*), unless the supplier itself is operating a facility that emits greenhouse gases. In the latter case, a permit pursuant to section 4 of the Greenhouse Gas Act is required. This permit is usually contained in the permit for emissions protection for existing facilities granted prior to 1 January 2013 under the Federal Emissions Protection Act

[211] With respect to the auction of allowances and any licence requirements please refer to section 8 of the Greenhouse Gas Act.

(*Bundes-Imissionsschutzgesetz*). In case such a facility is commissioned on or after 1 January 2013, a permit pursuant to section 4 of the Greenhouse Gas Act is required in addition to the permit for emissions protection under the Federal Emissions Protection Act. However, as permits for emissions protection under the Federal Emissions Protection Act have a "concentration effect", a licensing decision under the Federal Emissions Protection Act comprises all other necessary permits (including the permit pursuant to section 4 of the Greenhouse Gas Act), i.e. only a single overarching permitting decision is required.

In order to merely trade in allowances within the German Emissions Trading Scheme it is required to set up an account for the allowances according to section 17 of the Greenhouse Gas Act with the Union Registry pursuant to Directive 2003/87/EC of the European Parliament and of the Council, Decisions No. 280/2004/EC and No 406/2009/EC of the European Parliament and of the Council.

(e) Licence requirements under the Banking Act

Any person who intends to conduct banking business or to provide financial services in Germany[212] commercially or on a scale which requires a commercially organised business undertaking needs to be licensed by the BaFin pursuant to section 32 of the Banking Act.

Banking business comprises, *inter alia*, principal broking services (the purchase and sale of financial investment in one's own name but for the account of others, *i.e.* commission agency business regarding financial instruments).

Financial services comprise, *inter alia*,

(i) the brokering of business involving the purchase and sale of financial instruments (investment broking – *Anlagevermitt-lung*);

(ii) the placing of financial instruments without a firm underwriting commitment (placement business – *Platzie-rungsgeschäft*);

[212] The territorial scope of the licence requirements under the Banking Act is limited to business performed or services provided "in Germany". With respect to cross-border business from EU/EEA countries into Germany, the European Passport system applies (section 53b of the Banking Act). With respect to cross-border business from non-EU/EEA countries into Germany, the BaFin has set forth its policy on the interpretation of this territorial scope of the Banking in its note of April 2005 regarding the licensing requirements pursuant to section 32 para 1 of the Banking Act in conjunction with section 1 paras. 1 and 1a of the Banking Act for conducting cross-border banking business and/or providing cross-border financial services.

(iii) the purchase and sale of financial instruments in the name of and for the account of others (contract broking – *Abschlussvermittlung*);

(iv) the administration of individual portfolios of financial instruments for others on a discretionary basis (portfolio management – *Finanzportfolioverwaltung*);

(v) either (a) the continued offer to sell or buy financial instruments on an organised market or multilateral trading facility with own pricing or (b) the frequent organised and systematic trading for own account outside an organised market or multilateral trading facility by offering a system accessible for thirds parties in order to enter into transactions with them or (c) the purchase and sale of financial instruments on an own-account basis for others or (d) the purchase and sale of financial instruments on an own-account basis as a direct or indirect participant of a domestic regulated market or a multilateral trading facility by using an algorithmic high frequent trading technique characterised by the use of infrastructures which are aimed at minimising latency time by the decision of the system on the initiation, creation, forwarding or execution of a instruction for transactions or orders without human intervention and characterised by a high intraday message volume in the form of instructions, quotes or cancellations, even if the trading activity is not performed as a service for others, (proprietary trading - *Eigenhandel*); and

(vi) the purchase and sale of financial instruments for own account, if such own account trading does not qualify as proprietary trading as set out in sub-Paragraph (v) above, ("true" proprietary trading – *Eigengeschäft*, as defined in section 1 para 1a of the Banking Act), if such true proprietary trading is conducted by an enterprise which is not a credit institution or a financial services institution and conducts such trading activity commercially or on a scale which requires a commercially organised business undertaking and belongs to a group of institutions (*Institutsgruppe*, as defined in section 10a para 1 of the Banking Act), a financial holding group (*Finanzholding-Gruppe*, as defined in section 10a para 1 of the Banking Act) or a mixed financial holding group (*gemische Finanzholding-Gruppe* as defined in section 10a para 1 of the Banking Act) or a financial conglomerate (*Finanzkonglomerat*, as defined in section 1 para 20 of the Banking Act), provided that a CRR credit institution (*CRR-Kreditinstitut*, as defined in section 1 para 3d of the Banking Act) forms part of such group or conglomerate.

(f) Financial Instruments

The term "financial instruments"[213] includes derivatives contracts. Derivatives (including swaps) are outright forward transactions or option contracts the price of which depends directly or indirectly on the exchange or market price of underlying assets such as, *inter alia*, commodities or precious metals (section 1 para 11 sent. 3 of the Banking Act). The definition of derivatives may include both contracts which provide for cash settlement and contracts which provide for physical settlement.

Section 1 para 11 sent. 3 no. 2 of the Banking Act provides that forward transactions (*Termingeschäfte*) with commodities as underlying qualify as derivatives, and therefore, also as financial instruments, if

(i) they are cash settled, or if one party has the right to demand cash settlement, even absent an event of default;

(ii) they are traded on a regulated market of a multilateral trading system;

(iii) they have the characteristics of other derivative financial instruments pursuant to Commission Regulation (EC) No 1287/2006 of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council (OJ L 241, page 1) and are not for commercial purposes and do not meet the requirements set out in Article 38 para 4 of such Regulation

and if they do not qualify as spot contracts pursuant to Article 38 para 2 of Commission Regulation (EC) No 1287/2006.

The Banking Act does not explicitly define cash settlement. However, the BaFin[214] takes into consideration both the

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[213] Please note that MiFID II broadens the scope of transactions qualifying as "financial instruments" which also has an impact on the corresponding licence requirements (subject to any available exemptions). Member states need to transpose MiFID°II by 3 July 2017 and the provisions are scheduled to apply as of 3 January 2018 (see http://ec.europa.eu/finance/securities/docs/isd/mifid/160210-directive-amending-mifid_en.pdf). MiFID II will be implemented in Germany under the second financial markets amendment law (*Zweites Finanzmarktnovellierungsgesetz – 2. FiMaNoG*), which has been adopted by the German Parliament (*Bundestag*) on 30 March 2017. Upon publication in the official journal (*Bundesgesetzblatt*), it will enter into force on 3 January 2018 (with the exception of certain provisions relating to amendments made in view of, *inter alia*, the SFTR which will apply earlier).

[214] BaFin, *Hinweise zur Erlaubnispflicht von Geschäften im Zusammenhang mit Stromhandelsaktivitäten* (Stand: Juni 2011) (Note on licence requirements for transactions in connection with power trading activities (as of June 2011)).

wording of the contract and the underlying economic interests of the parties. Besides transactions that apparently (and solely) aim at cash settlement (*offenes Differenzgeschäft*), there are transactions that are deemed by the BaFin to aim at cash settlement due to the respective circumstances of the conclusion of the contract (*verdecktes Differenzgeschäft*). With respect to power derivatives, the BaFin has taken the view that significant evidence for the intention of cash settlement are (i) the parties' incapacity to deliver or receive the previously specified amount of power, (ii) the lacking of a licence as an power supply company and (iii) a frequent replication of similar transactions. It is currently not entirely clear whether the BaFin will uphold these criteria in the future.

(g) Exemptions

The Banking Act exempts, *inter alia,* the following entities from the licence requirements:

(i) Entities which do not provide services for third parties, but whose business consists in providing investment services solely for their parent undertakings, for their subsidiaries, or for other subsidiaries of their parent undertakings (section 2 para 6 sent. 1 no. 5 of the Banking Act);

(ii) entities dealing on own account in financial instruments, or providing investment services in derivatives within the meaning of section 1 para 11 sent. 3 nos. 2 and 5 of the Banking Act (commodity derivatives), provided that

(A) they are not a member of a group the main business of which is the provision of investment services or banking services within the meaning of the Banking Act;

(B) the financial services are only ancillary services compared to the group's main business and

(C) the financial services are offered only to customers of their main business in connection with services constituting the group's main business (section 2 para 6 sent. 1 no. 11 of the Banking Act); and

(iii) entities whose main business is proprietary trading for others with regard to derivatives, whose underlying is a commodity, and the company does not belong to a group of companies whose main activity is the provision of investment services or banking business (section 2 para 6 sent. 1 no. 13 of the Banking Act).

(h) Emission rights

Pursuant to section 7 para 5 of the Greenhouse Gas Act, emission rights are explicitly not defined as financial instruments within the meaning of the Banking Act.[215] Thus, the purchase or sale of emission rights in the form of spot contracts with physical settlement – be it on an OTC-basis or in organised markets – is (in contrast to the trading of derivatives with emission rights as underlying) not subject to any banking licence requirements under German law. [216] However, derivatives with emission rights as underlyings qualify as financial instruments (section 1 para 11 sent. 3 no. 2 of the Banking Act). Thus, trading in such derivatives may require a licence pursuant to section 32 para 1 of the Banking Act if such trading activity qualifies as a banking business or financial service (please see Paragraph 5.8.1(e)).

5.9 Other Provisions

5.9.1 *Recommendations that you would like EFET member companies to consider (for example to fully optimise the General Agreement for a specific purpose such as to support limited trading between two entities both organised and doing business solely in Germany).*

(a) If any single section in the General Agreement were illegal or unenforceable, such unenforceability or illegality would, under the laws of Germany, not undermine the Netting Provisions, unless the unenforceability or illegality was so material that the General Agreement would not have been entered into if it had not contained these provisions (section 139 of the German Civil Code).

(b) The arbitration clause in Section 22.2 of the General Agreement should determine the place of arbitration.

We would further suggest to include the model arbitration clause of the DIS (German Institution of Arbitration) which reads as follows:

"*All disputes arising in connection with the General Agreement [and ancillary contracts] or its validity shall be finally settled in accordance*

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[215] Licensing requirements in respect of dealings in financial instruments under the Banking Act are to a significant extent based on MiFID II and a Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 ("**MiFIR**").

[216] BaFin, *Hinweise zur Erlaubnispflicht nach § 32 Abs. 1 KWG in Verbindung mit § 1 Abs. 1 und Abs. 1a KWG bei Geschäftstätigkeiten im Zusammenhang mit Emissionszertifikaten* (Stand: Juni 2011, zuletzt geändert am 3. Juli 2013) (Note on licence requirements in accordance with section 32 para 1 of the Banking Act in connection with section 1 paras. 1 and 1a of the Banking Act for transactions in connection with emission allowances (as of June 2011, amended on 3 July 2013)).

with the Arbitration Rules of the German Institution of Arbitration e.V. (DIS) without recourse to the ordinary courts of law. The place of arbitration is [•]. The number of arbitrators shall be three. The applicable substantive law shall be [German] law. The language of the arbitral proceedings shall be English, unless otherwise specified in the Election Sheet."

6. RESERVATIONS

6.1 General

6.1.1 In this Opinion "enforceable" or any word of similar import means that an obligation is of a type which the German courts generally enforce. It does not mean that those obligations will be enforced in all circumstances in accordance with the terms of the General Agreement. In particular the following has to be taken into account:

(a) Any enforcement of the General Agreement in Germany is be subject to the rules of civil procedure arising by operation of law as applied by the courts or other competent authority of Germany which may, *inter alia*, require the translation of foreign language documents into the German language.

(b) In the event that an enforcement action is initiated in this jurisdiction in respect of a judgment in a foreign currency (including German court judgments rendered in connection with the enforcement of foreign court judgments) the sum claimed in such action may have to be converted in Euro.

6.1.2 A determination, designation, calculation or certificate by any Party to the General Agreement as to any matter provided for therein may, in certain circumstances, be held by a German court not to be final, conclusive and binding (for example, if it could be shown to have been incorrect or to have any other reasonable or arbitrary basis or not to have been made in good faith) notwithstanding the provisions of the General Agreement or Individual Contract.

6.1.3 A German court may refuse to give effect to any provision of the General Agreement (a) for the payment of expenses in respect of the costs of enforcement (actual or contemplated) of unsuccessful litigation brought before a German court or where the court has itself made an order for costs, (b) which would constitute an agreement to agree for the purposes of German law, (c) which would involve the enforcement of foreign tax or criminal laws, or (d) which would be inconsistent with German public policy.

6.1.4 If a party defaults on a payment obligation which expressly requires such party to make payment in an agreed currency and such requirement is expressed in a certain prescribed manner, the sum claimed in an enforcement action does not need to be converted into Euro at the time such action is filed; in such case, the claim may be discharged by converting the judgement currency into Euro at the exchange rate prevailing on the date of payment. However, with respect to bankruptcy, insolvency, liquidation, moratorium, reorganisation, reconstruction or similar proceedings, German law may require that all claims or debts are converted into Euro at an exchange rate determined by the court at a date related thereto, such as the date of the opening of Insolvency Proceedings.

6.1.5 Any action brought against any person in German courts will be subject to the rules and procedures of German courts, including the power of a German court to order a plaintiff in an action, being a party not ordinarily resident in Germany, to provide security for costs and to appoint a process agent (*Zustellungsbevollmächtigter)* in Germany.

6.1.6 The authenticity or completeness of any message or data in electronic form (even if saved on a medium of data storage), and therefore its evidential value, may in principle be challenged as not being solid and meaningful evidence in German courts on, *inter alia*, the grounds that (i) it may be altered and/or (ii) the sender thereof cannot be certified, and/or (iii) the date and time of its issue can be manipulated.

6.1.7 By virtue of section 2(b) of Article VIII of the International Monetary Fund Agreement, as interpreted and applied by German courts, an obligation which involves the currency of any member of the International Monetary Fund which is contrary to the exchange control regulations of that member may not be enforceable (*unklagbar*) in the German courts.

6.1.8 Any transfer of rights or payment in respect, or other performance, of an obligation under the General Agreement or any Individual Contract involving the government of any country which is currently the subject of United Nations or European Union sanctions, any person or body resident in, incorporated in or established under the laws of any such country or exercising public functions in any such country or any person or body controlled by any foregoing or by any person acting on behalf of any of the foregoing may be subject to restrictions pursuant to such sanctions as implemented in German law.

6.1.9 Pursuant to section 395 of the German Civil Code, a set-off against a claim of the Federal Republic of Germany, a German Federal State, a municipality or an association of municipalities (*Kommunalverband*) is only permissible if the performance is to be effected to the same fund (*Kasse*) from which the claim of the party which declares the set-off is to be paid.

6.1.10 We express no opinion on the enforceability of any guarantees or credit support (Section 16 of the General Agreement) or on the effectiveness of security provided under a request for a Performance Assurance (Section 17 of the General Agreement).

6.1.11 As set forth above in Paragraph 5.8.1(a), in respect of cross-border cash payments the notification requirements under the Foreign Trade Act and the Foreign Trade Regulation need to be observed. The reports have to be submitted to Deutsche Bundesbank using the applicable notification forms. Any omission of such notification may trigger an administrative fine (*Bußgeld*) under the Foreign Trade and Payment Regulation, but will neither affect the validity nor the enforceability of the respective transaction.

6.1.12 With respect to the doctrine of ultra vires, the capacity of a legal entity governed by public law to validly enter into a legally binding agreement may be limited under German law. Public law entities may principally only enter into transactions that fall within their scope of competence and functions (*Wirkungskreis*) as defined by a special law or bylaw enacted by a sovereign such as the Federal Republic of Germany or a Federal State. If a public law entity purports to enter into a contract under private law that is beyond or exceeding its statutorily specified powers, such a contract might be considered as ultra vires and therefore null and void. There is a risk that a court may decide that the concept of ultra vires is also applicable to municipalities. In contrast, the Federal States or the Federal Republic of Germany, when acting under private law, should not be restricted by the principle of ultra vires. Provided that the ultra vires doctrine is applicable, it applies regardless of the good faith of the counterparty or any representation to the contrary. As a rule, *ultra vires* measures are utterly unenforceable. They may not be ratified. Furthermore, no claims for damages might be raised either (for example, claims based on misrepresentation) and any collateral provided has to be returned.

6.1.13 Under German law, the Federal Republic of Germany, the Federal States, municipalities and public law entities in their capacity as party to the General Agreement do not enjoy an absolute right of sovereign immunity from legal proceedings, the execution of a judgment or an attachment. However, the procedural law provides for special provisions as regards legal proceedings against entities governed by public law and the execution of a judgement against such an entity might either be restricted or be subject to special requirements such as the consent of the supervisory authority.

6.1.14 We express no opinion as to whether any Party has complied with any applicable provisions of Title II 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 ("**EMIR**")[217] as amended, any delegated or implementing acts adopted under EMIR, the provisions of the Banking Act, the Securities Trading Act or the German Exchange Act (*Börsengesetz*) which were amended or enacted to implement EMIR, or any regulations adopted thereunder in respect of anything done by it in relation to or in connection with any of the Opinion Documents other than provisions on

[217] OJ No L 201 of 27 July 2012, p. 1.

which we expressly opine. However, Article 12 para 3 of EMIR provides that any infringement of the rules under Title II of EMIR "shall not affect the validity of an OTC derivative contract or the possibility for the parties to enforce the provisions of an OTC derivative contract", consequently any failure by a party to so comply should not make the General Agreement or the relevant Individual Contract invalid or unenforceable.

6.1.15 We express no opinions as to whether any party has complied with any applicable provision of Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012 ("**SFTR**").[218] Article 15 of the SFTR imposes obligations relating to rights of reuse where these are exercised. The SFTR has entered into force on 12 January 2016. Article 15 of the SFTR has taken effect from 13 July 2016 onwards.

6.1.16 We express no opinion on Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17EU and Regulation (EU) No 596/2014.[219]

6.2 Application of Foreign Law

6.2.1 If any obligation is to be performed in a jurisdiction outside Germany, it may not be enforceable in Germany to the extent that performance would be illegal or contrary to public policy under the laws of the other jurisdiction and a German court may take into account the law of the place of performance in relation to the manner of performance and to the steps to be taken in the event of defective performance.

6.2.2 Where the General Agreement is not governed by German law,

(a) A German court may give effect to mandatory provisions (i.e. provisions regarded as crucial for a country's safeguarding of its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the General Agreement or any Individual Contract (Article 9 para 1 of the Rome I Regulation) of the law of the country where the obligations arising out of the General Agreement or any Individual Contract have to be or have been performed, insofar as those overriding mandatory provisions render the performance of the contract unlawful (Article 9 para 3 of the Rome I Regulation).

[218] OJ EU No L 337 of 23 December 2015, p. 1.

[219] OJ EU No L 171 of 29 June 2016, p. 1

(b) A German court may apply the overriding mandatory provisions of German law (Article 9 para 2 of the Rome I Regulation) irrespective of the choice of foreign law in the General Agreement.

(c) A German court may refuse to apply the choice of law in the General Agreement if such application is manifestly incompatible with the public policy of Germany (Article 21 of the Rome I Regulation).

(d) A German court shall have regard to the law of the country in which performance takes place in relation to the manner of performance and the steps to be taken in the event of defective performance (Article 12 para 2 of the Rome I Regulation).

(e) Where all other elements relevant to the situation at the time that the General Agreement or any Individual Contract were entered into are located either in another state or in one or more EU member states, the relevant German court may apply the provision of such state's law or the law of the European Union (as the case may be), which cannot be derogated from by agreement (Article 3 paras. 3 and 4 of the Rome I Regulation).

6.3 **Reservations regarding Agreements governed by German Law**

6.3.1 The German law principle of *Treu und Glauben* (section 242 of the German Civil Code) requires that contracts are performed in good faith. Actions *contra bonos mores* may provide certain rights in favour of a contracting party or may render contracts or commitments void or voidable. In addition, public policy may lead to "equitable" rights being upheld in German courts or may render contracts or commitments void or voidable or may lead to the recharacterising of such contracts or commitments and German courts may declare provisions providing for strict liability invalid.

6.3.2 If a German court considers it impossible or unduly burdensome for obligations to be performed the debtor is discharged from performing such obligation; the debtor may however be held liable for damages.

6.3.3 In some circumstances, a German court will not give effect to any provision of the General Agreement which provides that, in the event of any invalidity, illegality or unenforceability of any provision of such General Agreement or omission therein the remaining provisions thereof are not affected or impaired or the omission will be corrected, particularly if to do so would not accord with public policy or would require that the court make a new contract for the parties or would contravene the intention of the parties to such General Agreement (i.e. the relevant court establishes that the parties would not have entered into the General Agreement without the illegal provision being agreed between them which may be found to be the case by the court under circumstances where the invalid, illegal or unenforceable provision is a material provision).

6.3.4 A German court might hold that, irrespective of the provisions of the General Agreement, any waiver of or amendment to the General Agreement agreed between the respective Parties is valid irrespective of whether it is given or made in writing or orally or implied by subsequent conduct of the relevant parties.

6.3.5 Claims may become time-barred under the German Civil Code or may be or become subject to the defence of set-off or to a counterclaim.

6.3.6 Where any person is vested with a discretion or may determine a matter in its opinion, German law may require that such discretion is exercised reasonably or that such opinion is based on reasonable grounds.

6.3.7 Under section 193 of the German Civil Code, unless the parties have agreed otherwise, any obligation which would have to be performed on a day which is an official holiday at the place where the performance has to take place, is to be performed instead on the next possible business day at such place.

6.3.8 Generally, a claim cannot be validly assigned under German law if the creditor and the debtor of the claim have contractually restricted the assignability of the claim. The assignment of a claim which contravenes a contractually agreed restriction on assignment will be invalid. However, under an exception contained in section 354a of the Commercial Code, the assignment of monetary claims (i.e. claims for the payment of money) governed by German law cannot effectively be contractually excluded if the underlying agreement constitutes a commercial transaction (*Handelsgeschäft*) for both contracting parties or if the debtor is a public law entity or public law fund (section 354a para 1 of the Commercial Code). Such monetary claims can be validly assigned notwithstanding a contractual restriction on assignment in the underlying contract, and, accordingly, notwithstanding that German courts would not enforce restrictions on the assignment of monetary claims to the extent to which section 354a para 1 of the Commercial Code provides that they are not enforceable, that same section allows the debtor of an assigned claim to pay and discharge its obligations to the original creditor, even if the debtor is notified of the assignment of its debt obligation. However, pursuant to section 354a para 2 of the Commercial Code, section 354a para 1 of the Commercial Code is no longer applicable to receivables resulting from a loan agreement which has been entered into after 18 August 2008 by a lender which is a credit institution.

From our point of view, the single agreement concept as set forth in Section 1.1 of the General Agreement would not constitute a statutory prohibition of assignment pursuant to section 399 of the German Civil Code pursuant to which the assignment of contractual rights is prohibited if such an assignment would lead to an alteration of the subject matter of the contract (section 399 alternative 1 of the German Civil Code). This provision applies primarily to contractual obligations the content of which is predominantly influenced by the person of the creditor such as personal claims or claims based on an agreement characterised by an exceptional amount of mutual trust which is not given under derivative transactions.

6.3.9 If any person expressed to be a Party to the General Agreement or an Individual Contract knew or should reasonably have known that any representation, warranty or statement in any General Agreement or Individual Contract was incorrect, inaccurate or incomplete or any covenant was or could reasonably be expected to be impossible to fulfil, such person will be limited in enforcing its rights under the General Agreement or under the Individual Contract.

6.3.10 Any provision of the General Agreement which constitutes, or purports to constitute, a restriction on the exercise of any statutory power by any Party or any other person may be ineffective.

6.3.11 Pursuant to section 248 of the German Civil Code (but subject to section 355 of the Commercial Code) any provision obliging a debtor to pay interest on interest (compound interest) is void. This provision renders void compound interest provided for in any General Agreement and all similar provisions in the General Agreement relating to default interest and indemnities in respect thereof. However, pursuant to section 289 of the German Civil Code, a debtor may be liable for damages incurred due to its late payment of interest. Such damages would have to be proven.

6.3.12 A German court might hold that any provision in the General Agreement stating that a representation or communication is deemed to have been made or delivered or which reverses the burden of proof is void or voidable.

6.3.13 A provision requiring a Party to represent that a General Agreement or Individual Contract is legal, valid and binding may be unenforceable to the extent that it applies to provisions of such General Agreement or Individual Contract which are not legal, valid and binding.

6.3.14 There is no final judicial precedent in Germany for holding facsimile or e-mail communications valid and binding in all circumstances (in particular where there is a statutory requirement for written form, a signature by way of a facsimile signing has been held insufficient to satisfy such requirement). Notwithstanding the foregoing, if there are no particular statutory or contractual requirements as to the form of communication (unless - in the latter case - the requirement of actual receipt has been validly waived), any communication actually received by the addressee will be deemed validly given (*widerlegbare Vermutung*).

6.3.15 **Standard Business Conditions**

The regulations on standard business conditions pursuant to sections 305 to 310 of the German Civil Code would apply in certain circumstances to the General Agreement or any Individual Contract (see Paragraph 5.4.1(b)(ii)(B) above). We would like to draw your attention in particular to the following specific aspects of these regulations on standard business conditions:

(a) The protection provided by sections 305 *et seq.* of the German Civil Code for the benefit of the counterparty of the user of standard business conditions (the "**Counterparty**") applies not only if the Counterparty is a consumer, but also if such Counterparty is an entrepreneur (*Unternehmer*); however, the standard of protection for entrepreneurs is not as high as the standard of protection provided to consumers;

(b) provisions contained in standard business conditions may be set aside by a court as invalid without a possibility to reduce its content to a valid provision, pursuant to sections 305b to 307 of the German Civil Code, if they are (a) surprising to the Counterparty (section 305c of the German Civil Code), (b) conflicting with a provision specifically negotiated with the Counterparty (section 305b of the German Civil Code), (c) intended to circumvent any provision contained in sections 305 to 307 of the German Civil Code (section 306a of the German Civil Code) or (d) contrary to good faith, inappropriately disadvantageous to the detriment of the Counterparty; in this respect the German Civil Code provides for an assumption that a standard business condition is (in particular without limitation) inappropriately disadvantageous to the detriment of the Counterparty if such provision contravenes the fundamental principles of a statutory provision from which it derogates or constrains fundamental rights and obligations which arise out of the specific nature of the respective contract in such a way that the achievement of the purpose of such contract is at danger (section 307 of the German Civil Code). However, although the main provisions on standard business conditions in sections 308 and 309 German Civil Code do not apply directly with respect to entrepreneurs, most infringements of the provisions contained therein count as an infringement of section 307 German Civil Code. Please note that the standard of good faith employed under section 307 of the German Civil Code is higher than the standard of good faith referred to in Paragraph 6.3.1 above;

(c) if a provision contained in standard business conditions is unclear, then such lack of clarity will be to the detriment of the user of the standard business conditions and not to the detriment of the Counterparty (section 305c para 2 of the German Civil Code);

(d) standard business conditions may be subject to a challenge by individual Counterparties or by way of class actions in German courts (including cease-and-desist claims brought by (qualified) third parties under the German Act on Injunctive Relief (*Unterlassungsklagengesetz*));

(e) where standard business conditions are in a language other than the German language and no German translation has been provided at the time when the Counterparty accepts such standard business conditions, or if standard business conditions are otherwise non-transparent, there is a possibility that German courts will set aside provisions which favour the party using such standard business conditions, in particular, on the basis of lack of transparency; and

(f) severability clauses (*salvatorische Klauseln*) in standard business conditions pursuant to which an invalid, illegal or unenforceable provision is to be replaced by the parties with a provision which comes as close as legally possible to the commercial intentions of the invalid, illegal or unenforceable provisions are invalid (section 306 para 2 of the German Civil Code).

7. ADDRESSEES AND PURPOSE

7.1 Clifford Chance Deutschland LLP hereby consents to members of EFET (the "**Addressees**") and their affiliates relying on the opinion letter. This opinion letter may not, without our prior written consent, be relied upon by or be disclosed to any other person save that it may be disclosed without such consent to:

(a) the officers, employees, auditors and professional advisers of any Addressee or any of their affiliates;

(b) any person to whom disclosure is required to be made by applicable law or court order or pursuant to the rules or regulations of any supervisory or regulatory body or in connection with any judicial proceedings; and

(c) any competent authority supervising an Addressee or any of its affiliates

on the basis that (i) such disclosure is made solely to enable any such person to be informed that an opinion has been given and to be made aware of its terms but not for the purposes of reliance, and (ii) we do not assume any duty or liability to any person to whom such disclosure is made and in preparing this opinion we have not had regard to the interests of any such person.

7.2 This opinion letter was prepared by Clifford Chance Deutschland LLP on the basis of instructions from EFET in the context of the General Agreement, in particular the requirements under CRR, and Clifford Chance Deutschland LLP has not taken instructions from, and this opinion letter does not take account of the specific circumstances of, any Addressee. In preparing this opinion letter, Clifford Chance Deutschland LLP had no regard to any other purpose to which this opinion letter may be put by any Addressee.

7.3 By permitting Addresses to rely on this opinion letter as stated above, Clifford Chance Deutschland LLP accepts responsibility to such Addressees for the matters specifically opined upon in this opinion letter in the context stated in the preceding paragraph, but Clifford Chance Deutschland LLP does not have or assume any client relationship in connection therewith or assume any wider duty to any Addressee or their affiliates. This opinion letter has not been prepared in connection with, and is not intended for use in, any specific transaction.

7.4 Furthermore, this opinion letter is given on the basis that any limitation on the liability of any other adviser to EFET or any Addressee, whether or not we are aware of that limitation, will not adversely affect our position in any circumstances.

Yours faithfully,

(Dr. Marc Benzler)

CLIFFORD CHANCE DEUTSCHLAND LLP

ANNEX 1

Section 104 InsO (incorporating the amendments in Article 1 of the Third Insolvency Code Amendment Act) – Please note that this version only applies to Insolvency Proceedings opened between 10 June 2016 and 28 December 2016

§ 104

Fixed Date Transactions, Financial Transactions, contractual close-out netting

(1) In the event that a particular time or period was agreed upon for delivery of commodities (*Waren*) with a market or exchange price, and such time occurs or such period lapses after the opening of insolvency proceedings, specific performance may not be demanded, but rather only a claim for non-performance may be asserted.

(2) Where a specified time or a specified period has been agreed for the delivery of financial products which have a market or exchange price, and where this time, or the expiry of this period, is not until after the opening of insolvency proceedings, performance may not be demanded, but rather only damages for non-performance may be claimed. Financial transactions shall include in particular

1. delivery of precious metals,
2. delivery of securities or comparable rights, except where there is an intention to acquire an interest in another enterprise with the aim of establishing a long-term relationship with that enterprise,
3. payments of money which are to be made in a foreign currency or in a mathematical unit,
4. payments of money the amounts of which are calculated, directly or indirectly by referencing to the exchange rate of a foreign currency or a unit of account, to the interest rate for borrowings or to the price of other goods (*Güter*) or services,
5. options and other rights to demand delivery of something or performance of payment obligations within the meaning of numbers 1 to 4 above,
6. financial collateral within the meaning of section 1 para 17 Banking Act.

Where the contracts involving financial transactions are combined in a master agreement for which it has been agreed that, where reasons for the opening of insolvency proceedings exist, it can only be terminated in its entirety, then such contracts shall together be deemed to form one single mutual agreement within the meaning of sections 103, 104.

(3) The amount of any claim for non-performance shall be the difference between the agreed price and such a market or exchange price which is applicable at the place of performance to an agreement with the stipulated time for performance on the date agreed between the parties on the second working day after the opening of insolvency proceedings.

(4) The parties to the contract may agree deviating provisions as long as these are compatible with the fundamental principles applicable to the statutory provision which is to be amended. They may, in particular, agree that,

1. the effects of paragraph 1 or paragraph 2 may apply prior to the opening of proceedings, in particular upon the application by a party to the contract for the opening of insolvency proceedings over its assets or upon the existence of a reason for the opening for proceedings (contractual termination),

2. that a contractual termination will encompass also such transactions pursuant to paragraph 1 or paragraph 2 in respect of which the claim for delivery of the commodity (*Ware*) or the performance of the financial transaction becomes due prior to the opening of proceedings, but after the point in time agreed for contractual termination,

3. that the claim for non-performance

    a) is determined by virtue of the market or exchange price for a replacement transaction which is entered into without undue delay, but no later than on the fifth business day after the contractual termination,

    b) is determined by virtue of the market or exchange price for a replacement transaction which could have been entered into at a contractually agreed point in time, but no later than on the fifth business day after the contractual termination,

    c) in case the market conditions do not allow for the conclusion of a replacement transaction pursuant to lit. a and b, may be determined by way of methods and procedures allowing for an adequate assessment of the value of the terminated transaction.

(5) The other party may assert the claim for non-performance only as an insolvency creditor.

ANNEX 2

Section 104 InsO (incorporating the amendments in Article 2 of the the Third Insolvency Code Amendment Act) - This version applies to Insolvency Proceedings opened from 29 December 2016 onwards

§ 104

Fixed Date Transactions, Financial Transactions, contractual close-out netting

(1) In the event that a particular time or period was agreed upon for delivery of commodities (*Waren*) with a market or exchange price, and such time occurs or such period lapses after the opening of insolvency proceedings, specific performance may not be demanded, but rather only a claim for non-performance may be asserted. This also applies to financial transactions which have a market or exchange price, and for which a particular time or period was agreed which only occurs or expires after the opening of insolvency proceedings. Financial transactions shall include in particular

1. delivery of precious metals,
2. delivery of financial instruments or comparable rights, except where there is an intention to acquire an interest in another enterprise with the aim of establishing a long-term relationship with that enterprise,
3. payments of money
   a) which are to be made in a foreign currency or in a mathematical unit, or
   b) the amounts of which are calculated, directly or indirectly by referencing to the exchange rate of a foreign currency or a unit of account, to the interest rate for borrowings or to the price of other goods (*Güter*) or services,
4. deliveries and payments from derivative financial instruments not excluded pursuant to number 2 above,
5. options and other rights to demand delivery pursuant to sentence 1 or for delivery, payment or options and rights within the meaning of numbers 1 to 5 above,
6. financial collateral within the meaning of section 1 para 17 Banking Act .

Financial instruments within the meaning of sentence 3 numbers 2 and 4 are those instruments listed in Annex I Section C of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ. L 173 of 12.6.2014, p. 349; L 74 of 18.3.2015, p. 38; L 188 of 13.7.2016, p. 28), as last amended by Directive (EU) 2016/1034 (OJ. L 175 of 30.6.2016, p. 8).

(2) The amount of any claim for non-performance shall be determined on the basis of the market or exchange value of the transaction. The market or exchange value is deemed to be

1. market or exchange price for a replacement transaction which is concluded without undue delay, but no later than on the fifth business day after the opening of insolvency proceedings, or

2. if no replacement transaction is entered into in accordance with number 1, the market or exchange price for a replacement transaction, that could have been concluded on the second business day after the opening insolvency proceedings.

To the extent that the market conditions do not allow for the conclusion of a replacement transaction pursuant to sentence 2 numbers 1 or 2, the market or exchange value is to be determined by way of methods and procedures allowing for an adequate assessment of the value of the transaction.

(3) Where transactions pursuant to paragraph 1 are combined in a master agreement or the rules of a central counterparty within the meaning of Section 1 paragraph 31 of the German Banking Act, which provides that the covered transactions may, upon the occurrence of certain events, only be terminated in their entirety, then the whole of such covered transactions shall be deemed to be a single transaction within the meaning of paragraph 1. This shall also apply, if other transactions are covered by such agreement or rules; such transactions shall be subject to the general provisions.

(4) The parties to the contract may agree deviating provisions as long as these are compatible with the fundamental principles applicable to the relevant statutory provision which is to be amended. They may, in particular, agree that,

1. the effects of paragraph 1 may apply prior to the opening of proceedings, in particular upon the application by a party to the contract for the opening of insolvency proceedings over its assets or upon the existence of a reason for the opening for proceedings (contractual termination),

2. that a contractual termination will encompass also such transactions pursuant to paragraph 1) in respect of which the claim for delivery of the commodity (*Ware*) or the performance of the financial transaction becomes due prior to the opening of proceedings, but after the point in time agreed for the contractual termination,

3. that for the purposes of the determination of the market or exchange value of the transaction

   a) the point in time of the contractual termination applies instead of the point in time of the opening of insolvency proceedings,

   b) the entering into of the replacement transaction pursuant to paragraph 2, sentence 2, number 1 may occur until the 20th business day after the contractual termination, if this is required to ensure that the unwinding of the transaction is performed in a manner that will maximise value,

c) instead of the point in time specified in paragraph 2 sentence 2, number 2 a point in time or a period between the contractual termination and the expiry of the fifth business day following such termination shall apply.

(5) The other party may assert the claim for non-performance only as an insolvency creditor.

ANNEX 3

Transactions under the General Agreement

The following describes certain generic transaction types which may be concluded by the parties under a General Agreement. Since the terms of the General Agreement do not explicitly restrict the transactions to be entered into thereunder to physically settled transactions, our description also includes cash settled transactions, even though market participants might use the General Agreement only to enter into physically settled transactions.

For the purposes of section 104 of the Insolvency Code as explained in Paragraph 5.1.1(i)(ii) above of the Opinion, please see our following analysis. The analysis is an integral part of the Opinion and subject to our statements made therein, including the Assumptions and Reservations under Paragraph 4 and Paragraph 6 above.

	Transaction Type	Legal Background
1.	Physically settled fixed date transactions relating to a commodity	**Section 104 para 1 sent. 1 applicable**: Fixed date transaction if the preconditions as set out in Paragraph 5.1.1.(i)(ii)(D) are met, as natural gas qualifies in our view as "commodity" (*Ware*) within the meaning of section 104 para 1 of the Insolvency Code.[220]
2.	Physically settled transactions relating to a commodity	**Section 104 para 1 sent. 2, 3 applicable**: Deliveries of financial instruments or comparable rights qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 2 of the Insolvency Code.[221] Deliveries of derivative financial instruments qualify as financial transactions under section 104 para 1 sent. 3 no. 4 of the Insolvency Code. Derivative financial instruments are financial transactions covered by Annex I Section C(4) to C(10) of MiFID II.[222] As regards physically settled commodities transactions, Annex I Section C(6) of MiFID II and Annex I Section C(7) of MiFID II apply.

220 See above Fn. 105.

221 Financial instruments are defined in section 104 para 1 sent. 4 of the Insolvency Code by reference to Annex I Section C of MiFID II. The relevant underlyings referred to in Annex I Section C(1) to C(3) of MiFID II do not cover commodities, however.

222 We understand that the references in Annex I Section C(4) to C(10) to options, futures, swaps and forwards (including the references in C(8) to derivative instruments and in C(9) to financial contracts for difference) do not include any spot transactions. With respect to the view under German law please refer to Paragraph 5.1.1(i)(ii)(E) above. According to the legislative reasoning to section 104 of the Insolvency Code clarifies that the amendments made by the Third Insolvency Code Amendment Act were not intended to limit the scope of section 104 of the Insolvency Code applicable before such amendments entered into force, BT-Drs. 18/9983, p. 18.

	Transaction Type	Legal Background
3.	Options on physically settled transactions relating to a commodity	**Section 104 para 1 sent. 2, 3 applicable**: Options in respect of fixed date transactions relating to a commodity described under item 1 and in respect of physically settled transactions relating to a commodity under item 2 above qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 5 of the Insolvency Code in connection with section 104 para 1 sent. 1 of the Insolvency Code or in connection with sectin 104 para 1 sent. 3 no. 2 or no. 4 of the Insolvency Code.
4.	Cash-settled transactions relating to a commodity	**Section 104 para 1 sent. 2, 3 applicable:**[223] Financial transaction within the meaning of section 104 para 1 sent. 3 no. 3 lit. (b) of the Insolvency Code as payment obligation is derived from the price of the "good" (*Gut*) "electricity" which falls under the terms "other goods or performances" (*andere Güter oder Leistungen*).[224] Cash-settled financial transactions relating to a commodity may also qualify as derivative financial instruments under section 104 para 1 sent. 3 no. 4 of the Insolvency Code if they qualify as financial instruments under Annex I Section C(5) of MiFID II.

223 If payments have to be made in a foreign currency or calculation unit and the receipt of such foreign currency or calculation unit is the main purpose of such transaction, cash-settled transactions would generally also qualify as financial transaction within the meaning of section 104 para 2 sent. 2 no. 3 lit. a) of the Insolvency Code.

224 As regards the interpretation of the term "goods and performances", see *Bosch*, WM 1995, 413, 416 (arguing that the term "*Güter*" includes any type of assets). The terms "*Güter*" or "*Leistungen*" is therefore broader than the term commodity in section 104 para 1 of the Insolvency Code.

	Transaction Type	Legal Background
5.	Options on cash-settled transactions relating to a commodity	**Section 104 para 1 sent. 2, 3 applicable:** Options in respect of cash-settled transactions relating to a commodity described under item 4 above qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 5 of the Insolvency Code in connection with section 104 para 1 sent. 3 no. 3 lit. (b) or no. 4 of the Insolvency Code.
6.	Physically-settled transactions on Emission Rights	**Section 104 para 2 sent. 2, 3 applicable**: Physically-settled emission allowances transactions qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 2 of the Insolvency Code if they qualify as financial instruments under Annex I Section C(4) or C(11) of MiFID II.
7.	Options on physically-settled transactions on Emissions Rights	**Section 104 para 1 sent. 2, 3 applicable:** Options in respect of physically-settled transactions on Emissions Rights described under item 6 above qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 5 of the Insolvency Code in connection with section 104 para 1 sent. 3 no. 2 of the Insolvency Code.
8.	Cash-settled transactions on Emission Rights	**Section 104 para 1 sent. 2, 3 applicable**: Cash-settled emission allowances transactions may qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 4 of the Insolvency Code if they qualify as financial instruments under Annex I Section C(4) of MiFID II.

	Transaction Type	Legal Background
9.	Options on cash-settled transactions on Emissions Rights	**Section 104 para 1 sent. 2, 3 applicable:** Options in respect of cash-settled transactions on Emissions Rights described under item 8 above qualify as financial transactions within the meaning of section 104 para 1 sent. 3 no. 5 of the Insolvency Code in connection with section 104 para 1 sent. 3 no. 4 of the Insolvency Code

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