MEMORANDUM OF LAW
FOR THE EUROPEAN FEDERATION OF ENERGY TRADERS

Enforceability under Czech Law of Close-out Netting Provisions under the EFET Master Netting Agreement and the TBMA Cross Product Master Agreement and enforceability and validity of transfer of title in collateral provisions under related Credit Support Annexes

17 May 2021

1. INTRODUCTION

The European Federation of Energy Traders (the **EFET**) asked us in the instruction letter dated 2 July 2020 (the **Instruction Letter**) to prepare a memorandum considering the enforceability under Czech law of close-out netting of privately negotiated (over-the-counter) transactions (each a **Transaction**) entered into between two parties under:

- the Cross Product Master Agreement published in February 2000 by the Bond Market Association (the **CPMA Form**) as further modified by Version 1.0 of the European Commodities Schedule published on 23 June 2003 by EFET/ International Energy Credit Association (IECA) (the **Schedule** and the CPMA Form as modified by the Schedule the **CPMA**); and
- the Master Netting Agreement published by EFET in June 2010 (the **MNA** and together with the CPMA the **Master Agreements** and each the **Master Agreement**).

The EFET also asked us to consider the enforceability and validity of collateral arrangements entered into between two parties in relation to the Master Agreements under:

- the Cross-Product Credit Support Annex (the **CPMA CSA**) to the CPMA published by EFET on 23 June 2003; and
- the Credit Support Annex to the MNA published by EFET in February 2011 (the **MNA CSA** and together with the CPMA CSA the **Credit Support Annexes** or **CSAs**).

The Master Agreements and the CSAs are together referred to as the **Agreements**.

The Instruction Letter sets out the terms on which we are asked to advise.

Capitalised terms used in this memorandum that are not defined herein have the meaning given to them under the Agreements or the Underlying Agreements (as defined below).

2. LIMITATIONS OF OUR OPINIONS AND SCOPE OF THE MEMORANDUM

We give our opinions in this memorandum solely in respect of (i) each Master Agreement; (ii) each CSA; and (iii) each Master Agreement combined with the relevant CSA in relation to the enforceability of close-out netting under each Master Agreement (and application of Eligible Credit Support to such close-out netting process under each CSA) in the context of an insolvency in the Czech Republic under Act No. 182/2006 Coll., on Insolvency and Manners of its Resolution, as amended (the **Insolvency Act**), of an entity organized and existing in, and subject to the bankruptcy courts of, the Czech Republic, which may be:

(a) a bank[1] incorporated in the form of a joint-stock company (in Czech, *akciová společnost*) licensed under Act No. 21/1992 Coll., on Banks, as amended (the **Banks Act**), including Česká exportní banka, a.s. whose activities are, in addition, governed by the Act on Export Insurance and Finance (No. 58/1995 Coll., as amended) (a **Czech Bank**);

(b) a trading company (in Czech, *obchodní společnost*) incorporated under the Act on Companies and Cooperatives (No. 90/2012 Coll., as amended, the **Corporations Act**) either in the form of a limited liability company (in Czech, *společnost s ručením omezeným*), a joint-stock company (in Czech, *akciová společnost*), a general commercial partnership (in Czech, *veřejná obchodní společnost*) or a limited partnership (in Czech, *komanditní společnost*) and each of them is an "entrepreneur" (in Czech, *podnikatel*) under Act No. 89/2012 Coll., Civil Code, as amended (the **Civil Code**) (each a **Czech Corporation**); or

(c) a securities dealer[2] (in Czech, *obchodník s cennými papíry*) incorporated under the Corporations Act either in the form of a limited liability company (in Czech, *společnost s ručením omezeným*) or a joint-stock company (in Czech, *akciová společnost*) and licensed by the CNB under the Capital Market Act (No. 256/2004 Coll., as amended, the **CMA**) (a **Czech Securities Dealer**, and, together with a Czech Bank and a Czech Corporation a **Czech Entity**).

We do not consider other entities whose business activities are regulated by special regulations, in particular: insurance companies, pension funds management companies, pension funds, investment or management companies, investment funds, trust funds, private individuals (natural persons), municipalities, regions governments, civic associations, public budgetary organisations, state enterprises, statutory corporations or funds. If you wish to enter into a Transaction under any Master Agreement or exchange collateral under any CSA, we recommend obtaining a specific legal advice contemplating specific limitations that may apply in respect of those entities.

In this memorandum we may also refer to:

(a) a bank organised and licensed under the laws of a country other than the Czech Republic and having a branch in the Czech Republic (a **Foreign Bank**); or

(b) a securities dealer or investment firm organised and licensed under the laws of a country other than the Czech Republic and having a branch in the Czech Republic (a **Foreign Securities Dealer**).

[1] A Czech Bank under Czech law corresponds to the definition of a credit institution under Article 4(1) of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (the **CRR**).

[2] A Czech Securities Dealer under Czech law corresponds to the definition of a credit institution under Article 4(1) 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 (**MiFID 2**).

2.2 Naming conventions

The name of each Czech Entity must identify the Czech Entity's legal form. The legal form is usually not spelled out in full but rather suffixed in an abbreviated form, as follows: limited liability company (in Czech, *společnost s ručením omezeným*) is usually identified by the suffix "s.r.o." or "spol. s r.o.", a joint-stock company (in Czech, *akciová společnost*) is usually identified by the suffix "a.s.", a general commercial partnership (in Czech, *veřejná obchodní společnost*) is usually identified by the suffix "v.o.s." and a limited partnership (in Czech, *komanditní společnost*) is usually identified by the suffix "k.s.". However, the suffix itself does not allow for a distinction among Czech Entities with respect of their commercial activity. Such information is present in their respective business licence or authorisation they possess.

3. ASSUMPTIONS

3.1 General assumptions

For the purposes of this memorandum, we have made the following general assumptions that apply to all Agreements:

(a) Two institutions (either two professional clients[3] or a professional client and a non-professional corporation) enter into an agreement in the form of the Master Agreement and the relevant CSA which are all governed by either English law or German law (as selected by the parties). One of the institutions is a Czech Entity and its counterparty has its registered seat (or place of residence) outside the Czech Republic.

(b) No provision of any Agreement that is necessary for the giving of this opinion has been altered in any material respect (each such provision a **Core Provision**). The following provisions are considered to be the Core Provisions: Sections 2, 3 and 4 (together with related definitions and provisions) of the CPMA; Sections 3(1) first paragraph, 4, 7 and 8 (together with related definitions and provisions) of the MNA and Section 7 of each CSA. In our view, no selection contemplated by the Election Sheet to the MNA or made in a Schedule to CPMA would be considered a material alteration for this purpose, unless stated otherwise in this memorandum.

(c) Only those designated Principal Agreements or Netted Agreements (**Underlying Agreements**) and the commodities or financial instruments commonly traded thereunder are covered by the Master Agreement. The Underlying Agreements are only in the form of the GTMA, EFET Power Agreement (Version 2.1(a)/September 21, 2007), EFET Gas Agreement (Version 2.0(a), May 11, 2007), EECS Certificate Master Agreement (Version 1.0/14 December 2013) (EFET Power Agreement, EFET Gas Agreement and EECS Certificate Master Agreement, **EFET Master Agreements**), ISDA Master Agreement (either the 1992 or the 2002 version). Each of the Underlying Agreements is governed by either English or German law save in respect of the ISDA Master Agreement, which is governed by either English, New York, Irish or French law. Each of the Underlying Agreements has a close-out netting provision that is enforceable in the Czech Republic[4] and we base our conclusions in this opinion accordingly.

(d) On the basis of the terms and conditions in the Master Agreement, the relevant Underlying Agreement (if applicable) and other relevant factors, and acting in a manner consistent with the intentions stated in that Master Agreement, the parties over time enter into a number of Transactions that are intended to be governed by that Master Agreement either as Transactions entered into under the relevant Underlying Agreement or as Uncovered Transactions/Additional Netted Agreements (where such Uncovered Transactions/Additional Netted Agreements will only include long form confirmations incorporating, in substantially their original form, the terms and conditions of the Underlying Agreements identified below in either Division 1, Part 1, Section A of the Template Default Elections of the CPMA or in the

[3] In the meaning of Article 4(10) of MiFID 2.

[4] 1) Enforceability under Czech law of close-out netting provisions under the EFET Gas Agreement (Version 2.0(a), May 11, 2007) is discussed in the legal opinion on the general agreeement concenring the delivery and acceptance of natural gas to the EFET issued on 12 April 2019 by Havel & Partners.
2) Enforceability under Czech law of close-out netting provisions under the EFET Power Agreement (Version 2.1(a)/September 21, 2007) and EECS Certificate Master Agreement (Version 1.0/14 December 2013) is discussed in the legal opinion on the general agreeement concenring the delivery and acceptance of natural gas to the EFET issued on 26 February 2019 by Havel & Partners.
3) Enforceability under Czech law of close-out netting provisions under the ISDA Master Agreements (either the 1992 or the 2002 version) is discussed in the legal opinion Enforceability under Czech Law of Close-out Netting of Privately Negotiated Derivatives Transactions under the 1992 ISDA Master Agreements and the 2002 ISDA Master Agreement issued on 9 July 2020 by Allen & Overy (Czech Republic) LLP, organizační složka.
4) We have not investigated or reviewed the Underlying Agreements, other than the ISDA Master Agreements, and rely for the purposes of this memorandum solely on the conclusions set out in the opinions issued by other law firms or, if not available as is the case in respect of the GTMA, assume their enforceability under Czech law as a matter of fact.

Additional Netted Agreement Rider in Part III of the MNA Election Sheet). These Transactions include any or all of those Transactions described in Annex A to the Instruction Letter, a copy of which is attached to this memorandum as Annex 3.

(e) Certain Transactions contemplated provide for settlement in cash whilst others provide for the physical delivery of shares, bonds, commodities or emission allowances in exchange for cash. In some cases, this distinction will prove important to our analysis below and we have assumed that a particular type of Transaction will only be cash-settled unless physical delivery is specifically envisaged in Annex 3.

(f) The obligations of each party under the Master Agreement, each Underlying Agreement and each Uncovered Transaction/Additional Netted Agreement are legal, valid and binding under the relevant governing law[5]. There is no relevant bilateral or multilateral international treaty in place and effect that would govern any private international law (conflict of laws) matter between the parties. This assumption does not apply in our answers where we expressly mention the opposite.

(g) Each Close-Out Event specified as applicable pursuant to: (i) in respect of the CPMA, the Election for Division 1, Part II, Section A of the model Schedule; or (ii) in respect of the MNA, the Election for Section 3.1, Part I of the Election Sheet is an effective and valid Close-Out Event under the applicable Underlying Agreement.

(h) After entering into the Master Agreement and one or more Transactions and prior to their maturity, the Czech Entity becomes subject to voluntary or involuntary insolvency proceedings (in Czech, *insolvenční řízení*) under Czech law. After the relevant insolvency proceedings have commenced, the insolvency administrator seeks to assume the Transactions that are profitable for the insolvent party and to reject the Transactions that are unprofitable for the insolvent party.

(i) There are no mandatorily applicable (in Czech, *nutně použitelné*) rules of law of the country where the Czech Entity's counterparty, a branch of that counterparty or, for the purposes of Part 9, the Foreign Counterparty or the Non-Czech Branch, is located. This assumption is applicable only if, and to the extent that, such rules would affect the conclusions set out in this memorandum and if, according to the laws of that country, such rules must be applied regardless of the law governing the contract.

 (i) With respect to the Master Agreement concluded on or after 1 July 2006 but before 17 December 2009, there are no:

  (A) mandatory rules (in Czech, *imperativní ustanovení*) of the country in which all the other elements relevant to the situation at the time of the choice are connected which cannot be derogated from by contract;

  (B) mandatory rules (in Czech, *imperativní ustanovení*) of law of any other country with which the situation has a close connection;

  (C) mandatory rules (in Czech, *imperativní ustanovení*) of law of the forum; and

  (D) rules specified by the Rome Convention (as defined below) of the law application of which is manifestly incompatible with the public policy (in Czech, *veřejný pořádek*) of the forum.

[5] We make this assumption because the courts of the Czech Republic will look to the governing law of the relevant contract to determine the basic contractual position before considering the effect of Czech insolvency law on that position.

This assumption is applicable only if, and to the extent that, such rules would affect the conclusions set out in this memorandum and if, according to the laws of that country, such rules must be applied regardless of the law governing the contract.

(ii) With respect to the Master Agreement concluded on or after 17 December 2009, there are no:

(A) provisions of the law of the country in which all other elements relevant to the situation at the time of the choice of law are located which cannot be derogated from by agreement (in Czech, *ustanovení práva od nichž se nelze smluvně odchýlit*);

(B) provisions of Community law of one or more EU Member States in which all other elements relevant to the situation at the time of the choice of law are located which cannot be derogated from by agreement (in Czech, *ustanovení práva Společenství od nichž se nelze smluvně odchýlit*) (where appropriate as implemented in the EU Member State of the forum);

(C) overriding mandatory provisions (in Czech, *imperativní ustanovení*) of the law of the forum;

(D) overriding mandatory provisions (in Czech, *imperativní ustanovení*) of the law of the country where the obligations arising out of the contract have to be or have been performed, in so far as those mandatory overriding provisions render the performance of the contract unlawful; and

(E) provisions of the law specified by the Rome I Regulation (as defined below) application of which is manifestly incompatible with the public policy (in Czech, *veřejný pořádek*) of the forum.

This assumption is applicable only if, and to the extent that, such rules would affect the conclusions set out in this memorandum and if, according to the laws of that country, such rules must be applied regardless of the law governing the contract.

(j) Each party has the relevant power and capacity and is duly authorised to enter into and perform their obligations under the Agreements, each Underlying Agreement and each Uncovered Transaction/Additional Netted Agreement and Transactions. If one of the parties was, when entering into any of them, represented by a proxy or representative, such proxy or representative had full power and capacity and was fully competent and duly authorised to do so. The Agreements, each Underlying Agreement and each Uncovered Transaction/Additional Netted Agreement and Transactions are duly executed and delivered by the parties in accordance with their constitutional legal acts or similar documents and with all applicable laws, regulations and permissions.

(k) The parties are personally liable as principal for their obligations under the Agreements, each Underlying Agreement and each Uncovered Transaction/Additional Netted Agreement and Transactions and are beneficially entitled to their rights under such them.

(l) No member of the governing, supervisory or other body and no other person who is authorised to act on behalf of one of the parties to the relevant Master Agreement (an **Authorised Person**), any relative (in Czech, *osoby blízké*) of any Authorised Person or persons influenced or controlled by any Authorised Person is at the same time a party to the relevant Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction or is at the same time authorised to enter into them on behalf of any other party.[6]

(m) No party to the relevant Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction (or a person influenced or controlled by such party) is a founder or a shareholder of, person acting in concert with such a shareholder of, influencing or controlling person in relation to any other party or a member of its governing, supervisory or other body, or person influenced or controlled by the same person as, any other party to that Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction or, to the extent that the parties are connected in any of the ways described above, all relevant corporate approvals and other steps required by law have been obtained prior to entry into such Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction.

(n) The Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction is entered into by each party prior to any action being taken in respect of either party for, or in connection with, the commencement of insolvency, bankruptcy, reorganisation, composition, debt discharge, dissolution, liquidation, administration, interim injunction, crisis prevention measure (in Czech, *opatření k předcházení krizí*), crisis management measure (including crisis resolution measures and actions or the appointment of a special manager) (in Czech, *opatření k řešení krize*) or any similar measure or action, court or other involuntary enforcement or public auction proceedings under applicable Czech law.

(o) The Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction is entered into, and each payment or delivery made thereunder is made, at arm's-length so that no element of gift or undervalue from one party to the other party is involved and without any intention of the former party to prefer the latter party in the event of the former party becoming insolvent.

(p) The Czech Entity is, at the time it enters into any Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction, not insolvent (in Czech, *v úpadku*) under applicable Czech law and is not under a threat of insolvency and it will not cause itself to become insolvent under applicable Czech law as a result of entering into the Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction.

(q) A Czech Bank has entered into any Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction in compliance with the Banks Act, Act No. 374/2015 Coll., on Framework for the Recovery and Crisis Resolution on the Financial Market, as amended (the **Crisis Resolution Act**) and other legislation and regulation applicable to a Czech Bank and all rights and obligations under any Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction are compatible with the Banks Act, the Crisis Resolution Act and other legislation and regulation applicable to a Czech Bank.

(r) A Czech Securities Dealer has entered into any Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction and each Transaction in compliance with the CMA, the Crisis Resolution Act and other legislation, if applicable, and regulation applicable to a Czech Securities Dealer and all rights and obligations under any Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction

[6] We make this assumption, and assumption 3.1(m), because of the relatively complex and strict Czech corporate laws in relation to intragroup trading, conflicts of interest and transactions between affiliates and other connected persons which if breached by a Czech Entity can lead to a contract being rendered null and void.

are compatible with the CMA, the Crisis Resolution Act and other legislation and regulation applicable to a Czech Securities Dealer.

(s) At the time of, or at any time before, the initiation of insolvency proceedings in relation to the Czech Entity, no involuntary enforcement, public auction or interim injunction has been ordered by a Czech court against that Czech Entity, in respect of any existing, future or contingent receivable under the Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction between the parties.

(t) The parties have complied with all relevant regulatory and similar obligations when entering into the Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction, in particular:

(i) have complied with and fulfilled all obligations on conducting business in the financial markets and customer care as envisaged by the applicable laws, rules and regulations (including those set out in or implementing 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 (**MiFID II**) or Directive 2013/36/EU of the European Parliament and the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC);

(ii) have complied with 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 (the **SFTR**), 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 (the **EMIR**) and 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 2014/17/EU and Regulation (EU) No 596/2014 (the **BMR**) including any regulatory technical standards or other rules adopted and published in relation to either of the SFTR, the EMIR or the BMR;

(iii) have complied with Regulation (EU) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency (the **REMIT**) including any regulatory technical standards or other rules adopted and published in relation to the REMIT; and

(iv) where one party is a manufacturer of PRIIP or seller of PRIIP[7] and the other party being a Czech Entity is a non-professional client in the sense of the CMA provided to the Czech Entity, in relation to each Transaction, a key information document in accordance with (i) Regulation (EU) No 1286/2014 of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (the **PRIIPs Regulation**), (ii) Commission Delegated Regulation (EU) 2017/653 of 8 March 2017 supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance-based investment products by laying down regulatory technical standards with regard to the presentation, content, review and revision of key information documents and the conditions for fulfilling the requirement to provide such documents (the **KID Regulation**), (iii) and all regulatory technical standards and other adopted and

7 As defined in Article 4(3) of the PRIIPs Regulation.

published regulations and interpretative opinions issued by the European Securities and Market Authority (**ESMA**) or the Czech National Bank in relation to the PRIIPs Regulation or the KID Regulation.

(u) The parties to the Agreement, Underlying Agreement, Uncovered Transaction/Additional Netted Agreement or Transaction have, when entering into each of them, complied with Act No. 340/2015 Coll., on Register of Contracts, as amended (the **Register of Contracts Act**), if and to the extent that act applies to the parties[8].

(v) The assets used for the performance of each Transaction have not been acquired through any criminal activity, and the Czech Entity is not under the risk of forfeiture of property, confiscation of a thing or seizure of a thing under Act No. 40/2009 Coll., the Criminal Code, as amended.

(w) The state of emergency (in Czech, *nouzový stav*) pursuant to Constitutional Act No. 110/1998 Coll., on Security of the Czech Republic, as amended (the **Act on the Security of the Czech Republic**) has not been declared; or, if it was declared, no payments in foreign currency or abroad generally, interbank transfers of monies from abroad to the Czech Republic and/or sale of securities abroad were suspended in accordance with Act No. 240/2000 Coll., the Crisis Act, as amended (the **Crisis Act**).[9]

3.2 CSAs specific assumptions

For the purposes of the assessment of the enforceability and validity of transfer of title in collateral provisions under related Credit Support Annexes, we make the following additional assumptions:

(a) Although each of the CSAs is a bilateral arrangement that contemplates that either party may be required to transfer the Eligible Credit Support to the other party depending on movements in exposure (Credit Support Amount) under the relevant CSA, for the sake of simplicity the same party is the Transferor at all relevant times under the applicable CSA.

(b) The Transferor is a Czech Entity and the Transferee is not a Czech Entity.

(c) No provision of the relevant CSA has been altered in any material respect. The making of standard elections in the CSA and the specification of standard variables (consistent with the other assumptions in this memorandum) would not in our view constitute material alterations, unless we expressly indicate otherwise below. There are no other agreements, contracts or arrangements entered into between the parties or between a party and a third person except for the Master Agreement, the Underlying Agreement, Uncovered Transaction/Additional Netted

[8] The Register of -Contracts Act took effect on 1 July 2016 and requires that contracts concluded with certain public-sector entities (the **Relevant Entities**) be, subject to exemptions, concluded in writing, or in any other way enabling the publication of a contract through the Register of Contracts, and published in an on-line Register of Contracts maintained by the Ministry of Interior. The Relevant Entities include, for example, the Czech Republic itself, municipalities and regional governments, state-owned enterprises, health insurers and Czech corporations directly or indirectly majority owned by the state or by one or more municipalities or regional governments. The exemptions from the publication requirement include, for example, contracts performed predominantly outside the territory of the Czech Republic, contracts concluded on regulated markets, or cases where the Relevant Entity is a joint stock company that has securities admitted to trading on a regulated market (this exemption has ceased to apply as of 1 November 2019). The act explicitly states that it applies regardless of the governing law of the contract. As of 1 July 2017, a contract that is subject to the requirement of publication in the Register of Contracts will not become effective until it is published in the register and will automatically be deemed void *ab initio* if not published within three months from its conclusion. However, the requirement that a contract must be concluded in writing, or in any other way enabling the publication of a contract through the Register of Contracts and published in the Register of Contracts has applied already from 1 July 2016.

[9] The state of emergency may be declared by the Czech government for 30 days (and may be extended for as long as necessary), if the sovereignty, territorial integrity, democratic foundations of the Czech Republic or, to a large extent, internal order and security, lives and health, property or the environment are directly threatened, or if international obligations on common defence need to be fulfilled. In case of a prolongation of the state of emergency, the Czech government needs approval from the Chamber of Deputies of the Parliament of the Czech Republic. During the state of emergency, the Czech government may restrict certain rights and freedoms as well as impose certain obligations and prohibitions, including prohibitions of certain activities of a financial nature or with respect to foreign exchange.

Agreement or Transaction and the relevant CSA, and no matters of fact that may affect the conclusions set out in this memorandum[10].

(d) The Eligible Credit Support provided under the each CSA will only take the form of either cash or letters of credit. The cash collateral is denominated in a freely convertible currency credited to an account (as opposed to physical notes and coins) held under the control of the Transferee.

(e) The Eligible Credit Support is not encumbered and the Transferor has acquired and retains proper legal title to the Eligible Credit Support and is entitled to transfer it under the CSAs in line with its terms.[11]

3.3 Multi-branch specific assumptions

For the purposes of our answers addressing the multi-branch issues, we make the following additional assumptions:

(a) For the purposes of answering the question 9.1, a Czech Entity has one or more Underlying Agreements Transactions that have been entered into by branches or other duly registered overseas offices in other jurisdictions than the Czech Republic (a **Non-Czech Branch**).

(b) For the purposes of answering questions 9.2 and 9.3, an overseas counterparty is incorporated or organized outside the Czech Republic (a **Foreign Counterparty**) has one or more Underlying Agreements or Transactions that have been entered into by its branch or another duly registered office in the Czech Republic (a **Czech Branch**).

3.4 Elections

For the purposes of our assessment, we assess only the following elections made in the Master Agreements (incl. the Schedule). Accordingly, our conclusions apply only to the Master Agreement as modelled by such elections and so having those characteristics (therefore, the terms **model Master Agreement** and **Master Agreement** used in this memorandum are interchangeable).

(a) **Excluded Agreements.** There are no Excluded Agreements specified under the (i) CPMA: Division 1, Part I, Section B; or (ii) MNA: Section 2.1, Part I of the Election Sheet.

(b) **Uncovered Transactions / Additional Netted Agreements.** In respect of the (i) CPMA: Division 1, Part I, Section C; and (ii) MNA: Part III of the Election Sheet, Uncovered Transactions / Additional Netted Agreements should be included but all such Transactions will be long form confirmations incorporating, in substantially their original form, the terms and conditions of one of the Underlying Agreements save that an Uncovered Transaction / Additional Netted Agreement will also include confirmations incorporating the short term flat NBP 2015 trading terms and conditions which have not been amended and are therefore not subject to an NBP Master.

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10 This assumption means, among other things, that neither party has entered with the other party to the Agreement or with any third person into any agreement, contract or arrangement under which it would for instance be possible to pledge the Eligible Credit Support as an asset of a third party or otherwise provide that Eligible Credit Support as a security in favour of a third person after its transfer to the Transferee.

11 This assumption means that, among other things, in relation to the Eligible Credit Support provided and/or transferred no prohibition to encumber or dispose of the Eligible Credit Support has been agreed or created, including as a right *in rem* under Section 1761 of the Civil Code or otherwise (including as a suspension of the right to dispose of the Eligible Credit Support under Section 97(1)(e) of the Capital Market Act), nor has there been agreed or created any negative pledge obligation under Section 1309(2) of the Civil Code, and that no such prohibition or obligation has been registered in the register of pledges (in Czech, *rejstřík zástav*) maintained by the Notarial Chamber of the Czech Republic pursuant to the Act on Notarial Procedures (Act No. 358/1992 Coll., as amended) (the **Register of Pledges**) or in a public register (in Czech, *veřejný seznam*). This assumption further means that, among other things, the Eligible Credit Support provided and/or transferred is not a part of an enterprise or other collective asset that is subject to a pledge of enterprise or that other collective asset.

(c) **Close-Out Events.** In the (i) CPMA: Division 1, Part II, Section A; or (ii) MNA: Section 3.1, Part 1 of the Election Sheet, 'Close-Out Event' means any events that entitle close-out under the Underlying Agreements. In respect of the CPMA only, given the assumption in relation to Uncovered Transactions, we confirm that it is up to the Parties whether they will check all boxes or all boxes save for 'Uncovered Transaction Default'.

(d) **Excluded Events.** For the purposes of the (i) CPMA: Division 1, Part II, Section B; or (ii) MNA: Section 3.2, Part 1 of the Election Sheet, we assume that in respect of the definition of the Excluded Events only the first three boxes will be checked.

(e) **Automatic Close-Out of Underlying Agreements.** Unless expressly stated otherwise in this memorandum, we assume that (a) in the CPMA: Division 1, Part II, Section C the box is checked and that the rewrite of this provision contained in the Schedule is operative; and (b) in the MNA: Section 6.1, Part 1 of the Election Sheet the box is unchecked.

(f) Under the (a) CPMA: Division 1, Part III; or (b) MNA: Section 12.1, Part 1 of the Election Sheet there are no Additional Acknowledgements and Representations.

(g) For the purposes of the (a) CPMA: Division 1, Part IV; or (b) MNA: Section 12.2, Part 1 of the Election Sheet – Governing Law – we assume that English and German law applies, in the alternative.

(h) (a) For the purposes of the CPMA: Division 1, Part VII, we assume that no election, Section 7 applies but is amended as set out in (a) and (b) of the Election Sheet; and (b) for the purposes of the MNA: Section 12.5, Part 1 of the Election Sheet – Assignment, we assume that Section 12.5(A) is operative in respect of Party A and Party B.[12]

(i) We assume that the following elections apply[13]:

	CPMA: Division 1, Part VIII	**MNA: Election Sheet**
Set-off of Final Net Settlement Amount	10.1	Section 10.1(A)
No Waiver	10.2	Automatically included (see Section 10.8 of the MNA)
Suspension	10.4	Section 10.1(B)
Automatic Early Termination & Adjustment for Bankruptcy	10.5	Section 6.4
Benefit of Credit Support	10.7	Section 9.1
Withholding Final Net Settlement Amount	10.8	No equivalent

(j) For the purposes of the (a) CPMA: Division 1, Part X; or (b) MNA: Part II of the Election Sheet, we assume that there are no additional terms.

(k) We assume that the CPMA: Division 2 applies as set out in the Schedule.

12 We note that the validity of this provision is subject to its governing law. For the discussion regarding the valid choice of law, see our answer to question 6.8. We are not aware of any decision of Czech courts declaring that prohibition of an assignment is contrary to Czech public order and so unenforceable in the Czech Republic.

13 We note that the validity or of these provisions is subject to their governing law. For the discussion regarding the valid choice of law, see our answer to question 6.8. We are not aware of any decision of Czech courts declaring legal institutes represented by these elections contrary to Czech public order and so unenforceable in the Czech Republic.

4. SUMMARY OF CONCLUSIONS

On the basis of the assumptions and subject to the qualifications set out in this memorandum, our conclusions are that:

(a) Assuming that the parties have not selected Automatic Early Termination, the provisions of each Master Agreement entitling a non-defaulting Party (a Closing-Out Party) to terminate all Transactions in insolvency proceedings in respect of a counterparty that is a Czech Entity would be enforceable as a matter of Czech law.

(b) If elected, the Automatic Early Termination provisions of each Master Agreement would be enforceable as a matter of Czech law in insolvency proceedings in respect of a party that is a Czech Entity.

(c) The provisions of each Master Agreement providing for the netting of termination values in determining a single lump-sum termination amount would be enforceable under Czech law in insolvency proceedings in respect of a party that is a Czech Entity subject, in particular, to a number of qualifications discussed in Parts 6 and 7 below. One such qualification is that certain classes of Transactions may pertain to non-qualifying underlying assets or (depending on their precise structure) may not qualify as an investment instrument or other eligible underlying assets under Czech law and may therefore be ineligible for close-out netting. It is recommended that parties consider using a separate Master Agreement to govern any non-qualifying Transactions[14]. Transactions whose subject-matter is physical delivery of natural gas or power do not fall within the scope of transactions with non-qualifying underlying assets and as such are generally eligible to form a part of the determination of the single lump-sum termination amount.

(d) Enforceability of the determination of a single lump-sum termination amount under Czech law in insolvency proceedings is not subject to a requirement that parties to an agreement containing such determination must fall within certain class or possess a special status, as is the case of financial collateral arrangements.

(e) Where the parties select a Base Currency other than the Czech Koruna (**CZK**) under a Master Agreement and a party that is a Czech Entity becomes subject to insolvency proceedings, Czech law is likely to require that such net termination amount is converted into CZK before it is paid.

(f) The conclusions relating to the enforceability of close-out netting in insolvency proceedings in respect of a party that is a Czech Entity would not be affected by the fact that the Czech Entity entered into the Master Agreement on a multibranch basis.

(g) Upon the start of insolvency proceedings in relation to the Foreign Counterparty in Country H (as defined below), separate insolvency proceedings would not commence automatically in the Czech Republic in relation to the assets and liabilities of its Czech Branch. The Czech authorities would only be required to defer to the proceedings in Country H if the Foreign Counterparty has its registered seat in another EU Member State.

(h) If there were to be a separate insolvency proceeding in the Czech Republic with respect to the assets and liabilities of a Czech Branch (as defined below) and the Foreign Counterparty's position under the Master Agreement was included, then the Czech

[14] Namely those Transactions non-eligible for close-out netting under Czech law as discussed in our answers to questions 6.4 and 7.3

courts would recognise the close-out netting provisions of the Master Agreement to the same extent as described in Parts 6 and 7 below.

(i) Actions taken by an insolvency administrator or court in a jurisdiction where close-out netting may not be enforceable would not affect the conclusions referred to in paragraphs (a)-(g) above and would not affect the treatment of a multibranch Master Agreement as a single agreement under Czech law.

(j) Transfers of Collateral in the form of outright transfer of cash under the CSAs are not governed by Czech law and, so long as the Collateral is delivered prior to the commencement of the insolvency proceedings in respect of the Czech Entity, such transfers are recognized in the Czech Republic and protected from negative effects of the insolvency proceedings, provided that the parties are eligible legal entities to the financial collateral arrangements as listed in Annex 1. The same conclusion applies also in respect of a Czech Branch entering and delivering Collateral as Transferee under the CSA.

5. CZECH INSOLVENCY LAW

5.1 General description of Czech insolvency proceedings and exemption applicable to close-out netting arrangements

For your background information, in the Czech Republic, since 1 January 2008 the insolvency proceedings available to assist a debtor in the situation of insolvency or threatened insolvency have been governed by the Insolvency Act and by Regulation (EU) No 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (the **Insolvency Regulation**) that governs cross-border insolvency within the European Union (excluding Denmark).

The purpose of insolvency proceedings is to resolve the debtor's insolvency or threatened insolvency through the appropriate insolvency/restructuring proceedings, in order to: (i) arrange the debtor's proprietary relations to persons affected by the debtor's insolvency or threatened insolvency; and (ii) satisfy the debtor's creditors generally on a *pro rata* basis and to the greatest extent possible.

A debtor is insolvent if it has more than one creditor and unpaid debts which are more than 30 days overdue and is unable to pay these debts. The debtor is presumed to be unable to pay its debts if: (i) it has ceased to make payments in relation to a substantial part of its debts; (ii) its debts are more than three months overdue; (iii) it is impossible to satisfy any of the debtor's due debts through court enforcement or execution; or (iv) the insolvency court has requested that the debtor provide a list of its assets, liabilities and employees and the debtor fails to comply with this request.

Since 1 July 2017, a debtor who is an entrepreneur and keeps financial accounts is deemed able to pay its debts if (i) the difference between the amount of the Debtor's due financial liabilities and the amount of available funds (the coverage gap, in Czech, *mezera krytí*) represents less than 10% of the Debtor's due financial liabilities, or if (ii) the Debtor's liquidity forecast certifies that such difference will decrease below 10% in the given forecast period, in each case provided that this is based on a report of the state of liquidity or a liquidity forecast prepared by an authorised person.

A corporate debtor is also insolvent if it is over-indebted. A debtor is over-indebted if it has more than one creditor and its debts are greater than its assets (whilst estimating the value of the assets, the further operation of the business have to be taken into account). The debtor is threatened by insolvency if it is justified to assume, given all of the circumstances of the case, that the debtor will be unable to satisfy a substantial part of its debts when they become due.

The concept of single insolvency proceedings applies in the Czech Republic. There is a single entry system with a uniform initial stage of proceedings in which the insolvency court examines whether the debtor is indeed insolvent or, where applicable, at least threatened by insolvency. If the insolvency court reaches a positive decision on that issue, it will then decide on the method by which the debtor's insolvency should be resolved. It will generally follow the decision of the debtor's creditors (where such choice is possible). The insolvency proceedings will take the form of either bankruptcy, reorganisation or discharge from debts (only applicable to non-entrepreneurs).

In its decision declaring the debtor insolvent, the insolvency court will appoint an insolvency administrator (in Czech, *insolvenční správce*) who holds the power to deal with the insolvency estate to the extent that the debtor is prohibited by law or a decision of the insolvency court from dealing with its estate. The insolvency administrator will also ascertain, examine, list and collect the debtor's assets and scrutinise filed claims. The insolvency administrator's remaining tasks will depend on whether the debtor's insolvency will be resolved by bankruptcy or reorganisation. Furthermore, before declaring the debtor insolvent, the insolvency court may appoint a preliminary administrator (in Czech, *předběžný správce*). A preliminary administrator is likely to be appointed in circumstances where the insolvency estate is large, if the insolvency court approved a moratorium, or for other reasons specified in the Insolvency Act.

Bankruptcy proceedings qualify as main proceedings under the Insolvency Act. It is a stage which follows the initial examination of the debtor's insolvency and the insolvency court's decision on the method to be used in order to resolve the debtor's insolvency. Unlike reorganisation, bankruptcy may be used to resolve the insolvency of any type of debtor. When the insolvency court declares the debtor insolvent it will also place it into bankruptcy proceedings if no other method of resolving the debtor's insolvency is available. In bankruptcy, the debtor's insolvency is resolved generally by a *pro rata* satisfaction of the ascertained creditors' claims out of the proceeds from the liquidated insolvency estate. As a rule, the (in whole or in part) unsatisfied claims are not discharged. However, an exception to this rule includes corporate debtors that are wound up as a result of the termination of the bankruptcy proceedings.

The aim of reorganisation proceedings is the eventual satisfaction of creditors' claims while the debtor's business continues in operation. This is achieved by measures intended to revitalise the economic operation of the debtor's business in accordance with a reorganisation plan approved by the insolvency court. The performance of the reorganisation plan is continuously monitored by creditors. Reorganisation is generally available only to companies with total net turnover in the last accounting period of at least CZK 50,000,000 (approximately EUR 1,940,000), or with at least 50 employees. With the creditors' consent, however, reorganisation is also available to smaller debtors, subject to further procedural conditions. Reorganisation may not be used, *inter alia*, by companies in liquidation.

It is possible for an interested party to search for the existence of insolvency proceedings against a particular company in the insolvency register. The insolvency register (which is held in the Czech language) is publicly accessible online on the website of the Ministry of Justice of the Czech Republic, *www.justice.cz*. The register contains all information that has been published regarding all insolvency proceedings initiated by Czech courts and information on insolvency proceedings commenced by non-Czech EU courts that have been published at the relevant insolvency administrator's request pursuant to Art. 28(1) of the Insolvency Regulation. It also contains a list of debtors. The insolvency proceedings are initiated on the day of delivery of the insolvency petition to the relevant insolvency court (Section 97(1) of the Insolvency Act). Generally, the insolvency courts must publish the notice of initiation of insolvency proceedings in the insolvency register within two hours after it has received the insolvency petition. This time period will be extended by up to two hours after the insolvency court has opened its business if the insolvency petition is delivered to the court either outside its regular hours of operation or less than two hours prior to the end of its regular hours of operation.

Furthermore, if the creditors intend to initiate insolvency proceedings and file an insolvency petition, the Insolvency court must first conduct a preliminary assessment as to whether there exist "good grounds to doubt the legitimacy" of such insolvency petition (i.e. whether the insolvency court could dismiss the insolvency petition for being apparently groundless). This measure was enacted to serve as a protection of potential debtors against frivolous petitions filed by creditors. In general, insolvency petitions are considered to be frivolous if they, in fact, pursue a goal other than that of resolving the debtor's insolvency. According to Section 128a(4) of the Insolvency Act, an insolvency petition is groundless, in particular, where: (i) the creditor proves its entitlement to file the insolvency petition using a receivable which may not be considered for the purposes of a de cision on insolvency, (ii) it is a repeat filing and the insolvency petitioner fails to prove that it has fulfilled obligations imposed on it by a previous decision of the insolvency court, (iii) by filing the insolvency petition, the creditor clearly intends to abuse its rights to the debtor's detriment, or (iv) the deposit for the costs of the insolvency proceedings, which was payable simultaneously with the filing of the insolvency petition, was not paid in a due and timely manner. If the insolvency court concludes that there are, indeed, "good grounds to doubt the legitimacy" of the insolvency petition submitted by creditors, it must decide no later than by the end of the business day following the receipt of the insolvency petition that neither the insolvency petition nor other underlying documentation will be published in the insolvency register. Following this decision, the insolvency court has seven days to either (i) dismiss the insolvency petition as clearly groundless, or (ii) to publish a notice of initiation of insolvency proceedings in the insolvency register (if it, ultimately, concludes that there are no grounds for dismissing the insolvency petition).

Finally, the effects of the initiation of insolvency proceedings are only triggered upon the publication of the notice of initiation of insolvency proceedings in the insolvency register (Section 109(4) of the Insolvency Act).

The Insolvency Act states in Section 366(2) that its provisions do not affect close-out netting arrangements, which are defined in Section 193 of the CMA (see paragraph 6.4), provided that such close-out netting arrangement has been entered into prior to the initiation of insolvency proceedings. In light of this provision, the decisive moment for a Transaction to be eligible for close-out netting as contemplated by the CMA (see paragraph 6.4) is the moment of the initiation of insolvency proceedings.

Although we have assumed that the Master Agreement and each Transaction are entered into by each party prior to any action being taken in respect of either party for, or in connection with, among other things, the commencement of insolvency proceedings, we provide our analysis of what may constitute the decisive moment of the initiation of insolvency proceedings. The Insolvency Act uses two very similar terms and each of them may be considered the "initiation of insolvency proceedings" within the meaning of Section 366(2) of the Insolvency Act. Firstly, pursuant to Section 97(1) of the Insolvency Act, insolvency proceedings are "commenced" on the day of delivery of the insolvency petition to the relevant insolvency court. Secondly, based on Section 109(4) of the Insolvency Act, "the effects of the initiation of insolvency proceedings" are only invoked upon the publication of the notice of the initiation of insolvency proceedings in the insolvency register. The moment of publication in the insolvency register means the day, hour, and minute of publication (Section 71(2) of the Insolvency Act).

Both these moments (i.e., the day of delivery of the insolvency petition to the insolvency court, and the moment of publication of the notice in the insolvency register) may be interpreted as the initiation of insolvency proceedings for the purposes of Section 366(2) of the Insolvency Act and correct determination of this moment is crucial for ascertaining the eligibility of a Transaction for close-out netting (as discussed in paragraph 6.4).

The insolvency court is obliged to publish the notice of initiation of insolvency proceedings in the insolvency register within two hours after it has received the insolvency petition. However, if an insolvency petition is delivered to the insolvency court either less than two hours prior to the end of or outside its regular hours of operation, this two-hour time period may be extended by up to two hours after the insolvency court has again opened its office on the next business day. As a result, if an insolvency petition is delivered on a day when the insolvency court does not operate or shortly (i.e., less than two hours) prior to the end of its hours of operation, the initiation of insolvency proceedings within the meaning of Section 97(1) of the Insolvency Act could be interpreted to have occurred on that day. At the same time, however, the effects of initiation of insolvency proceedings as stated in Section 109(4) of the Insolvency Act would only be triggered on the following business day (or even lately if the insolvency court have doubts whether the insolvency petition is groundless). The discussed timing is subject to the fact that the publication of the notice of initiation of insolvency proceedings may be postponed due to existing of "good grounds to doubt the legitimacy" of the insolvency petition as discussed above.

Since the new wording of Section 366(2) came into effect only relatively recently (as of 1 January 2011), there is no official guidance or commentary available on this issue nor has it been tested in Czech courts.

Despite this ambiguity in the Insolvency Act, we are inclined to take a view that the moment of the initiation of insolvency proceedings within the meaning of Section 366(2) must be associated with the commencement of its effects *vis-à-vis* third persons, i.e. as of publication of the notice in the insolvency register. Even though the insolvency proceedings are formally commenced on the day of delivery of the insolvency petition to the insolvency court, they remain without any effects envisaged by the Insolvency Act until the moment of publication of the notice of initiation of insolvency proceedings. In other words, the Insolvency Act does not relate any of its effects to the moment of delivery of the insolvency petition to the relevant insolvency court. Moreover, the explanatory memorandum to Section 366(2) expressly states that this wording is aimed at the protection of close-out netting arrangements against *effects* of the insolvency proceedings.

However, Section 366(3) newly stipulates that, *inter alia*, Section 366(2) of the Insolvency Act does not apply to those provisions of the Insolvency Act concerning the invalidity of legal acts, and the ineffectiveness of legal acts at undervalue, preferential legal acts, fraudulent legal acts and legal acts performed by the debtor contrary to restrictions connected with the initiation of insolvency proceedings.

5.2 Procedural effects of insolvency

Filing an insolvency petition has a number of procedural effects on the part of both the debtor and the creditor, regardless of whether or not the debtor is actually insolvent. These effects are of two types:

(A) protection of the debtor from creditors (automatic moratorium); and

(B) restriction of the debtor's right to dispose of its assets and liabilities, aimed at protecting the creditor against impairment of the debtor's assets.[15]

The effects of an insolvency petition remain in existence until the insolvency court issues a decision on the method of resolving the insolvency (or until the insolvency court dismiss or refuse the insolvency petition or until the insolvency court terminate the insolvency proceedings).

Below are the effects of insolvency proceedings impacting the rights of creditors of a Czech debtor subject to insolvency proceeding that may be relevant for the purposes of this memorandum. The summary below is not a full disclosure.

Protection from creditors

Once insolvency proceedings have been commenced:

(i) creditors may only assert their claims relating to the debtor's estate by means of a claims submission made within the insolvency proceedings (no separate statement of claim can be submitted and no other means of debt recovery is possible);

(ii) the rights associated with the process of securing the claims can be established and exercised only in compliance with the Insolvency Act; and

(iii) although it is possible to order the enforcement of a judgment or distress with respect to the debtor's assets or the assets comprised in the estate, such enforcement or distress cannot be executed.

Restriction of the debtor's right to dispose of assets, discharge of obligations

Unless the Czech insolvency court decides otherwise, from the time the judicial notice on the commencement of insolvency proceedings is published in the insolvency register, the debtor must refrain from the following:

(i) disposing of its assets, provided that as a result of such disposal the structure, use or purpose of the assets would change materially or would be diminished to a significant extent; and

[15] However, even after an insolvency petition is filed, the debtor or its management remains the party exercising the right to dispose of its assets and liabilities.

(ii) repaying debts, save where such debts are discharged under the terms and conditions set out by the Insolvency Act.

The above restrictions do not apply to the disposal of assets or debt repayment within the ordinary course of business, the fulfilment of statutory obligations or averting imminent damage. Nevertheless, additional restrictions may ensue from (i) a preliminary injunction which can be ordered by the insolvency court even without a previous motion or (ii) from the appointment of a preliminary administrator by the Czech insolvency court. The preliminary administrator may be entrusted with the right to dispose of all or a part of the assets of the debtor. If the debtor does not abide by the restrictions, his/her legal acts are ineffective and the debtor is held liable for damage arising thereof *vis-à-vis* his/her creditors.

Moratorium

A debtor who is an entrepreneur may file a petition with the insolvency court to declare a moratorium. Such petition must be filed within seven days of the submission of an insolvency petition and within 15 days in the case of an insolvency petition of a creditor. The debtor is also entitled to file a petition for a moratorium even before the commencement of the insolvency proceedings.

For the duration of the moratorium, the ruling on insolvency may not be issued, and the debtor is entitled to pay its debts directly associated with maintaining its business which were established in the 30 days prior to the declaration of a moratorium, or after it, with priority over earlier payable debts (priority debts).

The other party (besides the debtor) in energy supply and raw materials agreements, as well as other agreements for the supply of goods and services, which by the date of the declaration of a moratorium had lasted for at least 3 months may not, for the duration of the moratorium, terminate or withdraw from such agreements due to the default of the debtor in payment for goods or services that occurred before the declaration of the moratorium. The above applies on the condition that the debtor fulfilled at least the priority debts (as described above) from such agreements.

A moratorium is effective from the date of publication of the decision on its declaration in the insolvency register, and it lasts for a period of no more than three months. The Czech insolvency court may, upon the petition of the debtor, extend the moratorium by a maximum of 30 days.

Set-off

Under Czech law, if parties owe to each other a financial obligation, each of them may declare with respect to the other party that it sets off its claim against the claim of the other party. A claim may be unilaterally set off once a party becomes entitled to demand satisfaction of its own claim and perform its own debt.

Claims eligible for a unilateral set-off are only those which can be asserted in court. An uncertain or indeterminate claim is not eligible for such a set-off. Parties may however agree in a contract to set off even claims which would not otherwise be eligible for a set-off.

The Insolvency Act does not in general prohibit a set-off of claims. There are however some exceptions to this rule. Set-off against claims that form a part of the insolvency estate is excluded during reorganization, moratorium and where the insolvency court issued an injunction prohibiting such set-offs. Section 140 of the Insolvency Act stipulates further requirements for set-off occurring after the debtor was declared insolvent:

"[…]*(2) The set-off of the mutual receivables of the debtor and the creditor is admissible after the decision on the insolvency if the statutory conditions of such set-off were met before the decision on the method of resolution of the insolvency, unless it is further stipulated otherwise*.

(3) The set-off under Subsection 2 is not admissible, if the debtor's creditor

(a) failed to become a registered creditor in relation to its receivables eligible for offsetting, or

(b) gained a receivable eligible for offsetting by an ineffective legal act, or

(c) at the time of the acquisition of the receivable eligible for offsetting, knew about the debtor's insolvency, or

(d) has not yet paid the mature receivable of the debtor to the extent in which it exceeds the receivable eligible for offsetting of such creditor.

(4) The set-off referred to in Subsection 2 is also not admissible in the cases provided for by this Act or by a preliminary measure of the insolvency court."

Pursuant to Section 82(3) of the Insolvency Act, the court may issue a preliminary measure under which it allows or prohibits a set-off of claims:

"[*…*]*Unless it is contrary to the common interest of the creditors, the insolvency court may, for reasons worthy of special consideration, through a preliminary measure also*

(a) grant consent to the set-off of the mutual receivables of the debtor and the creditor during the period of moratorium, or

(b) grant consent to the set-off of the mutual receivables of the debtor and the creditor even after the publication of the petition for the restructuring permit in the Insolvency Register, or

(c) prohibit the set-off of the mutual receivables of the debtor and the creditor for certain cases or for a set period of time."

Pursuant to Section 369(2)(c) and Section 381(2)(c) of the Insolvency Act, the insolvency proceedings of financial institutions (i.e. Czech Banks and Czech Security Dealers and their local branches) do not have an effect on the right of the creditors to request a set-off against the receivable of the debtor, where such set-off is permitted by the law that governs the receivable of the debtor.

5.3 Changes in Czech insolvency law caused by the Covid-19 pandemic

As a result of the Covid-19 pandemic, Act No. 191/2020 Coll., on Certain Measures to Alleviate the Impact of the SARS CoV-2 Coronavirus on Persons Participating in Court Proceedings, Injured Parties, Crime Victims and Legal Persons and on Change to the Insolvency Act and the Code of Civil Procedure, as amended (the **Covid-19 Act**) was adopted. The Covid-19 Act has created a new regime for Czech debtors[16] enabling them to apply for an extraordinary moratorium.

An extraordinary moratorium was passed in the form of Section 127a of the Insolvency Act, as opposed to being contained in a stand-alone law referencing the Insolvency Act indirectly. As such, it falls within the close-out netting exception set out in Section 366(2) of the Insolvency Act. The extraordinary moratorium therefore does not affect the ability of a counterparty under the Master Agreement to perform close-out netting in respect of all relevant Transactions entered thereunder, provided that the conditions set out in paragraph 6.4 for an eligible close-out netting arrangement are met.

[16] That is, debtors with their centre of main interest, within the meaning of the Insolvency Regulation, in the Czech Republic.

Additionally, under the Covid-19 Act, any insolvency petitions filed by creditors of a Czech debtor until 31 August 2020 are to be disregarded.[17] Lastly, when a debtor's insolvency (in Czech, *úpadek*) is caused by Covid-19 extraordinary measures, the Covid-19 Act suspends the obligation of Czech debtors (and their directors) to file for insolvency when normally required by law.[18] This suspension will last until the end of a six-month period starting from cancellation of the Covid-19 extraordinary measures, but not extending beyond 30 June 2021.

5.4 Regulation of resolutions of Czech banks and large Czech securities dealers

Chapter 1 of Part IV of Title 2 of the Insolvency Act addresses insolvency proceedings of a Czech Bank or Czech Securities Dealer operating in the Czech Republic and providing services in the Czech Republic. From 1 January 2016 it also addresses financial institutions, financial holding companies, mixed financial holding companies and mixed activity holding companies, as defined in the CRR, with their registered office in the Czech Republic. Chapter 1 of the Insolvency Act has implemented Directive 2001/24/EC of the European Parliament and Council of 4 April 2001 on the reorganisation and winding up of credit institutions (the **WUCI Directive**) as well as Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing framework for the recovery and resolution of credit institutions and investment firms, as published in the Official Journal of the EU on 12 June 2014 (the **BRRD**), and will apply to proceedings of:

(i) banks and savings and credit cooperatives after their licence or permission granted to them has terminated (i.e. Czech Banks);

(ii) foreign banks operating in the Czech Republic on the basis of a single European banking licence in line with the Banks Act (i.e. Foreign Banks from the EU having their licence passported into the Czech Republic);

(iii) branches of foreign banks other than those mentioned under point (ii) above (i.e. Czech Branches of non-EU Foreign Banks providing their services in the Czech Republic in line with the Banks Act);

(iv) securities dealers (i.e. Czech Securities Dealers);

(v) foreign securities dealers providing investment services in the Czech Republic on the basis of a single European licence in line with the CMA (i.e. Foreign Securities Dealers);

(vi) branches of foreign securities dealers other than those mentioned under point ((v)) above (i.e. Czech Branches of non-EU Foreign Securities Dealers providing their services in the Czech Republic in line with the CMA); and

(vii) financial institutions, financial holding companies, mixed financial holding companies and mixed activity holding companies as defined in the CRR.

The insolvency petition in respect of persons mentioned under points (i), (iii), (iv) and (vi) will be filed by the authority supervising the activities of such persons. Only the authority of the home Member State (of the European Union (**EU**) or the European Economic Area (**EEA**)) that granted the licence or permission on the basis of which this person operates in the Czech Republic may act[19] against persons mentioned under points (ii) and (v) above.

[17] Section 13 of the Covid-19 Act.
[18] Section 12 of the Covid-19 Act.
[17] Pursuant to Section 367(2) of the Insolvency Act, a foreign bank operating in the Czech Republic on the basis of a single licence pursuant to the Banks Act will be subject to insolvency proceedings if the following proceedings are carried out: (i) collective proceedings opened and monitored by the administrative or judicial authorities of a Member State of the European Union or other state of the European Economic Area with the aim of realising assets under the supervision of those authorities, including where the proceedings are terminated by a

The insolvency of a Czech Bank, the insolvency of a Czech Branch of a Foreign Bank defined in point (iii), and the insolvency of persons mentioned in points (iv), (vi) and (vii) above, if a crisis resolution measure pursuant the Crisis Resolution Act was imposed on them, may be resolved only by means of bankruptcy. A special regime applies to a Czech Securities Dealer which is subject to an initial capital requirement of EUR 730,000 (a **Large Securities Dealer**) with its registered office in the Czech Republic (a **Large Czech Securities Dealer**) and persons under point (vii) above.

Our conclusions in this memorandum in respect of Parties which are either a Czech Bank, a Large Czech Securities Dealer or a Czech Branch of a non-EEA Large Securities Dealer[20] are, to the extent described below, subject to the Crisis Resolution Act.

Subject to certain modifications, none of which are relevant to our conclusions provided below, the Crisis Resolution Acts applies similarly to all entities presented above. The Crisis Resolution Act implements BRRD in Czech law. BRRD seeks to establish a common framework for the orderly resolution of failing credit institutions and investment firms within the European Union (as well as entities within their group if deemed relevant). Member States, including the Czech Republic, had an obligation to transpose and implement BRRD into national law by 31 December 2014 and to apply the majority of its provisions from 1 January 2015 (Article 130(1) of BRRD allows for Member States to apply provisions relating to the 'bail-in tool' from 1 January 2016 at the latest).

Responsibility for operation of the Crisis Resolution Act rests almost exclusively with the CNB whilst the Ministry of Finance of the Czech Republic has some joint powers together with the CNB in adopting and applying the government stabilisation tools (including the temporary public ownership (nationalisation) of all or part of a Czech Bank or a Large Czech Securities Dealer).

The Crisis Resolution Act provides for a special resolution regime applicable to Czech Banks and Large Czech Securities Dealers and distinguishes between two basic sets of measures. These measures are crisis prevention measures and crisis management measures (including crisis resolution measures and actions and the appointment of a special manager). The Crisis Resolution Act also deals with certain other matters (e.g. recognition of the effect of a third-country special resolution action under the laws of a country outside the EEA), however, these have no direct relevance to the issues considered in this memorandum or are not governed by Czech laws.

A more detailed description of recovery and crisis resolution measures and tools process is enclosed to this memorandum at Annex 2.

discharge from debts or other similar measure, (ii) reorganisation measures which are intended to preserve or restore the financial situation of a credit institution and which could affect third parties' pre-existing rights, including measures involving the possibility of a suspension of payments, suspension of enforcement measures or reduction of claims.

[20] On top of that, the Crisis Resolution Act also applies to financial institutions, financial holding companies, mixed financial holding companies and mixed activity holding companies as such are defined in the CRR.

6. ENFORCEABILITY OF CLOSE-OUT NETTING AND TRANSFER OF COLLATERAL PROVISIONS UNDER CZECH LAW PRIOR TO THE INSOLVENCY OF A CZECH ENTITY

Model CPMA / Model MNA

6.1 *Your opinion on whether a Transaction entered into under an Underlying Agreement or an Uncovered Transaction / Additional Netted Agreement would be validly included in each model Master Agreement, assuming either a choice of English or German law as governing such documents (save for the trading terms and conditions of the 2015 NBP Master which is governed by English law)? Please elaborate if your analysis depends on whether or not the relevant Transaction: (i) was concluded before or after the execution of each Master Agreement; or (ii) makes explicit reference to a Master Agreement or the relevant Underlying Agreement.*

(1) A Transaction entered under an Underlying Agreement or an Uncovered Transaction / Additional Netted Agreement will be included in each Master Agreement as long as such inclusion is valid under the governing law of each Master Agreement that is not Czech law (for discussion in respect of the governing law of the Master Agreements please see answer to question 6.8).

(2) There are no requirements under Czech law affecting this conclusion. Therefore, as long as the parties choose to include Underlying Agreements or Uncovered Transactions / Additional Netted Agreements into the Master Agreement, each Transaction entered into thereunder is to be included in the Master Agreement being arguably expressed as the intention of the parties pursuant to Section 2.1 of the MNA or Section 2.1 of the CPMA, as amended and restated in the Schedule.

(3) For that reason, Czech law is not relevant for an assessment whether it is necessary to enter into the Transaction before or after the execution of the Master Agreement, or whether the Master Agreement or the Underlying Agreement explicitly refers to the Transaction.

6.2 *Your opinion regarding the legality, validity and enforceability of each model Master Agreement (absent an insolvency of either party) to the netting and set-off of obligations due between the parties:*

(a) *under one or more physically settling Transactions involving the same commodity or product,*

(b) *under one or more physically settling energy Transactions involving two or more different classes or types of commodity or product, and*

(c) *under a combination of physically and financially settling Transactions (transacted under two or more Underlying Agreements).*

(4) The netting and set-off obligations will be recognized in the Czech Republic as long as they are valid, legal and enforceable under their governing law (for discussion in respect of the governing law of the Master Agreements please see answer to question 6.8).

(5) The sole fact that a party to the Master Agreement is required to apply regulatory margining to derivative transactions under EMIR does not affect the validity, legality or enforceability of the Master Agreement, neither the recognition of its netting and set-off provisions in the Czech Republic.

(6) This conclusion applies regardless of the types of Transactions entered into under the Underlying Agreement or an Uncovered Transaction / Additional Netted Agreement.

6.3 *An analysis and your opinion regarding the necessity or efficacy of performing any due diligence (i.e., lien searches, filings etc.) prior to a party entering into each model Master Agreement.*

(7) It is not necessary to conduct any searches or due diligence prior to entering into each Master Agreement. Generally, all types of Czech Entities are capable of entering into the Master Agreement.

(8) Nevertheless, a cautious counterparty may wish to verify the existence of the Czech Entity and to have a confirmation that it is not insolvent as of the moment of entering into the Master Agreement. For these purposes, it is possible to review the extract from the commercial register[21] or the insolvency register[22], respectively.

(9) Considerations of authority of the Czech Entity go beyond this memorandum, and thus we do not discuss them further. Should a party wish to revise a legal authority of a specific Czech Entity, we recommend seeking a specific legal advice. Although not covered in this memorandum, we note that this may be relevant in case of certain Czech Entities established by law or by a decision of a public body.

6.4 *A general discussion of, and your opinion regarding, your jurisdiction's laws relevant to the concepts of close-out netting and set-off of claims between parties, combinations of accounts or such other terminology as is employed in your jurisdiction to address such issues.*

(10) Czech law knows the concept of close-out netting as is relevant for the purposes of Close-Out or determination of the Final Net Settlement Amount under each Master Agreement. The definition of "close-out netting" (in Czech*, závěrečné vyrovnání)* is in Section 193 of the CMA and expressly reads as follows[23]:

(1) "Close-out netting" means a contractual arrangement under Czech or foreign law,

(a) *which can be evidenced in writing or alternatively by a record that allows its reproduction in an unaltered condition,*

(b) *which relates to claims of the contractual parties, including appurtenances to these claims, which are eligible to be secured by way of the financial collateral arrangement pursuant to the Financial Collateral Act (No. 408/2010 Coll., as amended, the* ***Financial Collateral Act****), or to claims, including appurtenances to those claims, from a financial collateral arrangement or from similar legal relation under foreign legal regulation, and*

(c) *according to which if an agreed event occurs, the termination and replacement of debts which correspond to the claims of the parties stated in (b) above, or set-off of undue or, as the case may be, even due claims of the parties stated in (b) above occurs so that the result will be one claim of one contractual party and a corresponding debt of the other contractual party to pay the resulting (close-out) amount.*

[21] Available online in Czech here: https://or.justice.cz/ias/ui/rejstrik.
[22] Available online in Czech here: https://isir.justice.cz/isir/common/index.do.
[23] Given their significance, for the purposes of this memorandum we have translated these definitions rather precisely and literally which may lead to some phrasing that seems unusual in English.

(2) The method of valuation of claims described in paragraph (1) lit. (b) above, the moment in time as to which the valuation must be performed, and the manner and time of the performance of the sole resulting claim must be included in a contractual arrangement on close-out netting and must not be contrary to the practice [(in Czech, *zvyklosti*)] *of the relevant financial markets.*

(3) A decision or another act of the court or administrative authority which affects rights of third parties and which was adopted with the aim of maintenance or recovery of the financial situation of one of the contractual parties, or with the aim of prohibition or restriction of performance of certain trades or transfer of monetary funds by one of the contractual parties, does not affect close-out netting arrangements provided that such close-out netting arrangement was entered into prior to the adoption of such decision or that other act.

(4) Paragraph (3) above will not apply to the effects of legal acts connected with the initiation of insolvency proceedings, entry to the liquidation proceedings or imposition of involuntary administration; exclusion of such effects are governed by different statutes.

(11) This definition of close-out netting is then used in the Insolvency Act where "close-out netting" is distinguished from "set-off"[24] (and even where close-out netting contains a set-off element such set-off is permissible in an insolvency situation). This distinction, included in Section 366(2) of the Insolvency Act, was required because post-bankruptcy set-off is generally permitted under Czech law only if certain qualifications are met. The Insolvency Act protects close-out netting by the catch-all Section 366(2) which reads: "[t]*he provisions of this Act do not affect close-out netting pursuant to the CMA, provided that the close-out netting arrangement has been entered into prior to the initiation of insolvency proceedings*". Please see our discussion of what constitutes the decisive moment of the initiation of insolvency proceedings in paragraph 5.

What claims or transactions may form a part of close-out netting under Czech law?

(12) The sole purpose of the cross-reference to the Financial Collateral Act in Section 193 of the CMA is to define the scope of claims which are eligible for "close-out netting" in line with the scope of claims which are eligible to be secured by financial collateral arrangements. The cross-reference serves for definition purposes only and does not mean (and cannot be interpreted as meaning) that only claims which are secured by a financial collateral arrangement are covered by the definition of "close-out netting".

(13) It follows that close-out netting as contemplated by the CMA covers only those claims (including their appurtenances) which are eligible to be secured by way of the financial collateral arrangement, or claims (including their appurtenances) from a financial collateral arrangement or a similar legal relation under foreign legal regulation. Section 6(1) of the Financial Collateral Act then provides that financial collateral may secure solely a **claim of a financial nature** including appurtenances to this claim regardless of whether it is a claim against the collateral provider or a third party.

(14) The definition of a claim of a financial nature contained in Section 2(a) of the Financial Collateral Act reads: "*claims of the contractual parties from contracts, the subject-matter of which are cash, investment instruments, emission allowances or commodities, as well as rights and claims related to those contracts*". Further, financial collateral, as expressly stipulated in Section 6(2) of the Financial Collateral Act, may also be arranged for claims of a financial nature which are conditional or which will arise in the future.

[24] As included in Section 10(1)(A) of the MNA or Section 10.1 of the CPMA.

(15) In order for receivables from the relevant contracts to be eligible for close-out netting, the subject-matter of such contracts must either be cash, investment instruments, emission allowances or commodities, as well as rights and claims related to those contracts, or such receivables must be claims either from a financial collateral arrangement or from a similar legal relation under a foreign legal regulation. Accordingly, **Transactions with the subject-matter of natural gas or power fall within the scope of claims of a financial nature and are eligible for close-out netting**.

(16) Section 3(1) of the CMA defines "investment instruments" as:

(a) investment securities;

(b) securities for collective investment;

(c) money-market instruments;

(d) options, futures, swaps, forwards and other instruments, the value of which relates to a rate or a value of securities, currency rates, interest rate or interest yield, emission allowances, as well as to other derivatives, financial indices or quantitatively expressed financial indicators which carry the right to cash settlement or delivery of the asset to which their value relates;[25]

(e) instruments enabling the transfer of credit risk;

(f) financial contracts for differences;

(g) options, futures, swaps, forwards and other instruments, the value of which relates to commodities, and which carry the right to cash settlement or the right of at least one of the parties to choose whether it wishes settlement in cash, unless the cash settlement is due to a default of a party to the derivative or due to another reason for an early termination of the derivative;

(h) options, futures, swaps, forwards and other instruments, the value of which relates to commodities and which carry the right to the delivery of this commodity and which are traded on a European regulated market[26] or on a multilateral trading facility or in an organised trading facility, except for wholesale energy products pursuant to Article 2(4) of REMIT[27], traded in an organised trading facility, from which arises a duty to supply the commodity;

(i) options, futures, swaps, forwards and other instruments, the value of which relates to commodities and which carry the right to the delivery of this commodity, which are not otherwise mentioned in subparagraph (h), are not for commercial purposes and which have the characteristics of other derivative investment instruments;

(j) options, futures, swaps, forwards and other instruments, the value of which relates to climatic indicators, freight rates or inflation rates or other economic indicators published by the official statistic department and which carry the right to cash settlement or the right of at least one of the parties to choose whether it wishes cash

[25] Pursuant to Article 10(1)(b) of MiFID II Regulation (as defined below) certain FX or currency forwards may not be considered as investment instruments (**Means of Payment Exemption**). The Means of Payment Exemption is only applicable if the parties want to qualify an FX or currency forward as a mean of payment and all conditions set out in Article 10(1)(b) of MiFID II Regulation are met.
Section 55(2) of the CMA defines a European regulated market as a market with investment instruments similar to a regulated market that is entered in the list of regulated markets of an EU Member State.
[27] Article 2(4) of REMIT defines wholesale products as, among others, derivatives relating to electricity or natural gas produces, traded or delivered in the EU and derivatives relating to the transportation of electricity or natural gas in the EU.

settlement, unless the cash settlement is due to a default of a party to the derivative or due to another reason for an early termination of the derivative;

(k) instruments, the value of which relates to assets, rights, debts, indices or quantitatively expressed indicators which are not set out in subparagraphs (a) to (j) and which have the characteristics of other derivative investment instruments; in particular those which are traded on a European regulated market or on a multilateral trading facility or in an organised trading facility; and

(l) emission allowances.

(17) Section 3(2) of the CMA defines "investment securities"[28] as securities which are tradable in the capital market. Investment securities are, in particular, the following:

(a) shares or similar securities representing a share in a legal entity;

(b) bonds or similar securities with which is associated the right to repayment of an owed amount;

(c) depositary receipts representing title to the securities listed under (a) and (b);

(d) securities entitling to acquire or dispose of the securities listed under (a) and (b); and

(e) securities which carry the right to cash settlement and the value of which is determined on the basis of the value of investment securities, currency exchange rates, interest rates, interest yields, commodities or financial indices or other quantitative measures.

There is no official guidance on how broadly the term "*which are tradable in the capital market*" should be interpreted. In our view the phrase is not intended to be particularly limiting and should be seen as simply requiring that such securities are fungible and that a market exists for such securities on which they are customarily traded. This view was informally and orally confirmed to us by a representative of the CNB.

(18) Section 3(3) of the CMA stipulates that "collective investment securities" are securities representing a share in investment funds or in foreign investment funds.

(19) Section 3(4) of the CMA defines "money-market instruments" as instruments which are customarily traded in the money market, in particular treasury bills, certificates of deposit and commercial papers.

(20) Section 3(5) of the CMA expressly states that payment instruments do not fall within the definition of investment instruments.

(21) Finally, Section 3(6) of the CMA stipulates that an investment instrument which falls within one category of investment instruments can also fall within one or more other categories of investment instruments.

(22) The above definition of investment instruments is based on the definition of financial instruments contained in Section C of Annex I to the MiFID II. Certain derivative products may not be covered by this definition of investment instruments and will not constitute investment instruments altogether. In particular, the scope of parts (g)-(k) of the definition is significantly restricted by the requirements (as applicable) that the instrument in question:

[28] These are called "transferable securities" in the MiFID II.

(a) carries the right to cash settlement or the right of at least one of the parties to choose whether it wishes settlement in cash, unless the cash settlement is due to a default of a party to the derivative or due to another reason for an early termination of the derivative; or

(b) is traded on a European regulated market or on a multilateral trading facility or in an organised trading facility; or

(c) is not for commercial purposes and at the same time has the characteristics of other derivative financial instruments (as these terms are defined in Article 7 and 8 of Commission Delegated Regulation (EU) 2017/565, which implements the MiFID II (**MiFID II Regulation**), and the CMA).

The above means that some forms of purely physically settled derivative products and other derivative products that could qualify as investment instruments only by virtue of Section 3(1)(k) of the CMA may not constitute investment instruments for the purposes of the CMA (see our further analysis in paragraph (23)).

We hope that formal statements from the relevant authorities (in particular, from the CNB), may help to clarify the position in respect of some forms of derivative products in the future. However, we are not yet aware of any statements that would provide the necessary clarification, save for the fact that the CNB tends to follow guidance contained in consultation papers and technical advice of the Committee of European Securities Regulators (**CESR**) and the ESMA. [29]

(23) As mentioned in the point directly above, if structured in particular ways, certain Transactions may fall outside the scope of the CMA's definition of investment instruments and therefore may not be eligible for close-out netting as defined in Section 193 of the CMA. To clarify, what follows is a list of those Transactions that, we believe, are eligible for close-out netting followed by those which *may not* be eligible unless certain steps are taken to ensure they are structured to fall within the scope of the legislation.

(a) Transactions which are eligible for close-out netting:

Basis Swap, Bond Option, Bullion Option, Bullion Trade, Commodity Option, Commodity Swap, Credit Protection Transaction, Credit Spread Transaction[30], Cross Currency Rate Swap, Currency Option, Currency Swap, Emissions Allowance Transaction, Equity Index Option, Equity Option, Equity Index Swap, Foreign Exchange Transaction, Forward Rate Transaction, Interest Rate Option, Interest Rate Swap, Swap Option, Total Return Swap, Weather Option and Weather Transaction.

Each of the above classes of Transaction will be eligible for close-out netting by virtue of qualifying as an investment instrument within the definition in Section 3(1) of the CMA, with the exception of Bullion Option, Bullion Trade, Commodity Option and Foreign Exchange Transaction (only to the extent it is to be settled on a "spot" or two-day basis), which are instead eligible for reasons described below.

A Renewable Energy Certificates ("RECs") Transaction does not qualify as an investment instrument but will nevertheless be eligible for close-out netting as its

[29] In particular, the CNB could find guidance in the following: CESR/CEBS's technical advice to the European Commission on the review of commodities business dated 15 October 2008 (Ref. CESR/08-752) and CESR's technical advice on possible implementing measures of the MiFID of April 2005 (Ref. CESR/05-290b) and ESMA Consultation paper – Guidelines on the application of C6 and C7 of Annex I of MiFID dated 29 September 2014 (Ref. 2014/1189) and Q&A on MiFID II and MiFIR commodity derivatives topics (ESMA70-872942901-36).

[30] We understand such Transactions to be "instruments enabling the transfer of credit risk".

"subject-matter" is a commodity. There is no definition of a commodity under the Insolvency Act, the CMA or in the Financial Collateral Act. However, Article 2(6) of the MiFID II Regulation defines a commodity as 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. Since the subject-matter of the Renewable Energy Certificates ("RECs") Transaction is electricity, we believe that it would fall under the definition of the contract whose subject-matter is a commodity as envisaged under the Financial Collateral Act.

Also, a Bullion Option, Bullion Trade, and Commodity Option may either qualify as an investment instrument under Section 3(1)(g) of the CMA, if the instrument in question carries the right to cash settlement or the right of at least one of the parties to choose whether it wishes settlement in cash (unless the cash settlement is due to a default of a party to the derivative or due to another reason for an early termination of the derivative), or, to the extent it falls outside the scope of Section 3(1)(g) of the CMA and does not qualify as investment instrument, be eligible for close-out netting because its subject-matter is a commodity.

Finally, a Foreign Exchange Transaction (to be settled on a "spot" or two-day basis) will be eligible for close-out netting by virtue of its "subject-matter" being monetary funds.

(b) Transactions where eligibility for close-out netting is dependent on certain characteristics:

These Transactions can be split into the following sub-categories:

(i) Repurchase Transaction, Buy/Sell Back Transaction and Securities Lending Transaction

Repurchase Transactions, Buy/Sell Back Transactions and Securities Lending Transactions do not qualify as investment instruments but will nevertheless be eligible for close-out netting, provided that only investment securities (as defined in point (17)), collective investment securities or instruments which are regularly traded in the money market (money market instruments) are the subject of the Repurchase Transaction, Buy/Sell Back Transaction or Securities Lending Transaction.

(ii) Cap Transaction, Collar Transaction, Economic Statistic Option, Economic Statistic Transaction and Floor Transaction

Each of these classes of Transaction will normally be eligible for close-out netting by virtue of qualifying as an investment instrument within the definition in Section 3(1) of the CMA.

The Transactions related to the following underlying assets must satisfy the criteria set out in the catch-all Section 3(1)(k) of the CMA in order to qualify as investment instruments: Cap Transaction, Collar Transaction, Economic Statistic Transaction or Floor Transaction, each relating to a rate or index, if that rate or index is not a financial index, quantitatively expressed financial indicator, inflation rate or an economic indicator published by the official statistics department.

Amongst other things, Section 3(1)(k) requires that the instrument in question "has the characteristics of other derivative financial instruments". The circumstances in which such an investment instrument is not for commercial purposes and has the characteristics of other derivative financial instruments are specified by Articles 7 and 8 of the MiFID II Regulation. The full wording of Articles 7 and 8 is attached as Annex 4.

The MiFID II Regulation sets out in Articles 7(3) and (4) and 8 the circumstances under which a contract of the type listed in Section 3(1)(k) of the CMA will be considered as not having the characteristics of other derivative financial instruments.

Most importantly, the Transactions covered by Section 3(1)(k) of the CMA would be eligible for close-out netting, unless a particular Transaction was entered into with or by an operator or administrator of an energy transmission grid, energy balancing mechanism or pipeline network, and it was necessary to keep in balance the supplies and uses of energy at a given time (paragraph 4 of Article 7 of the MiFID II Regulation).

(24) We believe that parties should avoid any adverse consequences arising from Transactions that may not be eligible for close-out netting by structuring borderline Transactions to incorporate the characteristics required by Czech law to make them eligible (e.g. in the case of a Bullion Option, to include a right to cash settlement), whenever that is commercially viable. Even if non-qualifying Transactions cannot be avoided in this way, it is our tentative[31] view that the inclusion of a Transaction which is not eligible for close-out netting as defined in Section 193 of the CMA should not invalidate the whole calculation (it should only result in the net amount being adjusted to reflect the exclusion of the non-qualifying Transaction). However, the point is not expressly addressed under Czech law and we are not aware of any useful case law on the point. A conservative approach would certainly be to document qualifying and non-qualifying Transactions under two separate Master Agreements to avoid the residual risk that the presence of non-qualifying Transactions in a close-out netting calculation would taint the entire mechanism in the eyes of a Czech court. Alternatively, the same result could be achieved for the purposes of Czech law by excluding these Transactions from the scope of the Master Agreement[32] and provide for them a separate close-out.

Further conditions to be met for close-out netting mechanism to be recognized under Czech law

(25) As mentioned above, Section 193(2) of the CMA requires the following conditions to be met in order for the relevant mechanism to be regarded as close-out netting: (i) the method of valuation of claims of the contractual parties (as defined in paragraph 193(1)(b) of the CMA, see paragraph (10)); (ii) the moment in time as at which the valuation must be performed; and (iii) the manner and time of the performance of the sole resulting claim:

(a) must be included in a contractual arrangement on close-out netting; and

(b) must not be contrary to the practice (in Czech, *zvyklosti*) of the relevant financial markets.

(26) The requirement of the absence of conflict with the practice on the relevant financial markets is less clear. There is no definition of either "the practice" or "the relevant financial markets" in the CMA or elsewhere in Czech law. No views of the relevant regulators or legal scholars have been published which would clarify the position.

31 The point is not expressly addressed under Czech law.
32 Provided that the amendment is valid and effective under the relevant governing law.

(27) First of all, it is important to establish which financial markets will be regarded as "relevant". Among the possible interpretations, a court may decide, for example, that the relevant market includes (i) the capital markets in general; (ii) OTC derivatives, commodities, repurchase, securities lending, or other similar markets; (iii) OTC swap, option, forward, or other similar markets; (iv) OTC interest rate swap, equity swap, currency swap or other similar markets; or (v) a market determined using some other criteria. It is common sense that, in the circumstances where a Czech Entity enters into a Master Agreement with a non-Czech counterparty, the cross-border (and not purely domestic) market should be regarded as "relevant".

(28) Although the phrase "practice" (in Czech, *zvyklost*) is not defined, the phrase "customs of trade" (in Czech, *obchodní zvyklost*), which is not dissimilar, is used in the Civil Code. Legal scholars describe "customs of trade" as certain stable rules which are in fact complied with by the market participants in general even though they are not expressly set out in a legal regulation.[33] Customs of trade do not have to be reflected in contractual documentation of market participants. Customs of trade may be limited to a particular geographical or business area or even a particular case.[34] The Czech courts have held that the existence of a particular custom of trade will be determined on a case-by-case basis. The Czech courts would, *inter alia*, examine the documentation usually entered into by market participants, invite witnesses and review relevant expert opinion(s).

(29) It is possible that in the absence of a definition of "the practice" the Czech courts would to a certain extent make an analogy with the definition of "customs of trade" in the Civil Code.

(30) The determination of whether or not the details set out in Section 193(2) of the CMA are contrary to the practice in the relevant financial market is largely a matter of fact. We are therefore unable to confirm the existence of any practice developed in the Czech Republic in any market regarding Transactions entered into by a Czech Entity and a non-Czech counterparty and which would relate to close-out netting. However, in our opinion the determination of the Final Net Settlement Amount is not very controversial as it works more like the calculation of a standard set-off. Nevertheless, for a Czech court it will be relevant whether the Underlying Agreement or Uncovered Transaction / Additional Netted Agreement contain any Close-Out mechanism recognizable as in line with the practice on a relevant market. Needless to say, ISDA Master Agreements (versions 1992 or 2002) seem to be frequently used for cross-border Transactions which are derivatives (and financial derivatives, in particular) and EFET Master Agreements for cross-border Transactions with commodities such as electricity/power or natural gas as subject-matter.

(31) Finally, we confirm that, as the Czech law definition is purely contractual and it is up to the Parties to decide what Transactions become its part, in respect of the CPMA the Parties should elect that its Close-Out mechanism applies to Uncovered Transactions.

CPMA CSA / MNA CSA

6.5 *Your opinion on whether the laws of your jurisdiction characterize each transfer of Eligible Credit Support as effecting an unconditional transfer of ownership in the assets transferred and whether there is any risk that such transfer would be re-characterized as intending to create or creating in favour of either party any mortgage, charge, lien, pledge, encumbrance or other security interest in any Eligible Credit Support transferred from one party to the other under each CSA. If so, please opine on whether there is any way to minimize such risk and the*

33 The market participants comply with the customs of trade not because of law but, for example, because it is advantageous for them to comply.

34 It is clear from Section 193 of the CMA that the practice would have to exist in the relevant financial market in general (i.e. it would not be sufficient if the practice existed just between the relevant several counterparties – market participants).

consequences of such a re-characterization to ensure the valid transfer of each type of Eligible Credit Support created by the providing party under each CSA.

(32) The obligations to transfer cash under the CSAs are governed by the law applicable to the CSAs. In line with Article 3(1) of the Rome Convention (with respect to CSAs entered into before 17 December 2009) or Rome I Regulation (with respect to CSAs entered into on or after 17 December 2009), being the applicable law for the determination of a governing law of agreements in civil and commercial matters in the Czech Republic, the governing law is the law chosen by parties to each CSA. Under the assumption that CSAs are governed by English or German law, Czech law is, therefore, not applicable for the determination whether obligations under the CSA are valid, legal and enforceable.

(33) Czech law would be relevant to the transfer of ownership of cash only if it governed proprietary aspects of such transfer. To determine whether Czech law would govern the proprietary aspects of the transfer of cash (in the meaning of our assumption 3.2(d), i.e. other than physical notes and coins), it is first necessary to establish the legal nature of cash as recognized under Czech law. In line with various Czech laws, including the Financial Collateral Act, cash may constitute:

(a) money credited to an account in the Czech or foreign currency; or

(b) claim for the repayment of money (which is a claim for the repayment of monies from an account in the Czech or foreign currency, or a similar claim for the repayment of monies).

(34) The above should reflect that cash will likely be considered the latter (i.e. a claim for the repayment of money) as a matter of Czech legal doctrine but may well be viewed as the former (i.e. money credited to an account). Cash credited to an account should in our view be regarded as a payment claim of the account holder against the relevant account bank.

(35) The transfer of cash legally operates by satisfying a former payment claim (of the Transferor against its account bank) and creating a new payment claim (of the Transferee against its account bank), while creating and satisfying various other payment claims to effect the transfer between the bank account of the Transferor to the designated bank account of the Transferee.

(36) Such transfer of cash does not involve any actual transfer of ownership in respect of cash, but it reflects the (i) satisfaction of a claim of the Transferor against its account bank; and (ii) creation of a new claim of the Transferee against the account bank keeping the designated account for such transfer. Therefore, rather than a transfer of ownership, the transfer of cash represents the cessation of a claim and the creation of a new one.

(37) Whether a claim has ceased or has been created must be determined pursuant to the relevant bank account agreement. Such assessment goes beyond the scope of this memorandum.

(38) Since the described transfer of cash does not include a transfer of ownership, it does not involve any proprietary aspects that would be subject to Czech law.

(39) For the sake of completeness, the risk of re-characterisation of the transfer of cash under the CSA as a security interest is further diminished by the fact that Czech law knows and creates security interest over cash only by pledging receivables from a bank account of a transferor. Accordingly, since the CSAs do not intend to create security interest in receivables, but obliges the parties to transfer the Eligible Credit Support in the form of cash, we believe that there is no risk of re-characterization of the transfer as the creation of a security interest.

(40) A letter of credit does not include any transfer of ownership. Its validity must be assessed separately by reviewing its terms under its governing law.

6.6 *Assuming the transferee receives absolute ownership interest in the Eligible Credit Support, your opinion on whether it will need to take any subsequent action to ensure that its title in the Eligible Credit Support continues. Your opinion should include whether there are any requirements in your jurisdiction necessary or advisable, including any filing registration, notification, stamping, notarization or any other action or the obtaining of any governmental judicial, regulatory or other order, consent or approval together with any 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.*

(41) Since Czech law is not applicable to the contractual aspects of the CSA, nor there are any proprietary aspects of the transfer of cash to be governed by Czech law, we confirm that no further actions need to be undertaken to ensure that the Transferee has continuing title in the received cash collateral.

6.7 *Your opinion on the effect, if any, under the laws of your jurisdiction of the right to a providing party incorporated or otherwise organized under your jurisdiction to exchange Eligible Credit Support (for example, by swapping cash for a letter of credit) pursuant to Section 6 of each CSA. Does the presence of consent to substitution by the receiving party have any bearing on this question.*

Since Czech law is not applicable to the contractual aspects of the CSA, nor are there any proprietary aspects of the transfer of cash to be governed by Czech law, it is not a matter of Czech law to assess the effects of exchange or substitution of the Eligible Credit Support.

6.8 *Your opinion on whether the parties' agreement on the governing law of each CSA and their submission to jurisdiction would be upheld in your jurisdiction, and what would be the consequences if they were not.*

Choice of law

(42) As already discussed above in paragraph (32), the choice of foreign law will be recognized in the Czech Republic, although the choice of law is subject to certain exceptions.

(43) The most notable exceptions under the Rome Convention are the following:

(a) if all the other elements relevant to the CSA at the time of the choice were connected with one country only, the fact that the parties have chosen English or German law would not prejudice the application of any mandatory rules under the laws of that other country which cannot be derogated from by contract;

(b) the chosen law will not restrict the application of any rules of Czech law in a situation where they are mandatory, irrespective of the law otherwise applicable to the relevant CSA. Unless mentioned otherwise in this memorandum, we consider it unlikely that any such rules would adversely affect our analysis;

(c) effect may be given to the mandatory rules of the law of another country with which the situation has a close connection, if and in so far as, under the law of the latter country, those rules must be applied whatever the law applicable to the CSA. In considering whether to give effect to these mandatory rules, regard would be had to their nature and purpose and to the consequences of their application or non-application; and

(d) the chosen law may not be applied if its application would be incompatible with Czech public order. We are not aware of any public order rule that would prevent the parties from complying with their duties under the CSAs.

(44) The most notable exceptions under the Rome I Regulation are the following:

(a) if all other elements relevant to the situation at the time of the choice were located in a country other than the country whose law has been chosen, the choice will not prejudice the application of provisions of the law of that other country which cannot be derogated from by agreement;

(b) following Brexit only, in case of each CSA governed by English law, if all other elements relevant to the situation at the time of the choice were located in one or more EU Member States, the choice of English law would not prejudice the application of provisions of EU law, where appropriate as implemented in the Czech Republic, which cannot be derogated from by agreement. We are currently not aware of any such provision;

(c) the chosen law will not restrict the application of overriding mandatory provisions of Czech law. Unless mentioned otherwise in this memorandum, we consider it unlikely that any such provisions would adversely affect our analysis;

(d) effect may be given to the overriding mandatory provisions of the law of the country where the obligations arising out of the CSA have to be or have been performed, in so far as those overriding mandatory provisions render the performance of the CSA unlawful. In considering whether to give effect to those provisions, regard would be had to their nature and purpose and to the consequences of their application or non-application; and

(e) the provisions of chosen law may not be applied if their application would be manifestly incompatible with Czech public order. We are not aware of any public order rule that would prevent the parties from complying with their duties under the CSAs.

Submission to jurisdiction of English or German courts

(45) Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (the **Brussels Regulation (recast)**) would apply to all legal proceedings instituted on or after 10 January 2015, whilst Council Regulation (EC) No 44/2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, which had been repealed, would continue to apply to judgments given in proceedings instituted before 10 January 2015. Under the Brussels Regulation (recast), submission by the parties to the jurisdiction of the English or German courts, as applicable, would generally be upheld. However, please note that:

(a) Czech courts would have jurisdiction over all matters relating to the constitution and existence of the Czech Entity. Czech courts would also always have jurisdiction in respect of the insolvency of a Czech Entity and in respect of the enforcement of a claim in the Czech Republic; and

(b) a Czech court would have jurisdiction if the defendant enters an appearance before the Czech court, except where the appearance was entered in order to contest the jurisdiction of the Czech court.

(46) A judgment given by an English or German court, as applicable, would be, subject to the exemptions provided for by the Brussels Regulation (recast), generally recognised in the Czech Republic without a review by the Czech court as to its substance.

(47) A judgment obtained in England or Germany, as applicable, would be enforceable in the Czech Republic provided that the conditions set out in the Brussels Regulation (recast) are complied with. These conditions include, most notably, the following:

(a) the judgment being enforceable in England or Germany, as applicable;

(b) an application by the party seeking enforcement complying with certain formalities set out in the Brussels Regulation (recast); and

(c) the judgment not being manifestly contrary to Czech public policy.

Submission to jurisdiction of an arbitral tribunal

(48) The Czech Republic is a party to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the **NY Arbitration Convention**). As long as an arbitral award is issued in line with the terms of the NY Arbitration Convention, it is recognisable and enforceable in the Czech Republic

6.9 *Your opinion as to whether under local law of your jurisdiction, each CSA complies with any mandatory margining requirements applicable under the laws of your jurisdiction.*

(49) There are no Czech law specific margining requirements other than those required under EMIR and the Commission delegated regulation (EU) 2016/2251 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories with regard to regulatory technical standards for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty.

6.10 *Your opinion on whether there are any other local law considerations that a recipient of Eligible Credit Support should consider in connection with taking and realizing upon the Eligible Credit Support from a providing party incorporated or otherwise organized under your jurisdiction.*

(50) There are no further considerations.

Model CPMA combined with the CPMA CSA / Model MNA combined with the Model CSA

6.11 *The transferee's right in relation to the transferred Eligible Credit Support upon the occurrence of a Close-Out Event will be governed by: (i) in the case of the CPMA, Section 4 of the CPMA (see Section 11 of the CPMA CSA); and (ii) in the case of the MNA, Section 8 of the MNA (see Section 12 of the MNA CSA). Assuming that Section 4 of the CPMA / Section 8 of the MNA is valid and enforceable in your jurisdiction insofar as it relates to the determination of a Final Net Settlement Amount by either party on the termination of Underlying Agreements, your opinion on whether Section 11 of the CPMA CSA / Section 12 of the MNA CSA is also valid to the extent that it provides for the Base Currency Equivalent of all the Eligible Credit Support provided under each CSA on the Determination Date to be included in the calculation of the Final Net Settlement Amount. In other words whether, contractually, the right of a party to apply collateral to a Settlement Amount is enforceable.*

(51) Our assessment set out under our responses to question 6.5 in paragraph (32) and question 6.8 in paragraphs (42) to (44) applies similarly also in respect to the Master Agreements.

Therefore, as long as the provisions of the Master Agreement are legal, valid and enforceable under its governing law, they would be recognized in the Czech Republic.

(52) The right of a party to the Master Agreement to apply collateral to a Settlement Amount is, therefore, not affected by Czech law.

6.12 *Your opinion on whether the opinions that you have expressed on: (i) the CPMA and the CPMA CSA; and (ii) the MNA and MNA CSA would change in the event that the parties agree to place the Eligible Credit Support with an independent third party collateral agent rather than a party to each Master Agreement and relevant CSA.*

(53) Our answers provided above would not change in the event that the parties to the Master Agreement agree to place cash as the Eligible Credit Support with an independent third party collateral agent rather than a party to each Master Agreement and relevant CSA, subject to that the contractual arrangement governing such relation is legal, valid and enforceable under its governing law and the assessment of its enforceability in the Czech Republic.

7. ENFORCEABILITY OF CLOSE-OUT NETTING AND TRANSFER OF COLLATERAL PROVISIONS UNDER CZECH LAW AFTER THE COMMENCEMENT OF THE INSOLVENCY PROCEEDINGS IN RESPECT OF THE CZECH ENTITY

For the purposes of answering the following questions in this part 7, we further assume that after entering into a Transaction and prior to its maturity, a Czech Entity becomes the subject of voluntary or involuntary insolvency proceedings in the Czech Republic and, subsequent to the commencement of the insolvency proceedings, either that entity or an insolvency official seeks to assume the confirmations representing profitable Transactions for the insolvent party and reject the confirmations representing unprofitable Transactions for the insolvent party.

Model CPMA / Model MNA

7.1 *Assuming the parties have not selected Automatic Close-Out of each Underlying Agreement (Division 1, Part II, Section C of the Schedule to the CPMA / Section 6.1 of the MNA Election Sheet) and/or none of the Underlying Agreements provide for automatic early termination upon certain insolvency events to apply to the entity incorporated in your jurisdiction, your opinion on whether the provisions of each model Master Agreement permitting the non-defaulting party to terminate all the Underlying Agreements (including Uncovered Transactions / Additional Netted Agreements, if applicable) and all the Transactions done under them upon the insolvency of its counterparty would be enforceable under the laws of your jurisdiction.*

(54) If the parties have not elected Automatic Close-Out to apply in relation to the Czech Entity, then under Section 5(1.) of the MNA or Section 2.2(a) of the CPM, the Terminating Party or the Closing-out Party, respectively, is entitled to give a notice designating a date on which all the Underlying Agreements, Uncovered Transactions or Additional Netted Agreements, as applicable, are Closed-Out.

(55) Although the question is not expressly addressed in the Insolvency Act[35], these termination provisions of the Master Agreements would be enforceable under Czech law. The Master Agreements are not governed by Czech law and the Czech insolvency court would, as a matter of Czech private international law, the Rome Convention and the Rome I Regulation be required to apply English/German law as the law governing the Master Agreements (including its termination provisions), subject to our answer to question 6.8 as well as the assumption that there is no relevant bilateral or multilateral international treaty in place and effect that would govern any private international law (conflict of laws) matter between the parties.

(56) There are no published court judgments or articles by legal commentators in the Czech Republic to suggest the invalidity or unenforceability under Czech law of contractual termination provisions in the context of performance of Close-Out enabling the non-defaulting Party to terminate the Underlying Agreements or Uncovered Transactions / Additional Netted Agreements, if applicable, following the occurrence of an insolvency event of default in respect of the defaulting party (such as the Insolvency Event under the CPMA or Winding-up/Insolvency/Attachment Closed-out Event as specified under Section 3(C)(III)(b) or (d) of the MNA).

(57) The definition of "close-out netting" in Section 193 of the CMA (as discussed in our answer to question 6.4) expressly foresees that, following the occurrence of an agreed event, the mutual receivables and obligations of the relevant parties which are covered by close-out netting may cease to exist.

[35] In connection with the winding-up and reorganisation of monetary institutions (in Czech, *peněžní instituce*) the International Private Law Act also expressly sets out that close-out netting arrangements are governed solely by the law which governs the contract applicable to such close-out netting arrangements.

(58) Generally, the enforceability of Close-Out provisions as specified under Sections 2 to 4.4 of the CPMA or Sections 4, 5, 7 and 8.1 to 8.3 of the MNA, is further expressly confirmed (with respect to the close-out netting mechanism as contemplated by the CMA) in Section 366(2) of the Insolvency Act, which sets out that the provisions of the Insolvency Act do not affect close-out netting pursuant to the CMA, provided that the close-out netting arrangement has been entered into prior to the initiation of insolvency proceedings.[36,37] Since termination of claims forms an integral part of the close-out netting mechanism as contemplated by the CMA, as far as such mechanism is concerned, the Close-Out provisions of the Master Agreement would be enforceable in insolvency proceedings in respect of a Czech Entity, provided that the Master Agreement and all relevant Transactions entered into thereunder are duly executed (i.e., in a way which can be evidenced in writing or alternatively by a record that allows its reproduction in an unaltered condition) prior to the moment when the initiation of insolvency proceedings takes its effects, i.e., any time prior to the moment of publication of the notice of initiation of insolvency proceedings in the insolvency register (please see our discussion of what constitutes the decisive moment of the initiation of insolvency proceedings in part 5).

7.2 *Assuming the parties have selected Automatic Close-Out of each Underlying Agreement (Division 1, Part II, Section C of the Schedule / Section 6.1 of the MNA Election Sheet) and/or all of the Underlying Agreements provide for automatic early termination upon certain insolvency events to apply to the entity incorporated in your jurisdiction, your opinion on whether the provisions of each model Master Agreement permitting the non-defaulting party to terminate all the Underlying Agreements (including Uncovered Transactions / Additional Netted Agreements, if applicable) and all Transactions done under them upon the insolvency of its counterparty would be enforceable under the laws of your jurisdiction.*

(59) Where the parties have elected Automatic Close-Out under the Master Agreement, and/or all of the Underlying Agreements, Uncovered Transactions or Additional Netted Agreements, as applicable, provide for automatic early termination upon certain insolvency events, all of the Underlying Agreements, Uncovered Transactions or Additional Netted Agreements, as applicable, will Close-Out automatically upon the automatic Close-Out of any of the Principal Agreements or Uncovered Transactions, as applicable, or the Automatic Termination of any Netted Agreement pursuant to its own terms (provided that all other Netter Agreements will automatically and immediately terminate as well), respectively.

(60) Our answer to question 7.1 is equally applicable here and is unaffected by the election of Automatic Close-Out. As such, and subject to the following, the automatic termination provisions of each Master Agreements would be enforceable under Czech law.

(61) It is possible that even adjustments[38] to the respective Settlement Amount made under Section 6.4 of the MNA would form part of close-out netting as defined in Section 193 of the CMA. It is possible that any payments or deliveries made by one party to the other (and retained by such other party) during the period from the relevant moment of Automatic Close-Out pursuant to Section 6.1 of the MNA to the date for payment determined under Section 8.3(B) of the MNA could be regarded by the Czech insolvency courts as unjust enrichment of the relevant recipient. However, whether or not this is the case would most likely be a question

[36] As to whether the Close-Out mechanism under the Master Agreements constitutes close-out netting as defined under Czech law, please refer to our answer to question 6.4.

[37] In order for a party to a Master Agreement to be able to file any net claim against a Czech Entity with the Czech insolvency court, it will need to follow the procedures specified in the Insolvency Act (otherwise the net amount could be disregarded in the Czech Entity's insolvency proceedings).

[38] Please note that in this memorandum we do not give any opinion on the treatment under the relevant Czech laws of the payments and deliveries that are made in the period between the moment of automatic early termination that occurs automatically and the date for the payment determined under Section 6.1 of the MNA, and that are reflected by the adjustments referred to in Section 6.4 of the MNA.

governed by the law governing the relevant MNA. If such payments or deliveries constituted unjust enrichment, we would argue that any claims for the return of such unjust enrichment would be covered by close-out netting because they constitute "a right and/or claim related to a contract" within the meaning of Section 2(a) of the Financial Collateral Act to which the definition of close-out netting contained in Section 193 of the CMA cross-refers (see above in our answer to question 6.4).

(62) Since the automatic Close-Out has certain practical disadvantages and because its election has no effect on the enforceability of the Close-Out mechanism under the Master Agreements under Czech law, we do not recommend its selection. Nevertheless, if the parties decide otherwise, it does not negatively affect our conclusions.

7.3 *Your opinion on whether the provisions of each model Master Agreement provide for the calculation of a single Final Net Settlement Amount (see Sections 3 and 4 of the CPMA / Section 7 and 8 of the MNA) upon the insolvency of a counterparty would be enforceable in an insolvency of a party that is organized under the laws of your jurisdiction.*

(63) Provisions providing for the calculation of a single Final Net Settlement Amount (i.e. Sections 3 and 4 of the CPMA or Section 7 and 8 of the MNA) (the **Final Net Settlement Amount Provisions**) would be enforceable upon the insolvency of the Czech Entity subject to that the requirements on the close-out netting contractual provision under Section 193 of the CMA, as discussed in our answer to question 6.4, are met and the following limitations.

(64) Settlement Amounts under each Underlying Agreement, Uncovered Transaction or Additional Netted Agreement are monetary claims of one party to be paid by the other. Therefore, they will always form a claim of a financial nature in the meaning of the Financial Collateral Act and as such will be eligible claims for the close-out netting arrangement in the meaning of Section 193 of the CMA. This also means that any interest accrued on the Settlement Amounts will be considered as accessions of these claims of a financial nature regardless of whether it is a claim against the collateral provider or a third party and so will also be eligible to form a part of the close-out netting arrangement. Therefore, all these claims forming part of the Final Net Settlement Amount will be protected from the negative consequences of the Czech insolvency laws in line with Section 366(2) of the Insolvency Act, provided that the Master Agreement has been entered into prior to the initiation of insolvency proceedings. For further details on the aspects of the close-out netting provisions that must be met for the Final Net Settlement Amount Provisions to be protected from effects of Czech insolvency laws, please refer to our answer to question 6.4.

(65) Nevertheless, there are two issues arising in respect of the close-out netting of the owed amounts under the Underlying Agreements, Uncovered Transactions or Additional Netted Agreements. Although they might go beyond the scope of this memorandum, we consider them too important not to mention them.

(66) The first issue is that, if the close-out netting provision under the Master Agreement is not automatic, a Czech insolvency court could decide that if a non-defaulting party cherry picked only certain Underlying Agreements or Additional Netted Agreements and closed them out separately instead of closing out all of them under the Master Agreement, such action would be contrary to the purpose of the protection of close-out netting mechanism under the Insolvency Act and unreasonably advantageous for such creditor in the insolvency proceedings. On the other hand, since Czech law does not require any party to close out all arrangements that may be closed out if only one of them is closed out in case of insolvency of the Czech Entity. Therefore, we believe that the risk that a Czech insolvency court would dismiss the effectiveness of close-out netting only under certain Underlying Agreements or

Additional Netted Agreements, instead of the global close-out netting under the Master Agreement is remote and does not have any basis in Czech insolvency law.

(67) The second issue relates to non-eligible Transactions for close-out netting. As we discuss above in our answer to question 6.4, certain Transactions under certain circumstances may not form part of a close-out netting arrangement under Czech law as they are not considered to be claims that can be secured under the Financial Collateral Act. This applies also to Uncovered Transactions or to such non-eligible Transactions under applicable Underlying Agreement, or Additional Netted Agreement, although, as discussed in point (64), claims arising as a result of close-out netting made under these agreements are of a financial nature, these Transactions cannot be closed out in this way due to their ineligibility in the first place. We base this conclusion on the fact that each Underlying Agreement or Additional Netted Agreement contains its own close-out netting mechanism and that as such must comply with the Czech law requirements to be protected from the negative effects of initiation of insolvency proceedings against the Czech Entity. Accordingly, if any such close-out netting were held as ineligible for the protection, it could endanger the enforceability of the Final Net Settlement Amount Provisions in the Czech insolvency proceedings. Therefore, we recommend curtailing all Transactions that are not eligible for close-out netting under Czech law outside the Transactions that are to be closed out under the Underlying Agreements or Additional Netted Agreements.

(68) The CPMA, in our opinion, complies with almost all requirements as required for close-out netting provision under Section 193 of the CMA as listed in point (10). Specifically, it is in writing, the Final Net Settlement Amount Provisions provide for set-off of debts arising under the Underlying Agreements, Uncovered Transactions or Additional Netted Agreements, its method of valuation of underlying claims is in the form of a simple set-off of the Settlement Amounts (after their eventual conversion to the Base Currency) and specifies the time and method of the Final Net Settlement Amount in Section 4.4(b). Nevertheless, the CPMA lacks any express limitation of the date on which the Closing-Out Party must perform the Close-Out as Section 2.2(a) of the CPMA states only that "[t]*he Closing-Out Party shall specify in a notice to the Closed-Out Party […] the date on which the Principal Agreements are Closed-Out pursuant to Section 2.1.*" In other words, the Agreement provides the Closing-Out Party with unlimited time for the determination of an early termination date, which a Czech insolvency court may view as a lack of the requirement of a close-out netting arrangement to include "*the moment in time as to which the valuation must be performed*". We, however, do not agree with such argument as the CPMA includes the process of determination of such time and it must be read together with the Close-Out Notice. Nevertheless, whether such determination is not contrary to the practice of the relevant financial markets is a separate question we cannot opine on. To avoid the risk of a Czech court assessing the Final Net Settlement Amount Provision under the CPMA as non-compliant with the requirements under Section 193 of the CMA, we recommend amending Section 2.2(a) by specifying a final date as of which the Closing-Out Party must perform the Close-out. For instance, this can be made by adding analogically to the MNA providing for this limit in the last sentence of Section 5(1) of the MNA.

(69) The MNA, in our opinion, complies with all requirements as required for close-out netting provision under Section 193 of the CMA as listed in point (10). Specifically, it is in writing, the Final Net Settlement Amount Provisions provide for set-off of debts arising under the Underlying Agreements, Uncovered Transactions or Additional Netted Agreements, its method of valuation of underlying claims is in the form of a simple set-off of the Settlement Amounts (after their eventual conversion to the Base Currency), determines the period when the non-defaulting party may specify the Early Termination Date and specifies the time and method of the Final Net Settlement Amount in Section 8(3) of the MNA.

(70) Finally, the question whether the Final Net Settlement Amount Provisions under each Master Agreement satisfy the Czech law requirement that the method of valuation of claims under each Underlying Agreement, Uncovered Transaction or Additional Netted Agreement, the moment in time as to which the valuation must be performed, and the manner and time of the performance of the sole resulting claim must not be contrary to the practice (in Czech, *zvyklosti*) of the relevant financial markets is a matter of fact. Although we may not provide a final legal assessment in respect of this question, our legal opinion is that we are not aware of any reasoning a Czech insolvency court could use to decide otherwise. For further discussion regarding the practice of the relevant financial market, see our assessment in points (25) to (30).

(71) Under Section 170(a) of the Insolvency Act, interest (including default interest) on claims of creditors which filed their claims in insolvency proceedings which accrued after the decision on insolvency was made on a debt that was incurred before the declaration cannot be satisfied in insolvency proceedings[39]. This also applies to interest (including default interest) on claims of creditors which become due after the decision on insolvency was made (Section 170(b) of the Insolvency Act)[40].

(72) This would probably catch interest payable under Section 4.5(c) of the CPMA and Section 8.4 of the MNA being payable following the decision on insolvency of the Czech Entity. This means that as the interest does not form part of the Final Net Settlement Amount, it would likely not be protected from the negative effect of the insolvency proceedings.

(73) A different set of rules applies to interest on secured debts. Interest which accrued in relation to the secured part of the debt after the decision on the method of resolving the debtor's insolvency may be satisfied under certain conditions.

(74) Further, it is debatable whether, in the event of a Czech Entity's insolvency, the Final Net Settlement Amount will in all circumstances become due and payable on the Final Settlement Date or Early Termination Date, as applicable. For example, this uncertainty exists in relation to a net amount which would otherwise under a Master Agreement become payable after the date of the declaration of bankruptcy in respect of a Czech Entity. Section 250 of the Insolvency Act sets out that one of the effects of the declaration of bankruptcy is that undue receivables against the bankrupt are deemed to be due and payable upon the declaration of bankruptcy.

(75) The formal interpretation would be, given Section 250 of the Insolvency Act, that the net amount becomes due and payable on the declaration of bankruptcy. In our view, although the point is not free from doubt, such interpretation would not be correct because it would be incompatible with Section 366(2) of the Insolvency Act, which sets out that the Insolvency Act does not affect close-out netting and agreement of parties on "the manner and the moment of the settlement" (see paragraphs (10) and (25)) forms an integral part of the close-out netting arrangement (and as a result of that the moment of settlement should not be affected by the Insolvency Act).

(76) It is also doubtful that parties to an agreement providing for close-out netting would be able to agree that certain evidence will be "conclusive". If any close-out netting provision under the Underlying Agreement, Uncovered Transaction or Additional Netted Agreement contains a provision stating that a certain fact is conclusive, such an arrangement will be unenforceable

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39 A similar rule applies under Section 170(e) of the Insolvency Act to a contractual penalty (liquidated damages) where the circumstances enabling one party to claim the payment of the contractual penalty came into existence after the decision on insolvency. Finally, Section 170(f) of the Insolvency Act excludes the costs incurred by a party as a result of its participation in insolvency proceedings.

40 The distinguishing feature between Sections 170(a) and 170(b) is whether the relevant debt or claim became payable before or after the decision on insolvency was made.

in the Czech insolvency courts since how to evaluate evidence submitted is in the sole discretion of the Czech courts.

(77) The implementation of the WUCI Directive in the Czech Republic represents further protection for the counterparties of Czech Banks. In line with Article 25 of the WUCI Directive, Section 113(2) of the International Private Law Act sets out that, by way of an exception from the rule that insolvency is governed by the law where the credit institution is licensed or similarly authorised, close-out netting arrangements shall be governed solely by the law of the contract which contains such arrangements. Nevertheless, we believe that this provision only duplicates the already discussed exemption pursuant to Section 366(2) of the Insolvency Act.

(78) Although views have been expressed to the contrary[41], in our view it is very uncertain whether any additional comfort in relation to the enforceability of close-out netting under the Master Agreement could be derived from the Insolvency Regulation[42].

7.4 *Your opinion on whether or not early termination, close-out netting or the calculation and payment of a Final Net Settlement Amount under the provisions of each model Master Agreement are voidable, challengeable or in any way vulnerable to deletion by a liquidator or any third party if insolvency procedures are later opened against a party that is organized under the laws of your jurisdiction.*

(79) Generally not, as the close-out netting arrangement is protected from the negative effects of insolvency proceedings in line with Section 366(2) of the Insolvency Act, provided that the conditions discussed in our answers to questions 6.4 and 7.3 are met.

(80) The exemption under Section 366(2) of the Insolvency Act does not, however, cover any acts that would be considered as avoidance transfers.

(81) The statutory rules on the avoidance transfers are set out in the Insolvency Act and apply only to transactions entered into by the Czech Entity that is subject to ongoing insolvency proceedings before a Czech insolvency court.

(82) Generally, a Czech insolvency administrator can challenge transactions through which a debtor has reduced the sums available for the satisfaction of its creditors or has favoured certain creditors at the expense of others. These transactions are referred to as ineffective legal acts. The Insolvency Act recognises three specific categories of ineffective legal acts: (i) transfers at undervalue, (ii) preference transfers and (iii) fraudulent transfers. However, the Czech High Court in Prague has ruled[43] that other types of legal acts can also be ineffective if they led to the reduction of sums available for the satisfaction of creditors.

(83) The ineffectiveness of a legal act, including an act deemed to be ineffective by the Insolvency Act if carried out by the debtor following the commencement of insolvency proceedings (e.g. disposals of assets contrary to the restrictions imposed by the Insolvency Act), is established by the decision of a Czech insolvency court. In order to commence the court procedure, the insolvency administrator must file an action with the insolvency court against the debtor's counterparty. The insolvency administrator has the sole right to challenge the ineffectiveness of legal acts and must do so within one year from the date of the decision on the debtor's

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41 Virgos, Miguel; Garcimartin, Francisco: The European Insolvency Regulation: Law and Practice, Kluwer Law International, Hague, 2004.

42 Please see "Protection for Bilateral Insolvency Set-off and Netting Agreements under EC Law" – a report published by the European Financial Market Lawyers Group (EFMLG), October 2004.

43 Decision of the High Court in Prague no. 15 Cmo 72/2010.

insolvency. If the insolvency administrator fails to file the claim within this period, the right to challenge the transaction will expire.

Transfers at Undervalue

(84) A transfer at undervalue is a legal act on the basis of which the debtor enters into a transaction without receiving consideration, or receives consideration substantially lower than the "usual price" for performing such a transaction, provided that the debtor entered into the transaction when insolvent or that the transaction led to the debtor’s insolvency. The insolvency administrator may challenge a transaction entered into with a third party (other than a group company) if entered into within **one year** prior to the initiation of insolvency proceedings (three years if it concerns a group company).

(85) There are several specific acts that are automatically excluded from being classified as transfers at undervalue. These include: (i) a performance imposed by statute; or (ii) a legal act which the debtor reasonably expected to bring a reasonable profit, provided that the act was not undertaken for the benefit of a group company and that the person for whose benefit the act was undertaken could not have discovered, acting diligently, that the debtor was insolvent or that the act might cause the debtor’s insolvency.

(86) In light of the assumption in 3.1(o) and under the assumption that all Transactions are made in good faith and for the purpose of compliance with the provisions of the Agreement, we believe that the Czech insolvency court would have to conclude that the Master Agreement was entered into under reasonable expectations to save costs or make profits for the Czech Entity and that the transfer of the Final Net Settlement Amount was then made in line with the agreed terms and undertaken at arm’s length.

Preferential Transfers

(87) A preference transfer is a legal act which results in a creditor receiving greater consideration than it would have received in the debtor’s bankruptcy, to the detriment of other creditors, provided that the debtor undertook the legal act when insolvent or that the legal act led to the debtor’s insolvency. The insolvency administrator may challenge a transaction entered into with a third party (other than a group company), if entered into within **one year** prior to the initiation of insolvency proceedings (three years if it concerns a group company).

(88) The following acts are not preference transfers: (i) the granting of security by the debtor for an existing obligation, provided that the debtor obtained reasonable consideration in return; (ii) a legal act undertaken at arm’s length (in Czech, *za podmínek obvyklých v obchodním styku*) pursuant to which the debtor received an adequate counter-performance or other proprietary benefit, provided that the act was not undertaken for the benefit of a group company and that the person for whose benefit the act was undertaken could not have discovered, acting diligently, that the debtor was insolvent or that the act would cause the debtor’s insolvency; or (iii) an act undertaken by the debtor in the course of a moratorium or after the commencement of insolvency proceedings under the conditions set out in the Insolvency Act.

(89) In light of the assumption in 3.1(o) and under the assumption that all Transactions are made in good faith and for the purpose of compliance with the provisions of the Agreement, we believe that the Czech insolvency court would have to conclude that the Master Agreement was entered into under reasonable expectations to save costs or make profits for the Czech Entity and that the transfer of the Final Net Settlement Amount was then made in line with the agreed terms and undertaken at arm’s length.

Fraudulent Transfers

(90) A fraudulent transfer is a legal act through which a debtor intentionally alienates its property so that it is not available for its creditors and where, given all of the circumstances, the counterparty was, or should have been, aware of the debtor's intention. The insolvency administrator may challenge fraudulent transfers if entered into within **five years** prior to the initiation of insolvency proceedings.

(91) In light of the assumption in 3.1(o) and under the assumption that all Transactions are made in good faith and for the purpose of compliance with the provisions of the Agreement, the condition of intentional alienation cannot be met.

7.5 *"Cross Category Netting" – since the model Master Agreements contemplates the inclusion of various types of master agreements and other trading documentation covering both physical and financial trading, your opinion on any applicable issues that need to be considered as to the enforceability of netting between physical and financial transactions or various categories of physical products (see Annex 3 for potential categories).*

Your opinion should include a discussion of your jurisdiction's insolvency laws as they would apply to the close-out and netting via each model Master Agreement of obligations under different categories or types of traded products, and

(a) *if any distinctions are applicable based on whether these products are traded under one or more Underlying Agreements,*

(b) *if any distinctions are applicable when attempting to use a model Master Agreement to net / set-off physically settled Transactions when these involve the purchase, sale and/or optioning of different commodity types or categories (e.g. the netting obligations related to gas, power and coal trading) ("Cross Product Netting"), and*

(c) *if any distinctions are applicable based on whether both financially settled swaps, swaptions and derivative transactions and physically settled forwards and options are traded under one or more Underlying Agreements with respect to each Master Agreement.*

(92) Inclusion of various types of master agreements and other trading documentation does not affect our conclusions above.

(93) In respect of treating of Transactions non-eligible for the protection of close-out netting provision from the negative impacts of Czech insolvency laws, see our answer to questions 6.4 and 7.3.

7.6 *Assuming that the parties have selected a Base Currency (Division 1, Part VI of the CPMA Schedule and section 8.3(C) of the MNA Election Sheet) other than the legal currency of your jurisdiction in which the insolvent party is organized, your opinion on whether payment of the Final Net Settlement Amount in that currency would be enforceable under the laws of your jurisdiction.*

(94) Pursuant to Section 175 of the Insolvency Act a receivable such as a single netting amount denominated in a foreign currency, i.e. not denominated in CZK, must be converted into CZK using the foreign exchange rate published by the CNB on the date when insolvency proceedings were initiated or, if such receivable became due earlier, on the date when such receivable became due.

(95) The Insolvency Act does not expressly specify that the payments by the insolvency administrator to creditors following the determination of the insolvency estate must be denominated in CZK. It is, however, likely that the Insolvency Act contains an implied assumption that payments to creditors will only be made in CZK as otherwise the conversion of a non-CZK denominated claim under Section 175 would not make much sense. There are also no provisions in the Insolvency Act regarding currency fluctuations. Furthermore, we have not seen any court resolution on the distribution of proceeds from the insolvency estate where a payment has been made in a currency other than CZK.

(96) Therefore, we believe that a Czech insolvency courts would not enforce a payment of the single netting amount in a currency nor a claim for the single netting amount other than CZK.

(97) Any payments in non-Czech currencies to non-residents may be restricted for a maximum period of 30 days unless prolonged by the approval of the Chamber of Deputies of the Parliament of the Czech Republic should a state of emergency (in Czech, *nouzový stav*) in the foreign exchange economy be declared by the Czech Government or its prime minister.

(98) If you wish, you may include an additional Close-Out Event for situations when a Czech Entity would not be able to perform its obligations under the Master Agreement or Transactions due to the declaration of the state of emergency. The language for this purpose may be as follows:

(99) "*Due to a state of emergency (in Czech, nouzový stav) having been declared by the Government of the Czech Republic, it becomes unlawful for a party (which will be the defaulting party) to perform any contingent or other obligation which that party has under any Transaction.*"

7.7 *Your opinion on whether the rights of a party are enforceable in accordance with the terms of each model Master Agreement, irrespective of the insolvency of the entity incorporated in your jurisdiction.*

(100) The enforceability of rights of a party to the Master Agreement entered into with the Czech Entity in case of its insolvency relating to its right to perform the Close-Out or to set off claims under the Final Net Settlement Amount Provisions under the Master Agreement are further discussed in our answer to question 7.3.

(101) In respect of other rights of the counterparty to the Czech Entity under the Master Agreement, the limitations discussed in part 5 (and namely 5.2) apply accordingly. If a specific issue arose, we recommend seeking an individual advice reflecting the facts of each case.

7.8 *Your opinion on whether the parties' agreement on governing law of each model Master Agreement and submission to jurisdiction will be upheld in your jurisdiction, and the consequences if it were not.*

See our answer to question 6.8, which is equally applicable.

7.9 *Your opinion on whether, pursuant to the Insolvency Regulation most provisions of which became directly applicable in all EU Member States as from 26 June 2017, a Czech insolvency court would apply the laws relevant to close-out netting and set-off of the governing law of each EU Master Agreement if they differ from the analogous insolvency laws of your jurisdiction (please see question 7.19(c) below where this topic is to be discussed at greater length). In addition, on the assumption that one or more Underlying Agreements is not valid, binding and enforceable in accordance with its own respective terms and conditions, your opinion on* *whether the close-out netting and/or set-off provisions under each Master Agreement would nevertheless become valid by operation of the Insolvency Regulation.*

(102) The Czech insolvency court would apply the governing law of the Master Agreement in respect of the relevant close-out netting provisions. For our conclusions regarding the enforceability of these provisions, see our analysis in answers to questions 6.4 and 7.3 above.

7.10 *In addition, on the assumption that one or more Underlying Agreements is not valid, binding and enforceable in accordance with its own respective terms and conditions, your opinion on whether the close-out netting and/or set-off provisions under each Master Agreement would nevertheless become valid by operation of the Insolvency Regulation.*

(103) As we stated in answer to question 7.3 in our view it is very uncertain whether any additional comfort in relation to the enforceability of close-out netting under the Master Agreement could be derived from the Insolvency Regulation. Therefore, even the validity of close-out netting under the Master Agreement should not be question of the Insolvency Regulation.

7.11 *A general discussion of, and your opinion regarding, whether or not the mere institution of proceedings seeking a judgment of insolvency and/or the opening of the proceedings has any implication on the enforceability or operation of the model Master Agreement.*

(104) The mere institution of proceedings seeking a judgment of insolvency and/or the opening of the proceedings has no implication on the enforceability or operation of the Master Agreement subject to our answer to question 7.7.

(105) The enforceability of rights of a party to the Master Agreement entered into with the Czech Entity in case of its insolvency relating to its right to perform the Close-Out or to set off claims under the Final Net Settlement Amount Provisions under the Master Agreement are further discussed in our answer to question 7.3.

7.12 *An analysis and your opinion regarding the advisability in your jurisdiction of using each model Master Agreement to impose uniform default events across all types and categories of trades (effectively superseding the default terms of underlying master agreements or deal documentation) as opposed to allowing such underlying default provisions to operate for their respective categories of trades even if to do so might permit close-out and set-off of some trades governed by the relevant Master Agreement, but not others.*

(106) We believe that no such amendment is necessary for the purposes of effecting the Close-Out. We would only recommend excluding the Transactions non-eligible for close-out netting under Czech law as discussed in our answers to questions 6.4 and 7.3.

CPMA CSA / MNA CSA

7.13 *Your opinion on whether an entity duly organized or incorporated under the laws of your jurisdiction (or its administrator, provisional liquidator, receiver, trustee or other similar official) will be able to recover any transfer of Eligible Credit Support made to the transferee during a certain "suspect period" preceding the date of the insolvency that makes the recovery vulnerable to being treated as preferential or otherwise suspect (or other similar treatment) by such official and therefore subject to avoidance. If such a "suspect period" exists, please give your opinion on whether the substitution of Eligible Credit Support by a counterparty during this period would invalidate an otherwise valid transfer, assuming that the exchanged assets are of no greater value than the assets that they are replacing. Please also include an analysis of the relevant time-period(s) surrounding the insolvency.*

(107) Generally, the insolvency administrator can claim that a transfer of Eligible Credit Support was an avoidance transfer. For full description of avoidance transfers, see our answer to question 7.4.

(108) If the substitute assets are not of greater value than the assets they are replacing, the substitution of financial collateral to the counterparty during the hardening period should not invalidate the transfer as such an action would not be considered to be detrimental to the debtor.[44] Such a transfer should therefore be considered valid, yet we are not aware of any court decision which would unambiguously support the conclusion.

(109) Considering the mark-to-market provisions of CSA we are of the opinion that a transfer of additional financial collateral would most probably not be considered detrimental to other creditors and would be considered valid.

(110) However, an act by which the debtor provided their property for the financial collateral of the already existing liability could be considered as an ineffective act.

7.14 *Your opinion on whether the transfer of additional Eligible Credit Support pursuant to the mark-to-market provisions of each CSA during any applicable "suspect period" described above is subject to avoidance, either because it will be considered to relate to an antecedent or pre-existing obligation or for some other reason.*

(111) Generally, the insolvency administrator can claim that a transfer of Eligible Credit Support was an avoidance transfer. For full description of avoidance transfers, see our answer to question 7.4.

(112) Our answer to question 7.14 applies analogically. Further, as long as the assumption in 3.1(o) and the assumption that all transfers of Eligible Credit Support are made in good faith and for the purpose of compliance with the provisions of the Agreement, we believe that a Czech insolvency court would not hold a transfer of Eligible Credit Support as an invalid and ineffective avoidance transfer.

7.15 *A general discussion of, and your opinion regarding, whether or not the mere institution of proceedings seeking a judgment of insolvency and/or the opening of the proceedings has any implication on the enforceability or operation of each CSA.*

(113) The mere institution of proceedings seeking a judgment of insolvency and/or the opening of the proceedings against the Czech Entity should, generally, not have any implication on the enforceability or operation of each CSA.

(114) As we discuss in our answer to question 6.5, Czech law is not applicable to the transfer of ownership of the Eligible Credit Support under the terms of each CSA. Therefore, as long as the CSA and compliance with its conditions are in line with their governing laws, a Czech court should recognize their validity.

(115) Following the commencement of insolvency proceedings, we must consider whether the transfer of the Eligible Credit Support is exempted from the effects of the Insolvency Act.

(116) The Insolvency Act contains one sweeping protective provision for financial collateral arrangements. Under Section 366(1)(b) of the Insolvency Act, the provisions of the Insolvency Act will not affect the exercise of all rights and fulfilment of all obligations arising

[44] In our view, from an economic perspective in its complexity, the position of the creditor is not improved by the substitution of the Eligible Credit Support made mark-to-market. By the same token, the position of other creditors is not deteriorated, even though formally new Eligible Credit Support is provided to a pre-existing liability.

in relation to a financial collateral arrangement pursuant to the Financial Collateral Act or an equivalent foreign legal regulation, provided that such financial collateral arrangement has been entered into and come into existence prior to the initiation of insolvency proceedings[45], or later on the same day if the Transferee can prove that it neither knew nor should have known about the initiation of the insolvency proceedings. The mere fact that the opening of the insolvency proceedings has been published in the insolvency register does not in itself mean that the Transferee knew or should have known about the initiation of the insolvency proceedings.

(117) The protection afforded to financial collateral arrangements by Section 366(1)(b) of the Insolvency Act also covers the new provisions of the Insolvency Act inserted by the Covid-19 Act.

(118) It follows that, subject to one caveat discussed below, the Transferee's rights to the Eligible Credit Support would be protected from the effects of the Insolvency Act, and therefore also from any competing claims of other general creditors against the insolvency estate, if the provision of the Eligible Credit Support under the CSA qualified as a financial collateral arrangement under the Financial Collateral Act or under an equivalent foreign legal regulation, as defined in Section 366(1)(b) of the Insolvency Act (together **Financial Collateral Arrangements**).

(119) As explicitly mentioned by Section 366(1)(b) of the Insolvency Act, and in line with Article 8 of Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements (the **Financial Collateral Directive**), Section 366(1)(b) will only protect Financial Collateral Arrangements if the Eligible Credit Support was provided before the information about the commencement of insolvency proceedings concerning the Transferor is published in the insolvency register, or later on the same day if the Transferee can prove that it neither knew nor should have known about the initiation of the insolvency proceedings.

(120) However, Section 366(3) of the Insolvency Act stipulates that, *inter alia*, the exemption under Section 366(1)(b)[46] of the Insolvency Act does not apply to those provisions of the Insolvency Act concerning the avoidance transfers as discussed above.

(121) Since the provision of the Eligible Credit Support is not governed by the laws of the Czech Republic, the following criteria should be met to increase the likelihood that the provision of the Eligible Credit Support is recognised as a Financial Collateral Arrangement which is a "*financial collateral arrangement pursuant to an equivalent foreign regulation*":

(i) The Eligible Credit Support should only be constituted by those types of assets which are classified as "cash" within the meaning of paragraph 1(d) of Article 2 of the Financial Collateral Directive[47].

(ii) The provision of the Eligible Credit Support should be evidenced in writing or in a legally equivalent manner (see paragraph 2 of Article 3 of the Financial Collateral Directive). Under the Czech law implementation set out in Section 9(2) of the Financial Collateral Act, this requirement applies to the provision of the Eligible Credit Support itself and the evidencing in legally equivalent manner to writing includes records proving a transfer of collateral that ensures unaltered reproduction. We believe that the

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45 This would be the commencement of its effects *vis-à-vis* third persons, i.e., publication of the initiation notice in the insolvency register.

46 Section 366 of the Insolvency Act contains an error in reference following its amendment. Section 366(3) incorrectly refers to Section 366(1)(d), which has been transformed into Section 366(1)(b) due to the amendment. We are of the view that Section 366 cannot be interpreted in a way other than described in this memorandum since Section 366(1)(d) does not exist anymore.

47 Money credited to an account in any currency, or similar claims for the repayment of money, such as money market deposits.

Czech insolvency court when applying Section 366(1)(b) of the Insolvency Act would qualify this requirement along the lines of the Czech implementation.

(iii) The obligations secured under the CSA should give a right to a cash settlement and/or delivery of financial instruments.

(iv) The Transferee and the Transferor should fall within one of the types of eligible legal entities listed in Annex 1.

(v) The Eligible Credit Support is surrendered to the Transferee, i.e., by crediting such Eligible Credit Support to the Transferee's designated account, or provided to it in another way that allows the Transferee or a person acting on its behalf to hold or otherwise legally or factually control such Eligible Credit Support.

(vi) The Transferee may enforce the Eligible Credit Support upon the occurrence of an agreed Close-Out Event in respect of the Transferor or another event, in a timely manner without any restrictions (e.g. a requirement to obtain a court order or another approval for enforcing the security interest in the Eligible Credit Support).

(122) The above conditions should be generally met when receiving the Eligible Credit Support from the Czech Entity, nevertheless, we recommend observing their compliance on a case-by-case basis.

7.16 *An analysis of local law issues surrounding the insolvency of a recipient of Eligible Credit Support, when the recipient of the Eligible Credit Support is an entity based in your jurisdiction, with the provider of the Eligible Credit Support being an entity based outside your jurisdiction. If title vests in the recipient because of an outright transfer of Eligible Credit Support, is there any way that a bankruptcy court in your jurisdiction can bolster or re-characterize the nature of the providing party's rights to that Eligible Credit Support.*

(a) *What rights does the providing party have against such an asset located in your local jurisdiction upon the insolvency of the recipient party?*

(b) *Are there other steps that the providing party should be taking to minimize its risk and best protect such an asset?*

(123) Our answer to question 7.15 applies analogically also in respect of this question.

(124) In line with Section 366(1)(b) of the Insolvency Act, the provisions of the Insolvency Act do not affect the exercise of all rights and fulfilment of all obligations arising in relation to a Financial Collateral Arrangement, provided that it has been entered into and come into existence prior to the initiation of insolvency proceedings, or later on the same day if the Transferee can prove that it neither knew nor should have known about the initiation of the insolvency proceedings.

(125) Section 366(3) of the Insolvency Act stipulates that, *inter alia*, the exemption under Section 366(1)(b) of the Insolvency Act does not apply to those provisions of the Insolvency Act concerning the avoidance transfers as discussed above.

(126) The Czech court would recognise the validity of a Financial Collateral Arrangement creating security interest under each CSA if it was valid under both its governing laws.

(127) Accordingly, the Transferor's rights arising under the CSA will be valid and enforceable even after the initiation of the insolvency proceedings in respect of the Transferee.

7.17 *An analysis of the rights and obligations of an insolvent party organized in your jurisdiction with respect to Eligible Credit Support held by a recipient party organized outside your jurisdiction. If title vests in the recipient because of an outright transfer of Eligible Credit Support, is there any way that a bankruptcy court in your jurisdiction can undermine or re-characterize the nature of the recipient's rights to that Eligible Credit Support?*

(128) See our assessment in our answer to question 7.15.

Model CPMA combined with the CPMA CSA / Model MNA combined with the MNA CSA

7.18 *Your opinion on whether the rights of the Transferee of Eligible Credit Support would be enforceable in accordance with the terms of: (i) the model CPMA and the CPMA CSA; and (ii) the model MNA and the MNA CSA, irrespective of the insolvency of the providing party incorporated or otherwise organized under your jurisdiction.*

(129) See our assessment in our answer to question 7.15 which applies analogically.

7.19 *A general discussion of, and your opinion regarding, your jurisdiction's insolvency laws, and any relevant terminology with an emphasis on law and precedent applicable to the concepts of close-out netting and set-off of claims between parties, and:*

(a) *how generally applicable statutory or common law set-off (or similar) rights could interact with the contractual netting and set-off rights contained in each Master Agreement, each CSA and each Master Agreement as modified by the relevant CSA;*

(b) *applicable law which might have an impact on the respective priorities assigned to such rights by a court in your jurisdiction; and*

(c) *specifically, whether the Insolvency Regulation affects local jurisdiction conflict of law rules such as overruling local jurisdiction insolvency laws if the parties to the Master Agreement have opted for a jurisdiction other than the jurisdiction relevant to the insolvent party. In particular, your opinion on whether or not a bankruptcy court in your jurisdiction would apply the Insolvency Regulation to close-out netting and/or set-off such that it would apply the governing law of the Master Agreement or CSA as the law applicable to close-out netting and/or set-off or whether it would seek to apply local law in its stead;*

(d) *whether, on the assumption that one or more Underlying Agreements is not valid, binding and enforceable in accordance with its own respective terms and conditions, the close-out netting and/or set-off provisions under each Master Agreement when combined with the relevant CSA would nevertheless become valid by operation of the Insolvency Regulation; and*

(e) *whether the laws of your jurisdiction consider set-off and close-out netting as separate or similar rights.*

(130) See our assessment in our answers to questions 7.3, 7.4 and 7.15 which applies analogically.

8. CROSS AFFILIATE CLOSE-OUT NETTING AND SET-OFF

Since the versions of the model CPMA and model MNA you are reviewing do not address this topic and are not intended for these purposes, but because this issue may be of use to some EFET members, only to the extent that there is established law in your jurisdiction on the subject, a summary of such law and a review of the different risk considerations involved in choosing to add multiple parties to each model Master Agreement.

(131) Cross affiliate close-out netting or set-off is not an established concept under Czech law.

9. MULTI-BRANCH PARTIES

In the case of a counterparty that has entered into Transactions under a Master Agreement as a multi-branch party, it is clearly necessary to obtain enforceability opinions from each country where a branch of that counterparty is located that has entered into one or more Transactions under that Master Agreement. In this regard, please provide your opinion on the following:

9.1 *Would be any change in your conclusions expressed in Parts 6 and 7 above concerning the enforceability of close-out netting under each Master Agreement and each Master Agreement combined with the relevant CSA (given the assumption in 3.3(a), i.e. if a Non-Czech Branch enters into a Transaction for the benefit of the Czech Entity))?*

(132) For the purposes of the below we assume that the Czech Entity's centre of main interests (COMI) in the meaning of Article 3(1) of the Insolvency Regulation is in the Czech Republic.

(133) As a matter of Czech law, Non-Czech Branches of a Czech Entity would not be regarded as separate entities (being branches we assume they would not be separate legal entities independent from their founder). The Non-Czech Branches' acts (including the entry into the various Transactions) would be attributed to the founder, i.e. the Czech Entity. Therefore, our relevant conclusions expressed in Parts 6 and 7 above would remain unaffected

(134) Where the Insolvency Regulation is applicable to the Czech Entity, in line with Article 3(1) of the Insolvency Regulation the Czech insolvency courts have jurisdiction to open main insolvency proceedings with respect to the Czech Entity. In general, the effects of main insolvency proceedings cover all of the debtor's assets located in the EU Member States. Any commencement of insolvency proceedings should be recognized in all EU Member States as of the date it becomes effective in the Czech Republic.

(135) After the commencement of the main insolvency proceedings in an EU Member State, secondary insolvency proceedings[48] may be commenced in other EU Member States against branches and other assets located in such other EU Member States. Furthermore, pursuant to Article 12(1) of the Insolvency Regulation, the effects of insolvency proceedings on the rights and obligations of the parties to a payment or settlement system or to a financial market will be governed solely by the law of the EU Member State applicable to that system or market.

(136) Besides the above, we note that in situations where the Czech Entity is a Czech Bank, the Insolvency Regulation is not applicable to it and following the implementation of the WUCI Directive through the Insolvency Act:

(i) the Insolvency Act does not apply to the Czech Bank unless the Czech Bank's banking licence has been revoked;

(ii) the principle of single universal insolvency proceeding across the territory of all EU Member States has been introduced for banks and their branches having a single European banking licence.

9.2 *Could separate proceedings be brought in the Czech Republic with respect to assets and liabilities of the Czech Branch upon the commencement of insolvency proceedings against the Foreign Counterparty in a respective foreign country (the **Country H**)? Your opinion should include how the relevant authorities in the Czech Republic would treat the proceedings in an outside jurisdiction by, for example, deferring to them so that the assets and liabilities of the*

[48] Secondary insolvency proceedings commenced in the Czech Republic are governed by the Insolvency Regulation and partly also by Section 430a of the Insolvency Act.

Czech Branch would be treated as part of the proceedings against the Foreign Counterparty. Please also include whether or not in your opinion local creditors of the Czech branch would be able to initiate separate proceedings in the Czech Republic even if the relevant authorities did not do so.

(137) Further to the applicable assumptions as set forth in Part 3 (and namely 3.3(b)) above, we have assumed the following.

(a) the Foreign Party's centre of main interest (COMI) in the meaning of Article 3(1) of the Insolvency Regulation is outside the Czech Republic; and

(b) after entering into these Transactions and prior to the maturity thereof, the Foreign Counterparty becomes the subject of voluntary or involuntary proceedings under the insolvency laws of Country H and close-out netting provisions under the Master Agreements would be enforced in accordance with their respective terms in these proceedings against the Foreign Counterparty.

(138) As a starting point, the Insolvency Act does not contain any provisions dealing with cross-border insolvency proceedings other than those which are applicable within the European Union in the circumstances where the Insolvency Regulation or the WUCI Directive applies.

Insolvency proceedings commenced under the regime set out in the Insolvency Regulation

(139) In accordance with the Insolvency Regulation, after the commencement of the main insolvency proceedings in an EU Member State, secondary insolvency proceedings may be commenced in the Czech Republic against the Czech Branch. The effects of such proceedings are restricted only to the assets and liabilities of the respective Czech Branch. The Czech insolvency administrator is obliged to cooperate with the insolvency administrator appointed in the main insolvency proceedings and *vice versa* and must give that insolvency administrator an early opportunity to submit proposals on the realization or use of the assets in the secondary insolvency proceedings.

(140) The commencement of the secondary insolvency proceedings may be requested by the insolvency administrator in the main insolvency proceedings or any other person or authority empowered to do so under Czech law, including local Czech creditors whose claims arise from or are in connection with the operation of the Czech Branch.

(141) At the request of the insolvency administrator or the Foreign Counterparty, being a debtor in possession, the Czech insolvency court may stay the commencement of secondary insolvency proceedings of the Czech Branch for up to three months if:

(i) a temporary stay of individual enforcement proceedings have been granted in order to allow for negotiations between the debtor and its creditors; and

(ii) suitable measures are in place to protect the interests of local creditors.

(142) Where the Insolvency Regulation is applicable, after the commencement of the secondary insolvency proceedings, any judgments handed down by an insolvency court deciding on the main insolvency proceedings concerning the course and closure of the insolvency proceedings, and compositions approved by that court, will be recognized in the Czech Republic with no further formalities under Article 32 of the Insolvency Regulation.

(143) The Czech insolvency courts may also commence insolvency proceedings in respect of the Czech Branch of Foreign Counterparties that are not covered by the Insolvency Regulation[49] if its opening is requested by a creditor residing or seated in the Czech Republic or whose claim against the Foreign Counterparty has arisen in connection with the activities of the Czech Branch. In this case, the Czech insolvency proceedings only apply to the Foreign Counterparty's assets located in the Czech Republic.

(144) Based on the above, we are of the opinion that close-out netting should be recognized and executed accordingly. The Czech insolvency administrator should thus be bound by the close-out netting and the netting rights of the counterparty of the Foreign Counterparty executing the Master Agreement and any Transactions via its Czech Branch, subject to our analysis set out in our answers to questions 6.4, 7.3 and 7.4 above.

Insolvency proceedings commenced under foreign law outside the scope of the Insolvency Regulation

(145) In the scenario where neither the Insolvency Regulation nor the WUCI Directive apply (i.e. when the Foreign Counterparty is located outside the EEA), in general, upon the start of the insolvency proceedings for the Foreign Counterparty in the Country H no separate proceedings would automatically start in the Czech Republic with respect to the assets and liabilities of the Czech Branch.

(146) If insolvency proceedings are started in the Country H in respect of the Foreign Counterparty, generally, such proceedings would not have any effect in the Czech Republic[50] (but see below in relation to Czech Branches of EEA banks). In the absence of a bilateral or multilateral treaty (and we are not aware of any relevant treaty relating to the recognition of foreign insolvency proceedings[51]) the proceedings would only be recognised in the Czech Republic if there were reciprocity between the Czech Republic and the Country H (again we are not aware that this is the case in relation to insolvency proceedings). Further, if the proceedings are recognised in the Czech Republic, the Czech insolvency court delivers to a court in the Country H only a movable property of the Foreign Counterparty that remained after satisfaction of rights on exclusion from the bankruptcy assets of the Foreign Counterparty in the Czech Republic and rights of secured creditors.

(147) Moreover, save as set out below, under Czech law the relevant authorities in the Czech Republic would not be required in such circumstances to defer to the proceedings in the Country H.

(148) Should the conditions be satisfied under the Insolvency Act for the initiation of insolvency proceedings in respect of the Foreign Counterparty (not only in respect of the Czech Branch), insolvency proceedings in the Czech Republic could be initiated by the Foreign Counterparty or its creditors (with usual place of residence or registered office in the Czech Republic, or if a creditor's receivable has arisen in connection with its business activities in question) in the Czech insolvency court.[52] But please see also below.

(149) The insolvency proceedings in the Czech Republic would apply to the Foreign Counterparty's assets located in the Czech Republic as well as to its assets located outside the Czech Republic. It is however uncertain how the inclusion of the assets located outside the Czech Republic would be implemented in practice. This is likely to depend on the legal system of

[49] For instance, it is not applicable to Foreign Banks.

[50] One exception from rule is if the Foreign Counterparty ceases to exist as a result of winding up proceedings outside the Czech Republic. As a matter of Czech law, corporate existence is considered under the law of the state where the relevant legal entity is incorporated.

[51] The Insolvency Regulation does not apply to credit institutions.

[52] Although we are not aware of any occasion where this has actually occurred.

the state where the assets are located and to require the cooperation of the authorities of that state.

Special Regimes applicable to EEA Foreign Banks and EEA Foreign Large Securities Dealers

(150) In relation to an EEA Foreign Bank (i.e. where the Foreign Counterparty has its registered office within the EEA and possesses a single European banking licence) the situation as described in this paragraph above is significantly different given the implementation of the WUCI Directive in the Czech Republic through the Insolvency Act. Following the implementation of the WUCI Directive:

(i) the Insolvency Act does not apply to a Czech Bank unless the Czech Bank's banking licence has been revoked;

(ii) the principle of single universal insolvency proceeding across the territory of all EU Member States has been introduced for banks and their branches having a single European banking licence. This means that Czech Branches of foreign banks operating in the Czech Republic on the basis of a single licence regime are also insolvent provided that the collective insolvency proceedings were initiated and held by administrative and judicial institutions of another EEA state with the purpose of a sale of assets under supervision of these institutions, including cases where such proceedings are terminated by discharge of debt or similarly.

(151) When facing the Czech Branch of the Foreign Counterparty where the Foreign Counterparty is not an EEA Foreign Bank, consideration should also be given to the application of the Crisis Resolution Act to the Czech Branch.

(152) The Crisis Resolution Act and the BRRD are discussed in more detail in the part 5.4 and Annex 2 as they apply to a Czech Bank or a Large Czech Securities Dealer. Certain terms defined in paragraph the part 5.4 and Annex 2 are used in the discussion that follows.

(153) The powers under the Crisis Resolution Act can be exercised, subject to certain modifications, by the CNB in respect of a third country institution (a **Third Country Institution**), being broadly an entity the head office of which is established in a country outside the EU that would, if it were established within the EU, be a credit institution or an investment firm as defined in the BRRD, in circumstances where a Third Country Institution (or third-country parent undertaking) is subject to resolution action in a state other than an EEA state (a **Third Country Resolution Action**).

(154) Where, pursuant to Section 195 of the Crisis Resolution Act, the CNB chooses to recognise a Third Country Resolution Action, in whole or in part, the CNB may, for the purposes of supporting, or giving full effect to, the Third Country Resolution Action (or its part), exercise, in relation to a Third Country Institution, one or more of crisis resolution measures or tools available to the CNB in relation to a similar entity in the Czech Republic.

(155) Under the Crisis Resolution Act, the crisis resolution measures or tools may generally apply to: (i) assets of the Third Country Institution or its group located in the Czech Republic or governed by Czech law; and (ii) rights or liabilities of the Third Country Institution that are booked by its Czech Branch or governed by Czech law.

(156) It remains to be seen how these powers will be exercised by the CNB. However, the relevant provisions of the Crisis Resolution Act, as discussed above, make it clear that the crisis resolution measures or tools are only available in respect of the Third Country Institution to the extent that they would be available in respect of a similar entity in the Czech Republic.

Moreover, the relevant provisions of the Crisis Resolution Act make it clear that such measures and tools are available to the CNB for the specific purpose of supporting or giving effect to the Third Country Resolution Action carried out by the relevant third country resolution authority, and only to the extent necessary to support such Third Country Resolution Action.

(157) Accordingly, please refer to the analysis in paragraph 3.3(e) above in respect of a Czech Bank and a Large Czech Securities Dealer, on which basis we do not consider that the above described rules or powers would have any adverse impact on the conclusions in this memorandum.

(158) However, it should be noted that, where the CNB recognises a Third Country Resolution Action (or a part of it), in addition to the availability of crisis resolution measures or tools in respect of the Third Country Institution, such Third Country Resolution Action (or part of it) produces the same legal effects in the Czech Republic as it would have produced had it been made (with due authority) under the law of the Czech Republic. Yet, it can be inferred from the text of the Crisis Resolution Act that to qualify as a Third Country Resolution Action, the anticipated results of the third country action must be broadly comparable to the results which could have been anticipated from the exercise of a crisis resolution measure or tool in relation to an entity in the Czech Republic corresponding to the relevant third-country institution or parent undertaking and the objectives of the action must also be broadly comparable to those set out in the Crisis Resolution Act. In any case, the nature and effect of the recognised Third Country Resolution Action is ultimately a question for the relevant foreign law.

(159) Note that above we discuss the position with respect to Third Country Institutions but the Crisis Resolution Act also provides for the recognition of resolution action in respect of third-country parent undertakings.

9.3 *In the event that proceedings are brought in the Czech Republic with respect to the assets and liabilities of the Czech Branch, would the administrator, provisional liquidator, receiver, trustee or other similar official and/or the courts in the Czech Republic include the Foreign Counterparty's position under its Underlying Agreements or Transactions among the assets of its Czech Branch? If so, would the administrator, provisional liquidator, receiver, trustee or other similar official and/or the courts in the Czech Republic recognize their respective close-out and netting provisions in accordance with their terms? You may assume that the close-out netting provisions under the relevant Underlying Agreements or Transactions would be enforceable in the proceedings against the Foreign Counterparty brought outside the Czech Republic.*

(160) Our conclusions in respect of the recognition of close-out netting provisions do not differ from the conclusions set out in our answers to questions 7.3 and 7.4.

(161) If there were separate (secondary) insolvency proceedings in respect of the Foreign Counterparty in the Czech Republic, following the carrying out of close-out netting, the insolvency administrator and the Czech courts, on the facts above, could include the Foreign Counterparty's obligation (if any) corresponding to the net amount payable under the Final Net Settlement Amount Provisions among the assets which are subject to the insolvency proceedings in the Czech Republic and regardless of whether the Master Agreement was entered into on a multibranch basis or not.

10. CSA SPECIFIC PERMUTATIONS.

In relation to each of the questions in paragraph expressed in Parts 6 and 7 above concerning the enforceability of transfers of Collateral, the assumption is that the Transferor is the Czech Entity. Please consider your answer to each question and indicate how your answer would be different, if at all, assuming instead that:

10.1 *The Transferee is a branch located in the Czech Republic of a bank organised outside the Czech Republic.*

(162) Our conclusions above would remain unaffected.

10.2 *The Transferee is neither incorporated nor otherwise organised in nor a branch located in the Czech Republic, but has assets in the Czech Republic.*

(163) Our conclusions above would remain unaffected.

10.3 *None of the above applies to the Transferee (that is, it has no connection with the Czech Republic), but the margin was issued by the government of the Czech Republic or comprises cash in the lawful currency of the Czech Republic.*

(164) Our conclusions above would remain unaffected. Nevertheless, the parties may wish to include such action as an additional Close-Out Event.

11. CHOICE OF LAW AND JURISDICTION

11.1 *Given your above stated assumptions, are the: (i) CPMA and the CPMA CSA; and (ii) MNA and the MNA CSA legal, valid and binding under the laws of your jurisdiction?*

(165) See our answers to questions 6.8 and 7.8.

11.2 *Are there any applicable limitations on the courts in your country with regard to upholding a choice of local law and submission to the jurisdiction of local courts*

(166) See our answers to questions 6.8 and 7.8.

12. OTHER PROVISIONS

Are there any other provisions of either Master Agreement or either CSA that, given a choice of your local law, either (a) need to be revised in order to be enforceable in your jurisdiction; or (b) the legal efficacy of which could be materially improved upon or optimized with different wording (given such provision's apparent intent)? Please provide suggested revisions.

(167) The Master Agreements and CSAs are not governed by Czech law. Accordingly, besides what is otherwise stated on our advice above, we do not recommend any further revisions in the provisions of any Master Agreement and any CSA.

13. RECENT & PENDING DEVELOPMENTS:

Please highlight any recent or anticipated future developments in the laws, rules and/or regulations of your jurisdiction or those of the European Union that may affect the laws of your jurisdiction and any of the opinions that you have provided in respect of each Master Agreement and each CSA.

(168) We are not aware of any recent and pending developments materially affecting our assessment or conclusions discussed or provided in this memorandum.

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Petr Vybíral
Partner
on behalf of **Allen & Overy (Czech Republic) LLP, organizační složka**

ANNEX 1

ELIGIBLE LEGAL ENTITIES TO THE FINANCIAL COLLATERAL ARRANGEMENTS

Czech law limits the types of parties which are eligible to enter into a Financial Collateral Arrangement if conditions set out in special laws are complied with[53]. The types of parties correspond to those listed in Article 1(2) of the Financial Collateral Directive. We list below only those we believe are most relevant for the purposes of this memorandum:

(a) a bank;

(b) other credit institution as defined in point (1) of Article 4(1) of the CRR as well as persons listed in Annex I Sections 2 – 12 of Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC;

(c) an insurance company, reinsurance company, investment firm, management company, investment company or pension fund;

(d) a central counterparty, settlement agent or clearing house pursuant to a special law regulating payment services;

(e) a savings and credit co-operative;

(f) a legal person that trades on its own account with investment instruments for hedging purposes in respect of trades with investment instruments, that are not financial instruments in the meaning of the Financial Collateral Act[54], and such activity is one of its principal activities;

(g) a legal person that trades on its own account with commodities or investment instruments, that are not financial instruments in the meaning of the Financial Collateral Act[55], and such activity is one of its principal activities;

(h) a foreign entity with a similar scope of business or activity as any of the persons listed above;

(i) a state or a member state of a federation;

(j) a municipality or region or an analogous foreign entity;

(k) a central bank; or

(l) any other legal entity or a foreign person other than a natural person (including a corporate/company) as long as the other party qualifies as one of the entities envisaged in points (a) to (k) above.

53 Section 7 of the Financial Collateral Act.
54 Section 2(c) of the Financial Collateral Act.
55 Section 2(c) of the Financial Collateral Act.

ANNEX 2

APPLICABLE RESOLUTION REGIMES IN RESPECT OF CZECH BANKS AND LARGE CZECH SECURITIES DEALERS

Crisis Prevention Measures

The crisis prevention measures represent, for the most part, early intervention measures and as such can be described as pre-resolution measures or tools. Their main goal is to prevent the spread of financial problems among Czech Banks.

Accordingly, if a situation arises whereby shortcomings in a Czech Bank's activities, including by virtue of breaches or series of breaches of the Crisis Resolution Act, the BRRD or the Banks Act (including various deficiencies or impediments to recoverability of the Czech Bank), endanger the stability of the banking or financial system, the CNB may, among other things, gradually: (i) impose specific administration measures on the Czech Bank in order to remedy the shortcomings or breaches and/or address or remove deficiencies or impediments to recoverability[56], (ii) remove the Czech Bank's senior management and executive board members and make the appointment of new senior management and executive board members conditional upon the CNB's prior consent, or (iii) impose temporary administration by virtue of the appointment of a temporary administrator.[57]

It is important for the purposes of this memorandum that nothing under the crisis prevention measures controls what a third party may or may not do *vis-à-vis* the Czech Bank as a debtor and so we believe that neither the onset of temporary administration nor the exercise of any other crisis prevention measures will affect the enforceability of close-out netting or validity and enforceability of financial collateral arrangements under Czech law.

In addition, in this context we note that, pursuant to Sections 59 to 74 of the Crisis Resolution Act (which is also technically a pre-resolution measure or tool), the CNB must, prior to or simultaneously with exercising of certain crisis resolution measures pursuant to the Crisis Resolution Act (i.e. a transfer to a private sector purchaser, a transfer to a bridge institution, a transfer to an asset management entity or write down or conversion of eligible liabilities ('bail-in tool')), make a measure for the write-down or conversion of capital instruments in accordance with the principles and procedures specified in Sections 59 to 74 of the Crisis Resolution Act. The capital instruments subject to these provisions are Common Equity Tier 1 instruments, Additional Tier 1 instruments and Tier 2 instruments as defined in the CRR. Accordingly, we confirm that the Transactions under the Master Agreement would not be directly affected by these provisions.

Crisis Management Measures

The crisis management measures under the Crisis Resolution Act comprise crisis resolution measures (or tools or actions) and the appointment of a special manager for crisis resolution.

The general conditions to the exercise of crisis management measures (including crisis resolution measures or actions) set out in the Crisis Resolution Act broadly require that the Czech Bank is failing or is likely to fail[58] and it is beyond the reach of a less drastic remedial action to prevent such failing than the application of crisis resolution measures. Such measure or action must also be necessary having regard to the public interest in the advancement of the resolution objectives and one or more of the

[56] Such specific measures broadly correspond to those set out in Article 27 of the BRRD as implemented in the Crisis Resolution Act.

[57] The temporary administrator is appointed by the Czech National Bank in order to facilitate the functions of a Czech Bank's senior management and executive directors. The temporary administration may last for up to 12 months, unless extended by the Czech National Bank.

[58] Under the Crisis Resolution Act, an affected entity is deemed to be failing, for example, if: (i) it meets conditions for withdrawal of its licence to operate due to a loss that causes or may cause a significant decrease in the amount of its capital, (ii) its liabilities exceed the value of its assets or (iii) it is unable to pay its debts as they fall due.

resolution objectives would not be met to the same extent by the winding up or insolvency proceedings in respect of the Czech Bank.[59]

In case of a special management for crisis resolution, either the CNB nominates one or more of its employees directly or appoints special a manager (or administrator) replacing and automatically fully suspending the authority of the Czech Bank's governing bodies (senior management and executive board members) and supreme body (general or shareholders' meeting).

Although the Crisis Resolution Act does not expressly state that the appointment of a special manager does not affect the performance of close-out netting or enforceability of financial collateral arrangements, we are of the view that it would not have an adverse effect on the enforceability of the relevant termination and close-out netting provisions of the Master Agreement as long as they are validly entered into (even if entered into on or after the commencement of special management for crisis resolution). This is because all restrictions on the failing debtor (i.e. the Czech Bank) and the focus of the law in question is on ensuring that the failing debtor and its bodies are not able to act in a way that would be detrimental to the bank's customers or the bank itself. This is particularly confirmed by the fact that the Crisis Resolution Act does not contain any provisions allowing the CNB or the appointed special manager to terminate or not follow contracts of the affected Czech Bank concluded before the commencement of special management for crisis resolution.

Crisis Resolution Measures

It is not the purpose of this memorandum to describe the scope of all crisis resolution measures and tools available under the Crisis Resolution Act. We consider here whether the application of any of the resolution powers set out in the Crisis Resolution Act in relation to the Czech Bank could affect the enforceability of the relevant termination and close-out netting provisions of the Master Agreement as a matter of Czech law against the Czech Bank and consequently our conclusions in this memorandum.

The Crisis Resolution Act provides for the following crisis resolution measures and tools:

- a transfer to a private sector purchaser of all or part of the business of the Czech Bank (a **transfer of business measure**);
- a transfer of all or part of the business of the Czech Bank to a bridge institution that is wholly or partially owned (directly or indirectly) by and controlled by the state of the Czech Republic (a **transfer to a bridge institution measure**);
- a transfer of all or part of the business of the Czech Bank to an asset management entity owned (directly or indirectly) by and controlled by the state of the Czech Republic (a **transfer to an asset management entity measure**)[60];
- a write down of certain claims of unsecured creditors of the relevant entity and/or conversion of certain unsecured debt claims (eligible liabilities) to equity, (the **bail-in tool**), which equity could also be subject to any future write-down; and
- a temporary stabilisation tool comprising a transfer to temporary public ownership (**nationalisation**) of all or part of the Czech Bank.

Please note that certain 'reverse' and 'onward' transfers are also possible where one of the transfer measures has been exercised.

The CNB has certain wide-ranging powers pursuant to Section 164 of the Crisis Resolution Act including, in certain circumstances, powers to unilaterally cancel a contract or modify contractual

[59] Under Section 80 of the Crisis Resolution Act, the exercise of a crisis resolution measure is deemed to be in the public interest if it is necessary and adequate in the advancement of one or more crisis resolution objectives which would not be met to the same extent by the winding up or insolvency proceedings in respect of the relevant affected entity.
[60] This measure can only be used in conjunction with one of the other crisis resolution measures or tools.

arrangements or transfer all rights and obligations under a contract. To this end, Sections 171 and 173 of the Crisis Resolution Act contain specific safeguards in respect of the "protected rights and liabilities". Their primary effect is that the exercise of crisis resolution powers by the CNB pursuant to Section 164(d) by virtue of cancellation or modification of contractual arrangements or transfer of all rights and obligations under a contract cannot result in the "protected rights and liabilities" having been changed or become extinguished. Also, in relation to a secured claim, the CNB must not take a crisis resolution action in the form of cancellation or modification of contractual arrangements or transfer of all rights and obligations under a contract or certain other crisis resolution actions under Section 164 if the result of that action were the extinguishment of the secured claim.

On the basis of the above, we do not envisage that the exercise by the CNB of ancillary resolution powers pursuant to Section 164 of the Crisis Resolution Act could affect the enforceability of the relevant termination and close-out netting provisions of the Master Agreement as a matter of Czech law against the Czech Bank and consequently our conclusions in this memorandum.

Exercise of share transfers and property transfers

The share transfers can be used by the CNB (or, in certain circumstances, the Ministry of Finance of the Czech Republic) when making any of the transfer of business, the transfer to a bridge institution, the transfer to an asset management entity or the transfer to temporary public ownership (nationalisation) measures.

We confirm that the exercise of the share transfers by the CNB (or the Ministry of Finance of the Czech Republic) in respect of a Czech Bank that is a party to the Master Agreement would not, as a matter of Czech law, affect the enforceability of the relevant termination and close-out netting provisions of the Master Agreement against a Czech Bank, and therefore it would have no impact on our conclusions in this memorandum.

The exercise of the property transfers may in turn provide for the transfer of all property, rights and liabilities of a Czech Bank or for the transfer of some, but not all, of the property, rights or liabilities of a Czech Bank. In the latter case, the transfer would be a "partial property transfer"[61].

The transfer of all of the property, rights and liabilities of a Czech Bank to a private sector purchaser, a bridge institution or asset management entity would necessarily include any Master Agreement entered into by the relevant entity with another market participant, including all Transactions under that Master Agreement. From the point of view of the other market participant, the identity of its contracting party would change, however the enforceability of the relevant termination and close-out netting provisions of the Master Agreement against a Czech Bank and in respect of Transactions would be unaffected.

In relation to a partial property transfer, which again could be used by the CNB in applying any of the transfer of business, the transfer to a bridge institution or the transfer to an asset management entity measures, the concern is that the CNB could use such power to "cherry-pick" Transactions (or parts of such Transactions) covered by the Master Agreement or otherwise disrupt the mutuality of rights and obligations under that arrangement.

Sections 171(1) and 173(2)(c) and (d) of the Crisis Resolution Act seek to protect from any adverse effects of a partial property transfer set-off arrangements under which two or more mutual claims of an obligor and a counterparty may be set off against each other and a set-off of mutual claims based on which there will occur the settlement or clearing of claims resulting in a single claim of one party and the corresponding liability of the other party to pay the resulting amount, including close-out netting.

[61] Note that Section 170 of the Crisis Resolution Act protects any transfers of property, rights and liabilities pursuant to the Crisis Resolution Act from any adverse effect of rules in respect on invalidity or ineffectiveness of legal acts due to preferential treatment of some creditors under laws governing liquidation and insolvency.

Since the safeguard set out in Section 171(1) of the Crisis Resolution Act does not cover a transfer or passage of property, rights and liabilities under a secured claim or debt (as they are referred to in Section 173(2)(a)), Section 171(3) contains a separate safeguard in respect of secured claims or debts. The restriction on partial property transfers of secured claims requires that the CNB must not (a) decide on the transfer or passage of a security without the simultaneous passage of the secured claim or debt and the benefit of the security, (b) decide on the transfer or passage of a secured claim or debt without the simultaneous passage of the benefit of the security, and (c) transfer the benefit of the security without the simultaneous transfer of the subject-matter of the secured claim or debt. It is clear that, in relation to a partial property transfer within the scope of the applicable rules, the secured property, the security interest and the secured liabilities move together or not at all.

Similarly, in relation to unsecured liabilities, despite the somewhat unfortunate, and in certain technical respects deficient, wording of Section 173(2)(d) that refers to "set-off of mutual claims on the basis of which mutual claims are settled or netted so that the result is only one claim of one contractual party and a corresponding obligation of the other party to pay the resulting amount, including close-out netting", there cannot be any doubt that the scope of the protected rights and liabilities as set out in the Crisis Resolution Act purports to cover any rights and liabilities arising under a "set-off" arrangement" or a "netting arrangement". In our view, a Master Agreement would be such a "set-off" arrangement" or a "netting arrangement" as referred to in Section 173(2)(c) and (d), and all rights and obligations under the Master Agreement, including in relation to Transactions, between the Czech Bank and the other party would be "protected rights and liabilities" within the scope of Sections 171 and 173 of the Crisis Resolution Act if they are subject to set-off or netting under the Master Agreement and as such comply with the requirement that they are claims that are capable of contractual set-off[62].

Therefore, on the basis of Sections 171 and 173 of the Crisis Resolution Act and subject to the above analysis, we conclude that the exercise by the CNB of a partial property transfer in relation to a Czech Bank would not negatively affect the enforceability of the relevant termination and close-out netting provisions of the Master Agreement as a matter of Czech law against a Czech Bank and consequently our conclusions in this memorandum.

We further believe that the inclusion under a Master Agreement of any rights or obligations that are not derivatives (as defined in the Crisis Resolution Act and EMIR) and are not protected rights and obligations within the scope of Sections 171 and 173 of the Crisis Resolution Act would not affect the enforceability of the relevant termination and close-out netting provisions of the Master Agreement in relation to any Transactions. In other words, the relevant provisions of the Crisis Resolution Act would protect a netting arrangement, such as an agreement in the form of the Master Agreement, in relation to all protected rights and liabilities within its scope, notwithstanding the inclusion within the scope of the netting arrangement of one or more rights or liabilities that are not protected.

The bail-in tool

The bail-in tool represents another crisis resolution measure under the Crisis Resolution Act[63]. It is exercised by the CNB through a write down of certain claims of unsecured creditors of a Czech Bank and/or conversion of certain unsecured debt claims (eligible liabilities) to equity, which equity (i.e. capital instruments[64]) could also be subject to any future write-down. The Crisis Resolution Act stipulates certain specific conditions to the exercise of the bail-in tool, which the CNB will be obliged

[62] While a German Master Agreement with one Transaction may be capable of satisfying these definitions, rights and liabilities are only protected for the purposes of these safeguards if a party is entitled to set off or net them under the relevant arrangement.

[63] In line with the BRRD, the "bail-in" is a process of internal recapitalisation that is triggered when a Czech Bank reaches the point of non-viability. In this process, losses are imposed on some of the Czech Bank's direct stakeholders by either a write-down of their claims or by their conversion to equity. The purpose of the bail-in tool is to recapitalise all or a part of the Czech Bank or its successor entity so that it is put on a stable footing and can be further restructured as necessary. This should ensure that there is no immediate need for a split of the Czech Bank's business or use of public funds to resolve the Czech Bank.

[64] These capital instruments may take the form of Common Equity Tier 1 instruments, Additional Tier 1 instruments and Tier 2 instruments as such are referred to in the Crisis Resolution Act and defined in the CRR.

to observe when making this crisis resolution measure[65]. We discuss some of these conditions (including, in particular, which of the Czech Bank's liabilities constitute eligible liabilities), to the extent that they are relevant to our conclusions in this memorandum, further below.

The effect of the exercise of the bail-in tool is broadly that (i) the nominal value or the amount of principal of an eligible liability owed by a Czech Bank is permanently decreased as a result of the partial write-down or partial conversion to equity; or (ii) an eligible liability owed by a Czech Bank is cancelled altogether as a result of the full write-down or cancelled and modified as a result of full conversion to equity.

The scope of eligible liabilities (which can be subject to the bail-in tool) includes all liabilities of the Czech Bank or another relevant entity, unless such liabilities are explicitly excluded[66].

Although the rules explicitly exclude from the scope of eligible liabilities, among other things, any secured debt up to the value of the security provided, the concern for the close-out netting provisions under the Master Agreement is primarily that the bail-in tool could apply so as to reduce or eliminate the amount owed by the Czech Bank or under a Transaction with the effect that the ability of the other party to net amounts due in respect of those liabilities against liabilities owed by such party would be commensurately reduced or eliminated.

First of all, the bail-in tool may not be exercised so as to affect any excluded liability which includes any liability so far as it is secured (or any secured debt up to the value of the security provided). For the purposes of the Crisis Resolution Act, secured debt is defined as any debt if a security has been provided to its creditor or for its creditor's benefit to secure its repayment by the debtor. We read these provisions so that secured for this purpose means secured against property or rights, or otherwise covered by collateral arrangements. However, an unsecured liability outstanding under a Transaction entered into under the Master Agreement may constitute eligible liability and as such may be subject to the bail-in tool.

The most important rule for the present purposes is Section 142 of the Crisis Resolution Act. It provides that the CNB, when applying the bail-in tool by virtue of a write-down or conversion to equity of eligible liabilities arising from a "derivative", applies the bail-in tool so that it terminates such a "derivative" and performs a set-off of mutual claims of contractual parties in accordance with a "close-out netting arrangement" or in a similar manner so that the relevant eligible liabilities result in one claim of one contractual party and a corresponding debt of the other contractual party to pay the resulting (close-out) amount. In the Crisis Resolution Act a "derivative" means a derivative as defined in Article 2(5) of EMIR.

Based on the above, we can conclude that, to the extent the Transactions under the Master Agreement are constituted by "derivatives" as defined in the Crisis Resolution Act, the operation of the close-out netting provisions of the Master Agreement would be effectively protected against any adverse effects of the bail-in tool[67]. Please note that these protections would apply only to unsecured liabilities in so far as those liabilities relate to Transactions that are derivatives.

On top of that, as articulated above, where the Master Agreement is collateralised by the Czech Bank, the bail-in tool should not apply to Transactions under the Master Agreement notwithstanding the existence of one or more Transactions that do not fall within the definition of a derivative. This is because, as also mentioned above, a liability may not be subject to bail-in so far as it is secured and, in light of the single agreement concept and provided that the collateralisation is performed on a net basis,

[65] See, in particular, Sections 120 to 148 of the Crisis Resolution Act.
[66] The list of excluded liabilities is set out in Section 122 (and to some extent Section 123) of the Crisis Resolution Act.
[67] This conclusion is further supported by certain other provisions of the Crisis Resolution Act such as Section 136 regarding valuation of an eligible liability under a derivative or Sections 129 and 135 setting out conditions for inclusion of an eligible liability under a derivative in the minimum requirement for own funds and eligible liabilities.

we would argue that all liabilities under the Master Agreement would need to be converted into a net debt in accordance with the close-out netting provisions before any net debt that exceeds the value of the collateral could be considered for a bail-in.

Subject to the above discussion, we have concluded that the Crisis Resolution Act preserves the envisaged effects of the close-out netting provisions under the Master Agreement, although any net sum owed by the Czech Bank as a result of the operation of such provisions would itself be at risk of being reduced or eliminated by the making of the bail-in tool.

Overrides and stays

Sections 168 and 169 of the Crisis Resolution Act, which fully implement Article 68 of the BRRD, provide that the following are to be disregarded in determining whether a termination event or event of default (including an insolvency or similar event) has occurred and whether a corresponding provision (which includes any provision of an agreement that has the effect that, if a specified event occurs or situation arises, the agreement or any rights or duties thereunder are terminated or a sum becomes payable or other right, including the right to acquire or enforce collateral, accrues) applies in respect of the Czech Bank or a member of the same group as that Czech Bank in the case of a cross-default provision (as defined in Section 168(2) of the Crisis Resolution Act):

– a crisis prevention measure or crisis management measure taken in relation to the Czech Bank or a member of the same group as that Czech Bank in the case of a cross-default provision; and

– the occurrence of any event directly linked to the application of such a measure.

The above overrides apply where a contract or other agreement is entered into by a Czech Bank but only if the substantive obligations provided for in the contract or agreement, including payment obligations and provision of collateral, continue to be performed. These restrictions on termination rights could also be engaged in certain cross-border scenarios.

In the present context, the effect of these provisions of the Crisis Resolution Act is that the right to terminate and close out Transactions in accordance with the close-out netting provisions would be ineffective in certain circumstances including where such rights arise as a result of the exercise of crisis prevention or crisis resolution measures (or events directly linked to the application of such measures) in relation to the Czech Bank. The same effect arises in respect of enforcement of security or collateral. In any event, the parties to the Master Agreement should not seek to interpret Section 7(2) (*Termination*) as allowing them to terminate the Master Agreement or any related Transaction on the sole basis that the CNB made a crisis prevention measure or a crisis management measure pursuant to the Crisis Resolution Act in respect of the Czech Bank, if the substantive obligations provided for in the contract or agreement, including payment obligations and provision of collateral, continue to be performed.

However, if such termination or other above described right arises based on the existence or occurrence of other events or circumstances set out in Section 7 of the Master Agreement, they should not be affected. Therefore we believe that these provisions of the Crisis Resolution Act have no impact on the conclusions in this memorandum.

Under Section 83 of the Crisis Resolution Act, the CNB may suspend, subject to certain very specific caveats, obligations to make a payment or delivery under a contract where one of the parties to the contract is a Czech Bank. Suspension of these obligations, however, is not applicable to debts of a Czech Bank owed to, *inter alia*, the CNB or other central banks. Similarly Section 84 of the Crisis Resolution Act, that is relevant for any transfers of financial collateral, allows the CNB to temporarily restrict the enforcement of security interest regardless its form. Again, the CNB and other central banks are exempted from this restriction.

In accordance with Section 83(2) of the Crisis Resolution Act, any payments or deliveries that become due under the Master Agreement during the stay period, while not being made by either party, will instead become due and payable at the end of such period (subject to the terms of the Master Agreement) and, if an Early Termination Date is designated under the Master Agreement and such amounts remain outstanding as at such Early Termination Date, the affected party will be in default as of the moment the suspension ends.

The CNB may suspend the termination rights (which includes a right to withdrawal, settlement, set-off or netting of obligations, or a right which will or may result in the acceleration of an obligation or close-out netting, or any similar right that will or may result in the creation, modification, suspension or termination of other rights or obligations of parties to the contract) of any party to a contract with a Czech Bank assuming that all the substantive obligations under the contract, including obligations to make payments or deliveries or provide collateral, continue to be performed. Similarly, the CNB can also suspend the termination rights of any party to a contract with the Czech Bank's subsidiary, where such subsidiary's obligations are secured by the Czech Bank and the relevant termination rights would be based solely on insolvency or financial conditions of the Czech Bank in question. Neither of these suspensions is applicable to termination rights of the CNB and another central bank that is a counterparty of the affected Czech Bank. On top of the powers mentioned above, the Czech National Bank may impose an obligation to keep detailed records about financial contracts to which a Czech bank is a party.

All of the above described suspensions commence as of the publication of the decision on the CNB's website and must end no later than at midnight at the end of the first business day following the day of the publication. The reason for these suspensions is to give the CNB time to take measures without any interference of effects from the exercise of various termination or other rights of parties to a contract.

Noting that the restrictions under Sections 83 to 85 of the Crisis Resolution Act will not prejudice a party in seeking to enforce its rights against the Czech Bank under the Master Agreement upon expiration of the stay, we believe that such powers have no impact on our conclusions herein regarding the enforceability of the close-out netting provisions.

ANNEX 3

TRANSACTIONS ENTERED INTO UNDER THE UNDERLYING AGREEMENTS

(A) Energy Transactions

Commodity Transaction. A transaction in which one party agrees to buy from or sell to the other party a specified quantity of commodity (e.g., base metals, gas, oil, electricity, emission rights or freight) in exchange for payment of a specified price, which becomes due on the same day, two days later or on another agreed future date. The transaction may be settled by physical delivery of the quantity of commodity in exchange for the specified price or may be cash settled based on the difference between the market price of the commodities on the settlement date and the specified price.

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

Commodity Swap. A transaction in which one party pays periodic amounts of a given currency based on a fixed price and the other party pays periodic amounts of the same currency based on the price of a commodity, such as base metals, gas, oil, electricity, emission rights or freight, or a futures contract on a commodity (e.g., Brent Crude Futures on the ICE Futures Europe Exchange); all calculations are based on a notional quantity of the commodity.

(B) Energy Related Transactions

Emissions Allowance Transaction. A transaction, structured in the form of a swap, cap, collar, floor or some combination thereof, in which one party agrees to buy from or sell to the other party a specified quantity of a right to emit one tonne of carbon dioxide (CO2) or other emissions product such as Nitrogen Oxide ("NOx") or sulphur dioxide ("SOx") during a specified period valid only for the purposes of meeting the requirements of applicable law and which is capable of being transferred from the seller to the buyer under a trading system established pursuant to applicable law.

Renewable Energy Certificates ("RECs") Transaction. A transaction in which one party agrees to buy from or sell to the other party one or more fungible renewable energy certificates, each evidencing the production of 1MWhr of renewable energy and which is capable of being issued, evidenced, traded and redeemed in accordance with international standard practices such as the European Energy Certificate System.

Weather Transaction. A transaction, structured in the form of a swap, cap, collar, floor, or some combination thereof, between two parties in which the underlying value of the transaction is based on a rate or index pertaining to weather conditions, which may include measurements of heating, cooling, precipitation and wind.

Weather Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to receive a payment determined by reference to the amount by which a particular release of statistical data on weather conditions, which may include heating, cooling, precipitation and wind either exceeds (in the case of a call option) or is less than (in the case of a put option) a specified strike level.

(C) Other Transactions

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

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

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

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

Swap Option. A transaction in which one party grants to the other party the right (in consideration for a premium payment), but not the obligation, to enter into a swap with certain specified terms. In some cases the swap option may be settled with a cash payment equal to the market value of the underlying swap at the time of the exercise.

Total Return Swap. A transaction in which one party pays either a single amount or periodic amounts based on the total return on one or more loans, debt securities or other financial instruments (each a "Reference Obligation") issued, guaranteed or otherwise entered into by a third party (the "Reference Entity"), calculated by reference to interest, dividend and fee payments and any appreciation in the market value of each Reference Obligation, and the other party pays either a single amount or periodic amounts determined by reference to a specified notional amount and any depreciation in the market value of each Reference Obligation.

A total return swap may (but need not) provide for acceleration of its termination date upon the occurrence of one or more specified events with respect to a Reference Entity or a Reference Obligation with a termination payment made by one party to the other calculated by reference to the value of the Reference Obligation.

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

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

For the purposes of Bullion Trades, Bullion Options and Bullion Swaps, "Bullion" means gold, silver, platinum or palladium and "Ounce" means, in the case of gold, a fine troy ounce, and in the case of silver, platinum and palladium, a troy ounce.

Equity Index Transaction. A transaction in which one party agrees to buy from or sell to the other party a specified quantity of shares of an issuer or a basket of shares of several issuers for payment of a specified price for settlement either on a "spot" or two-day basis or a specified future date. The transaction may be settled by physical delivery of the agreed quantity of shares in exchange for the specified price or may be cash settled based on the difference between the index value on the settlement date and the specified index value.

<u>Equity Transaction</u>. A transaction in which one party agrees to buy from or sell to the other party a specified quantity of shares included in an equity index for payment of a specified price for settlement either on a "spot" or two-day basis or a specified future date. The transaction may be settled by physical delivery of the agreed quantity of shares in exchange for the specified price or may be cash settled based on the difference between the market price of the shares on the settlement date and the specified price.

<u>Equity Index Option</u>. A transaction in which one party grants to the other party (in consideration for a premium payment) the right to receive a payment equal to the amount by which an equity index either exceeds (in the case of a call) or is less than (in the case of a put) a specified strike price.

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

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

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

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

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

<u>Credit Protection Transaction</u>. A transaction in which one party pays either a single fixed amount or periodic fixed amounts or floating amounts determined by reference to a specified notional amount, and the other party (the credit protection seller) pays either a fixed amount or an amount determined by reference to the value of one or more loans, debt securities or other financial instruments (each a "Reference Obligation") issued, guaranteed or otherwise entered into by a third party (the "Reference Entity") upon the occurrence of one or more specified credit events with respect to the Reference Entity (e.g., bankruptcy or payment default). The amount payable by the credit protection seller is typically determined based upon the market value of one or more debt securities or other debt instruments issued, guaranteed or otherwise entered into by the Reference Entity. Credit protection transactions may also be physically settled by payment of a specified fixed amount by one party against delivery of specified Reference Obligations by the other party. A credit protection transaction may also refer to a "basket" of two or more Reference Entities.

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

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

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

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

Economic Statistic Transaction. A transaction, structured in the form of a swap, cap, collar, floor, or some combination thereof, between two parties in which the underlying value of the transaction is based on a rate or index pertaining to statistical data on macroeconomic conditions, which may include economic growth, retail sales, inflation, consumer prices, consumer sentiment, unemployment and housing.

Economic Statistic Option. A transaction in which one party grants to the other party (in consideration for a premium payment) the right, but not the obligation, to receive a payment determined by reference to the amount by which a particular release of statistical data on macroeconomic conditions, which may include economic growth, retail sales, inflation, consumer prices, consumer sentiment, unemployment and housing, either exceeds (in the case of a call option) or is less than (in the case of a put option) a specified strike level.

Foreign Exchange Transaction. A transaction providing for the purchase of one currency with another currency providing for settlement either on a "spot" or two-day basis or a specified future date. The transaction may be settled by physical delivery of the agreed currency or unit of account in exchange for payment of the agreed other currency or unit of account, or may be cash settled based on the difference between the market price of the agreed other currency or unit of account on the settlement date and the specified price.

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

Interest Rate Swap. A transaction in which one party pays periodic amounts of a given currency based on a specified fixed rate and the other party pays periodic amounts of the same currency based on a specified floating rate that is reset periodically, such as the London inter-bank offered rate; all calculations are based on a notional amount of the given currency.

Repurchase Transaction. A transaction in which one party agrees to sell securities to the other party and such party has the right to repurchase those securities from such other party at a future date.

Securities Lending Transaction. A transaction in which one party transfers securities to a party acting as the borrower in exchange for a payment or a series of payments from the borrower and the borrower's obligation to replace the securities at a defined date with identical securities.

ANNEX 4

ARTICLES 7 AND 8 OF THE MIFID II REGULATION[68]

Article 7

Other derivative financial instruments

(Article 4(1)(2) of Directive 2014/65/EU)

1. For the purposes of Section C(7) of Annex I to Directive 2014/65/EU, a contract which is not a spot contract in accordance with paragraph 2 and which is not for commercial purposes as laid down in paragraph 4 shall be considered as having the characteristics of other derivative financial instruments where it satisfies the following conditions:

(a) it meets one of the following criteria:

(i) it is traded on a third country trading venue that performs a similar function to a regulated market, an MTF or an OTF;

(ii) it is expressly stated to be traded on, or is subject to the rules of, a regulated market, an MTF, an OTF or such a third country trading venue;

(iii) it is equivalent to a contract traded on a regulated market, MTF, an OTF or such a third country trading venue, with regards to the price, the lot, the delivery date and other contractual terms;

(b) it is standardised so that the price, the lot, the delivery date and other terms are determined principally by reference to regularly published prices, standard lots or standard delivery dates.

2. A spot contract for the purposes of paragraph 1 shall be 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) 2 trading days;

(b) the period generally accepted in the market for that commodity, asset or right as the standard delivery period.

A contract shall not be considered a spot contract where, irrespective of its explicit terms, there is an understanding between the parties to the contract that delivery of the underlying is to be postponed and not to be performed within the period referred to in paragraph 2.

3. For the purposes of Section C(10) of Annex I to Directive 2004/39/EC of the European Parliament and of the Council[69], a derivative contract relating to an underlying referred to in that Section or in Article 8 of this Regulation shall be considered to have the characteristics of other derivative financial instruments where one of the following conditions is satisfied:

(a) it is settled in cash or may be settled in cash at the option of one or more of the parties, otherwise than by reason of a default or other termination event;

68 Note that Section C(7) of Annex I MiFID II was implemented into Section 3(1)(i) of the CMA and Section C(10) of Annex I to MiFID II was implemented into Sections 3(1)(j) and 3(1)(k) of the CMA.

69 Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (OJ L 145, 30.4.2004, p. 1).

(b) it is traded on a regulated market, an MTF, an OTF, or a third country trading venue that performs a similar function to a regulated market, MTF or an OTF;

(c) the conditions laid down in paragraph 1 are satisfied in relation to that contract.

4. A contract shall be considered to be for commercial purposes for the purposes of Section C(7) of Annex I to Directive 2014/65/EU, and as not having the characteristics of other derivative financial instruments for the purposes of Sections C(7) and (10) of that Annex, where the following conditions are both met:

(a) it is entered into with or by an operator or administrator of an energy transmission grid, energy balancing mechanism or pipeline network,

(b) it is necessary to keep in balance the supplies and uses of energy at a given time, including the case when the reserve capacity contracted by an electricity transmission system operator as defined in Article 2(4) of Directive 2009/72/EC is being transferred from one prequalified balancing service provider to another prequalified balancing service provider with the consent of the relevant transmission system operator.

Article 8

Derivatives under Section C(10) of Annex I to Directive 2014/65/EU

(Article 4(1)(2) of Directive 2014/65/EU)

In addition to derivative contracts expressly referred to in Section C(10) of Annex I to Directive 2014/65/EU, a derivative contract shall be subject to the provisions in that Section where it meets the criteria set out in that Section and in Article 7(3) of this Regulation and it relates to any of the following:

(a) telecommunications bandwidth;

(b) commodity storage capacity;

(c) transmission or transportation capacity relating to commodities, whether cable, pipeline or other means with the exception of transmission rights related to electricity transmission cross zonal capacities when they are, on the primary market, entered into with or by a transmission system operator or any persons acting as service providers on their behalf and in order to allocate the transmission capacity;

(d) an allowance, credit, permit, right or similar asset which is directly linked to the supply, distribution or consumption of energy derived from renewable resources, except where the contract is already within the scope of Section C of Annex I to Directive 2014/65/EU;

(e) a geological, environmental or other physical variable, except if the contract is relating to any units recognised for compliance with the requirements of Directive 2003/87/EC of the European Parliament and of the Council[70];

(f) any other asset or right of a fungible nature, other than a right to receive a service, that is capable of being transferred;

[70] Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC (OJ L 275, 25.10.2003, p. 32).

(g) an index or measure related to the price or value of, or volume of transactions in any asset, right, service or obligation;

(h) an index or measure based on actuarial statistics.