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VALIDITY AND ENFORCEABILITY UNDER AUSTRALIAN LAW OF COLLATERAL ARRANGEMENTS UNDER THE ISDA CREDIT SUPPORT DOCUMENTS

CONTENTS

PART A. BACKGROUND **4**

1 Introduction **4**

2 Scope **6**

3 Structure of our memorandum **7**

4 Overview of collateral laws in Australia **8**

5 Summary of relevant requirements under the PPSA **10**

6 Summary of the relevant requirements for the protection of enforcement of security under the *Netting Act* **16**

PART B: SECURITY INTEREST APPROACH PURSUANT TO THE SECURITY DOCUMENTS **25**

1 Law governing contractual and validity aspects of security **25**

2 Law governing perfection of security interest **27**

3 Recognition of security interest **29**

4 Effect of fluctuating exposures or Collateral **30**

5 Steps for attachment and perfection **32**

6	Other requirements for valid security interests	41
7	Action required to maintain security interest	41
8	Requirements where Australian Law is not the governing law for validity and perfection	41
9	Secured party duties	43
10	Dealings with Collateral	43
11	Substitution of Collateral	44
12	Formalities in exercising enforcement rights	46
13	Formalities where Australian Law is not the law governing the validity and perfection	48
14	Special limitations on enforcement	48
15	Secured Party in default	49
16	Competing claims	50
17	Stay on rights	50
18	Clawback	52
19	Governing law of Security Document	52
20	Other issues	54
21	Other circumstances that might affect enforcement	54
22	Collateral held with a Custodian under an IM Security Document	56
23	Collateral held with Euroclear or Clearstream	56
24	IM NY Annex Japanese Amendments	58
25	VM NY Annex IA Amendments	58
26	IM Deed Japanese Amendments	58
PART C: TITLE TRANSFER APPROACH PURSUANT TO THE TRANSFER ANNEX		60
1	Nature of transfers	60
2	Action needed to perfect transfers	62
3	Substitutions	63
4	Enforceability of CSA being a "Transaction"	63
5	Effect of insolvency of the Transferor	64
6	Clawback	64
7	Agreements on governing law	65
8	Validity of outright transfer concept	65
9	Additional questions in relation to the VM Transfer Annex	66
10	VM Transfer Annex IA Amendments	66
PART D: CLOSE-OUT AMOUNT PROTOCOL AND COLLATERAL AGREEMENT NEGATIVE INTEREST PROTOCOL		67

SCHEDULE 1 ASSUMPTIONS **68**

SCHEDULE 2 COMPETING CLAIMS **73**

SCHEDULE 3 CLAWBACK **75**

SCHEDULE 4 OTHER CIRCUMSTANCES THAT MIGHT AFFECT ENFORCEMENT WHERE THE *NETTING ACT* DOES NOT APPLY **80**

SCHEDULE 5 RE-CHARACTERISATION AS A CHARGE **83**

APPENDIX A **84**

APPENDIX B **89**

PART A. BACKGROUND

1 Introduction

This memorandum considers the validity and enforceability under Australian Law (as defined below) of collateral arrangements entered into under the following standard form collateral documents published by the International Swaps and Derivatives Association, Inc. ("**ISDA**"):

(a) the 1994 ISDA Credit Support Annex governed by New York law ("**NY Annex**"); and

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

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

(d) the 1995 ISDA Credit Support Deed governed by English law ("**1995 Deed**"); and

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

(f) the 1995 ISDA Credit Support Annex governed by English law ("**1995 Transfer Annex**"); and

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

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

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

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

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

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

(m) the ISDA Clearstream 2016 Collateral Transfer Agreement (Multi-Regime) ("**Clearstream Multi-Regime CTA**") and the Clearstream Japanese Amendments.

As requested, we have addressed the issues raised by ISDA in its letter to us provided on 29 October 2016 ("**Instruction Letter**") on the basis of the assumptions that we have been asked to make. We have also set out in this memorandum certain other assumptions that we consider necessary in order for us to answer the questions posed.

Defined terms in the Instruction Letter and the Credit Support Documents have the same meaning in this memorandum.

In this memorandum, we refer to our memorandum to you regarding the enforceability under Australian law of close-out netting dated 28 February 2017 ("**Netting Opinion**").

Also, for the purposes of this memorandum:

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

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

(iii) "**Security Documents**" means the Annexes and the Deeds;

(iv) "**IM Security Documents**" means the IM NY Annex and the IM Deed;

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

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

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

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

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

In this memorandum:

(A) "**Security Collateral Provider**" refers, in the case of each Security Document, to the Pledgor (under an Annex), the Chargor (under a Deed) or the Security-provider (under the Euroclear Security Agreement or the Clearstream Security Agreement), as the context requires; and

(B) "**Collateral Provider**" refers to the Security Collateral Provider (under a Security Document) or the Transferor (under a Transfer Annex), as the context requires;

(C) "**Collateral Taker**" refers to the Secured Party (under the IM Documents), the Security-taker (under the Euroclear Security Agreement or the Clearstream Security Agreement) or the Transferee (under a Transfer Annex), as the context requires;

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

Where the context requires, references in this memorandum, our Netting Opinion or our Collateral Taker Opinion to a term which is defined in a Credit Support Document or other document listed in paragraphs 1(a) to 1(m) above covered by this memorandum or the other opinion (as applicable) should be taken to refer to the equivalent defined term used in another relevant Credit Support Document or document listed in paragraphs 1(a) to 1(m) above.

2 Scope

This memorandum is given on the laws of the Commonwealth of Australia, New South Wales, Victoria, Queensland, Western Australia and the Australian Capital Territory (each an "**Australian Jurisdiction**"). The opinions expressed in this memorandum are limited to those laws. We express no opinion about the laws of any jurisdiction other than the Australian Jurisdictions, commercial, accounting, financial, prudential or factual matters. However, the *Corporations Act 2001* of Australia ("***Corporations Act***") is uniform throughout Australia and the other statutes mentioned in this memorandum are Commonwealth statutes (other than the statutes relating to stamp duty). In this memorandum the courts of the Australian Jurisdictions are sometimes referred to as the "**Australian Courts**" and the laws in force in the Australian Jurisdictions are sometimes referred to as "**Australian Law**".

This memorandum is subject to the following:

(a) The advice in this memorandum is only in relation to Australian Law as it stands at the date of this memorandum, and we have assumed that no law of a jurisdiction other than the Australian Jurisdictions adversely affects the conclusions in this memorandum.

(b) This memorandum incorporates all the assumptions contained in the Instruction Letter (which for convenience are repeated in Schedule 1 to this memorandum).

(c) The entity type in respect of which this memorandum is given is "**Australian Company**" which means a company which is registered as a company under the *Corporations Act*.

The term Australian Company includes all Australian authorised deposit-taking institutions ("**ADIs**"), and most life insurance companies, superannuation trustees and trustees of unit trusts (including managed investment schemes)[1] and other Australian business entities likely to be trading in derivatives which are companies which have been registered as a company under the *Corporations Act*. However, this needs to be confirmed in each case.

[1] Under Australian Law, superannuation funds, managed investment schemes and other trusts are not legal entities. The relevant entity is the superannuation trustee acting in its capacity as trustee of the superannuation fund, the responsible entity of the scheme or the trustee of the other trust, respectively.

The term Australian Company *does not* include foreign companies or entities, companies which do not have their centre of main interests in Australia for the purposes of the UNCITRAL Model Law on Cross-Border Insolvency ("**Model Law**"), private health insurers, the Crown and statutory corporations organised under any Australian law.

We set out in Appendix B (September 2009) further information on whether entities meeting particular descriptions would, or could, be Australian Companies.

(d) You have asked that we consider the list of transactions that can be documented under a Master Agreement in Appendix A (August 2015) ("**Transactions**"). We confirm that this memorandum applies to those Transactions.

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

(i) The Location of the Collateral Provider is in Australia and the Location of the Collateral is outside Australia.

(ii) The Location of the Collateral Provider is in Australia and the Location of the Collateral is in Australia.

(iii) The Location of the Collateral Provider is outside Australia and the Location of the Collateral is in Australia.

For these purposes "Location" is determined by reference to the rules in the PPSA (defined in paragraph A.4 below), which is described in paragraph A.5.4 of this memorandum.

We consider the enforceability under Australian Law of each of the Credit Support Documents, when entered into in connection with either the 1992 ISDA Master Agreement or the 2002 ISDA Master Agreement (each referred to as a "**Master Agreement**"), against an Australian Company. Where the location of the Collateral or the jurisdiction in which a company is organised or its status affects our analysis, it is generally clear from the wording of our memorandum.

(f) We do not consider in this memorandum the insolvency of any entity other than an Australian Company.

(g) The advice in this memorandum assumes that any Credit Support Documents are used together with a Master Agreement. In the case of the 2002 ISDA Master Agreement, we assume that the relevant Credit Support Documents have been appropriately amended.

(h) This memorandum is given for the sole benefit of ISDA and its members and may not be relied upon by any other person unless we otherwise specifically agree with that person in writing.

3 Structure of our memorandum

This memorandum is structured as follows:

Part	Subject	Paragraphs
Part A	Overview of collateral laws in Australia	A.4
	Summary of the relevant requirements under the PPSA	A.5
	Summary of the relevant requirements under the *Netting Act*	A.6
Part B	Questions and our responses relating to the Security Documents	B.1 to B.26
Part C	Questions and our responses relating to the Transfer Annex	C.1 to C.10
Part D	Close-out Amount Protocol and Collateral Agreement Negative Interest Protocol	D.1 to D.2
Schedule 1	Assumptions and qualifications	
Schedule 2	Competing claims	
Schedule 3	Clawback	
Schedule 4	Other circumstances which might affected enforcement where the *Netting Act* does not apply	
Schedule 5	Re-characterisation as a charge	
Appendix A	Certain transactions under the ISDA Master Agreements	
Appendix B	Certain counterparty types	

4 Overview of collateral laws in Australia

For the purposes of this memorandum, there are two key pieces of legislation relevant to the validity and enforcement of collateral arrangements under the Credit Support Documents under Australian Law. These are the *Personal Property Securities Act 2009* (Cth) ("**PPSA**") and the *Payments Systems and Netting Act 1998* (Cth) ("***Netting Act***"). In this memorandum, we summarise the relevance of the PPSA and the *Netting Act* to collateral arrangements in paragraphs A.4 to A.6 and then consider the application of these laws to the specific questions raised in the Instruction Letter in Parts B and C.

The PPSA is fundamental to collateral arrangements under Australian Law, establishing a national system for the registration of security interests in personal property, together with rules for the creation, priority and enforcement of security interests in personal property.

Part 4 of the *Netting Act* protects the process under close-out netting contracts by which particular obligations of the parties terminate or may be terminated, the termination values of the obligations are calculated or may be calculated and the termination values are netted, or may be netted, so that

only a net cash amount (whether in Australian currency or some other currency) is payable. This protection is considered further in our Netting Opinion. Relevantly, this protection applies to the inclusion of the obligation to transfer equivalent collateral under a Transfer Annex in the close-out netting process under the contract, as described further in Part C of this memorandum.

In 2016, the *Netting Act* was amended to protect the enforcement of security under security-based collateral arrangements where specified safeguards are satisfied.[2] The *Netting Act* protection overrides existing laws relating to the enforceability, validity and perfection of security interests, priority frameworks and any vesting which could otherwise occur under the PPSA or the *Corporations Act* due to non-perfection or a delay in perfection.[3] These amendments were made to ensure that entities subject to Australian Law can enforce rights in margin provided by way of security in the manner contemplated by the revised margin requirements for non-centrally cleared derivatives published by the Basel Committee on Banking Supervision and the International Organization of Securities Commissions in March 2015. As a facilitative enforcement regime, the *Netting Act* protection does not limit or otherwise restrict anything which would otherwise be available or protected at law (including any rights which a secured party would otherwise have by virtue of the PPSA, the exercise of those rights and any protection which applies to those rights or the exercise of those rights).[4]

However, there are circumstances where the *Netting Act* protection of the enforcement of security will not apply. These are described in this memorandum and they include, but are not limited to, circumstances where:

(a) the Secured Party seeks to enforce the security under the Security Document against the Secured Collateral Provider prior to the time when either party is subject to *external administration* governed by Australian Law. As we assume that the Master Agreement entered into by the Security Collateral Provider and the Secured Party is governed by English or New York law,[5] the *Netting Act* protection only applies if, at the time of the enforcement, either party is subject to *external administration* governed by Australian law. As a consequence, the steps for attachment and perfection under the PPSA continue to be relevant to an enforcement of security prior to any such *external administration*; or

(b) the Security Document is entered into in connection with the 1992 ISDA Master Agreement and "First Method" is chosen. As set out in paragraph B.2.2 of our Netting Opinion, if the "First Method" is chosen under the 1992 ISDA Master Agreement, then that 1992 ISDA Master Agreement would not satisfy the definition of *close-out netting contract;*[6] or

(c) any of the conditions of the application of the *Netting Act* are not met. These include the constitutional limits on the application of the *Netting Act* as set out in paragraphs B.2.7 to

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2 Explanatory Memorandum to the *Financial System Legislation Amendment (Resilience and Collateral Protection) Bill* ("**Explanatory Memorandum**"), [1.25]. In order for the *Netting Act* protection to apply to the enforcement of security, a number of conditions need to be met, including that the Collateral must be transferred or otherwise dealt with before enforcement so as to be in the possession or under the control of the Secured Party, or another person (who is not the Security Collateral Provider) on behalf of the Secured Party. These conditions are considered further in paragraph A.6 below.

3 The *Netting Act* protection of enforcement of security applies "despite any other law (including the specified provisions)" but "subject to a specified stay provision that applies to the contract"; see also Explanatory Memorandum, [1.114].

4 Explanatory Memorandum, [1.109].

5 Please refer to the assumption set out in paragraph (a) of Schedule 1 to this memorandum.

6 We do not consider a 1992 ISDA Master Agreement in respect of which the "First Method" is chosen further in this memorandum.

B.2.9 of our Netting Opinion (as referred to in paragraph A.4(a) above), and the particular conditions for protection of the enforcement of security (discussed in more detail in paragraph A.6 below).

Accordingly, we recommend in this memorandum that the applicable steps for attachment and perfection under the PPSA are taken, even where it is expected that the conditions for the application of the *Netting Act* protection for the enforcement of security will be satisfied. The steps for attachment and perfection under the PPSA continue to be relevant to an enforcement of security where the *Netting Act* does not apply, including in any of the circumstances identified in paragraphs A.4(a) to A.4(c) above.

We have noted in each response to the questions on the Security Documents in Part B and the Transfer Annex in Part C the extent to which our answer differs where the *Netting Act* protection applies.

5 Summary of relevant requirements under the PPSA

The PPSA is fundamental to collateral arrangements under Australian Law. The system is modelled on the personal property regimes in New Zealand, Canada and the United States. Some of the aspects of the PPSA which are most relevant to this memorandum are considered below.

The PPSA established a national system for the registration of security interests in personal property, whether given by a company or a natural person, together with new rules for the creation, priority and enforcement of security interests in personal property. It has replaced certain existing Australian Commonwealth and State based regimes co-ordinated by the Australian Securities and Investments Commission ("**ASIC**") and other regulators, including the previously existing regime under the *Corporations Act* for registration of charges. It also makes registrable as security interests certain transactions which were previously not registrable at all.

The PPSA commenced operation on 15 December 2009, and had operational effect from 30 January 2012 with a two year transitional period beginning at that time. It has an effect on security interests and security agreements arising before 30 January 2012 by operation of the transitional provisions.

5.1 Personal property

The PPSA applies to security interests in personal property. Personal property means property other than land or a right, entitlement or authority that is granted under an Australian Law and other than property which is declared not to be personal property for the purposes of the PPSA.

A security interest is defined as an:

> "interest in personal property provided for by a transaction that, in substance, secures payment or performance of an obligation".

The form of the transaction, or the identity of the person who has title, is irrelevant.

There are some key elements of the general definition of security interest which are particularly relevant to the analysis in this memorandum. For there to be a security interest under this general definition:

- *(secured obligation)* there must be an obligation to be paid or performed;
- *(security)* the payment or performance of that obligation must be secured "in substance";
- *(personal property)* that security must be an interest in personal property; and
- *(transaction)* that interest must be provided for by a transaction.

Security interests for the purposes of the PPSA include traditional securities such as charges and mortgages. However, they also include transactions that, in substance, secure payment or performance of an obligation but which may not have been formerly legally classified, or even thought of commercially, as security interests (for example, transfers of title and flawed asset arrangements).

Further, certain other interests are deemed to be security interests whether or not they secure payment or performance of an obligation. These deemed security interests include the absolute transfer of an account (ie even if by way of sale as opposed to an assignment or transfer by way of security).

5.2 PPSA collateral classes

The steps for attachment and perfection of a security interest in personal property depend on the PPSA collateral class attributed to the personal property for the purposes of the PPSA.

Based on the assumptions which we have been asked to make for the purposes of this memorandum, the Eligible Credit Support should fall within the PPSA collateral classes:

Collateral	**PPSA collateral class**
Directly held bearer debt security or equity security	Negotiable instrument (in respect of a debt security only) or an investment instrument
Directly held registered debt security or equity security	Investment instrument
Directly held dematerialized debt security or equity security	Negotiable instrument (in respect of a debt security only) or an investment instrument
Indirectly held debt security or equity security held through: (a) a custodian or nominee with an Australian financial services licence ("**AFSL**") or licence under a foreign jurisdiction permitting them to maintain securities accounts, such as a Custodian as described in assumption (n) in Schedule 1; (b) a clearing system such as Austraclear Limited ("**Austraclear**"), Euroclear Bank S.A./N.V. ("**Euroclear**") or Clearstream Banking S.A.	Intermediated security

Collateral	PPSA collateral class
("**Clearstream**");[7] or (c) CHESS.	
Indirectly held debt security or equity security held through an intermediary not listed above	Intangible property
Cash collateral	Account or, where held in an account of the Custodian or Clearstream, intermediated security[8] [9]
Rights associated with any of the above collateral, including dividends, payment rights arising on conversion or redemption and rights in liquidations or schemes of arrangement.	Proceeds

This memorandum does not address other types of collateral.

The classification of directly held bearer or dematerialized securities depends on whether or not they are negotiable, on the basis that:

(a) negotiable instruments are bills of exchange, cheques, promissory notes, letters of credit and any other writing that evidences a right to payment of currency if the writing is of a kind that, in the ordinary course of business, is transferred by delivery with any necessary endorsement or assignment, or the writing satisfies the requirements for negotiability under the law governing the negotiable instruments; or

(b) investment instruments are, relevantly, debentures of, a body (which commonly means a body corporate or an unincorporated body), debentures or bonds issued or proposed to be issued by a government, derivatives, foreign exchange contracts, interests in, or units in an interest in, managed investment schemes and other specified financial products, but do not include negotiable instruments.

The classification of indirectly held debt securities held in an account with an intermediary will depend on the licensing position of the intermediary. This is because intermediated securities are the rights of a person in whose name an intermediary maintains a securities account. A securities account is defined as:

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7 We assume that Euroclear and Clearstream each hold a licence issued under the law of a foreign jurisdiction permitting it, in the course of business or other regular activity, to *maintain securities accounts* on behalf of others.

8 There is another collateral class called "ADI Account" which is applicable to accounts held in an Authorised Deposit-taking Institution (which is an institution, Australian or not, which is authorised to carry on banking business under the *Banking Act 1959* of Australia). However, for technical reasons it should not be applicable to the interest which the grantor of security has in an account which is in the secured party's name and into which money delivered to the secured party is deposited. Accordingly, ADI Accounts are not relevant to this memorandum and this memorandum does not address ADI Accounts.

9 If the cash collateral is recorded in the same securities account as the indirectly held debt securities referred to above then it is likely to fall within the same characterisation.

- an account to which interests in financial products may be credited or debited; or
- in the case of an intermediary that operates a clearing and settlement facility under an Australian CS Facility licence, a record of holdings and transfers of interests in financial products.

In this context, financial products are, relevantly, bonds, any other financial instrument and any other financial asset (other than cash), or any interest in any of them.

An intermediary is defined as a person:

- who holds an AFSL or licence under the law of a foreign jurisdiction permitting them to maintain securities accounts on behalf of others; or
- who operates a clearing and settlement facility under an Australian CS Facility Licence,

but does not include a central bank.

On this basis, the following securities will be intermediated securities:

(a) securities held by a custodian or nominee with an AFSL or licence under a foreign jurisdiction permitting them to maintain securities accounts. If the custodian or nominee does not hold a licence (including if it does not need to under laws applicable to it), or is a central bank, then the rights of the account holder will be intangible property instead; and

(b) securities held in a clearing system such as Austraclear, Euroclear and Clearstream either:

(i) directly - this will be the case where the securities are held by a person who is a member of the clearing system in a securities account; and

(ii) indirectly - this will be the case where the securities are held on behalf of a person by a custodian or nominee that is a member of the clearing system and that has an AFSL or licence under a foreign jurisdiction permitting them to maintain securities accounts.

If the person that maintains the securities account does not hold a licence (including if it does not need to under laws applicable to it) then the rights of the account holder will not be intermediated securities. In the case of debt securities, they should be intangible property instead.

5.3 PPSA does not displace other laws

The PPSA contains express provisions which clarify its relationship with other laws. These provide that:

- the PPSA is not intended to exclude or limit the operation of Australian Commonwealth or State laws, or the general law of Australia,[10] to the extent that they are capable of operating concurrently with the PPSA;
- specific Australian laws, such as the *Netting Act*, prevail over the PPSA to the extent of any inconsistency; and

[10] The PPSA defines the general law as the principles and rules of the common law and equity.

- the PPSA prevails over laws of the Australian States and Territories which require or enable a person to register a security interest or an assignment of a security interest, the form in which the security agreement must take, or the attachment or perfection of security interests.

5.4 Jurisdictional application of the PPSA

The PPSA contains jurisdictional provisions which define the application of the Act to a security interest by reference to a connection with Australia. It provides that the PPSA applies to a security interest, relevantly:

(a) in any class of personal property if the grantor of the security interest is an Australian entity, which includes an "Australian Company" (as defined in paragraph A.2(c) above); and

(b) otherwise, in:

(i) a negotiable instrument or an investment instrument, if it is located in Australia;

(ii) an intermediated security, if the intermediary is located in Australia; and

(iii) intangible property (including an account) if, relevantly:

(A) it is an account that is payable in Australia; or

(B) it is created, arises or is provided for by a law of Australia (including the general law).[11]

The PPSA sets out rules for determining which entities are Australian entities and the location of entities and property. These are important for understanding its jurisdictional provisions.

Australian Entity

The definition of an Australian entity in the PPSA can be summarised as:

- an individual who is located in Australia; and
- a company registered under the *Corporations Act*;[12] and
- a corporation sole established under an Australian law; and

[11] There is a technical threshold issue to consider in relation to these provisions, being whether they are intended to be exclusive or inclusive. In other words, should these provisions be construed on the basis that the PPSA applies ***only*** to these security interests, or that it does apply to those security interests and may also apply to others. The drafting of the PPSA is not completely clear on this point. In our view, the effect of these provisions should be that the PPSA does not apply to security interests which are not described in these provisions. This is because the intention of the section appears to be to define the jurisdictional connection needed for the PPSA to apply, rather than specifying examples of when it does apply. Examples of this can be found in the Explanatory Memorandum for the PPSA Bill and its second reading speech. Also, this approach is consistent with the legislative principle that some connection (which could be remote, or general) between the subject matter of the legislation and the jurisdiction of legislation is needed for legislation to be valid and the presumption of statutory interpretation that legislation is not intended to have an extra-territorial effect unless a contrary intention is expressed.

[12] For this purpose, this should include foreign companies which are registered under the *Corporations Act*.

- a public authority or agency or instrumentality of the crown in right of Australia, or an Australian state or territory; and
- a registrable Australian body under the *Corporations Act* (in summary an Australian body corporate or unincorporated body which is none of the above).

Location

The rules in relation to the location of entities and property provide that, relevantly:

- a body corporate is located in the jurisdiction in which it is incorporated;
- a body politic is located in the jurisdiction of the body politic; and
- an individual is located at the individual's principal place of residence.
- personal property (including an investment instrument and a negotiable instrument) is located in the particular jurisdiction in which the personal property is situated. However, there are some additional rules including, relevantly:
    - an investment instrument that is not evidenced by a certificate is located in the jurisdiction the law of which governs the transfer of the investment instrument; and
    - a negotiable instrument that is evidenced by an electronic record is located in the jurisdiction the law of which governs the negotiable instrument.

5.5 Jurisdictional scope of this memorandum

This memorandum is given on the assumption that the PPSA applies on a jurisdictional basis. For example, this memorandum does not address security interests granted by an entity which is not an Australian entity in:

- intermediated securities held with an intermediary that is located outside of Australia;
- financial property which is located outside of Australia;
- accounts which are payable outside of Australia; or
- intangible property (other than accounts) which is not created, arises or provided for by a law of Australia.

It is still possible that the general law of Australia can still apply to these interests, if Australian conflict of law rules so determine. However, registration requirements under, and other provisions of, the PPSA would not apply.

6 Summary of the relevant requirements for the protection of enforcement of security under the *Netting Act*

6.1 Overview of the application of *Netting Act* to security-based collateral arrangements

In 2016, the *Financial System Legislation Amendment (Resilience and Collateral Protection) Act 2016* (Cth) ("***Collateral Protection Act***") and *Financial System Legislation Amendment (Resilience and Collateral Protection) Regulation 2016* (Cth) ("***Collateral Protection Regulation***") significantly altered the way in which Australian laws related to security, finance and insolvency apply in a financial market context.

Importantly, the *Collateral Protection Act* amended the *Netting Act* to facilitate the enforcement of particular forms of security. The amendments made to the *Netting Act* and other Acts by the *Collateral Protection Act* also clarified the manner in which close-out rights could be exercised and security could be enforced on the occurrence of specified resolution matters. However, like the current protections which the *Netting Act* provides to close-out netting, the new protections are subject to requirements (also described in this memorandum as safeguards) which must be satisfied in order for the *Netting Act* to protect the enforcement of security.

Some of the most relevant considerations as to the scope of the relevant amendments to the *Netting Act*, and implications on the Security Documents, are set out below.

6.2 Scope of application

The amendments to the *Netting Act* commenced on 1 June 2016. The amendments that are referred to in this memorandum apply in relation to:

(a) close-out netting contracts entered into after 1 June 2016, or that were in existence immediately before 1 June 2016;

(b) the enforcement of a security after 1 June 2016, even if the security was given before 1 June 2016;

(c) "trigger events" (as defined in the *Collateral Protection Act*) that occur for a close-out netting contract after 1 June 2016;[13]

(d) a partial transfer if the certificate of transfer comes into force after 1 June 2016.

Most of the amendments do not apply in relation to an *external administration* that commenced before 1 June 2016. Accordingly, this current form of our memorandum does not apply if there is an *external administration* that commenced before this date.

The amendments to the *Netting Act* have significant implications for the enforcement of security under security-based credit support arrangements which are entered into in respect of obligations of a party to a close-out netting contract (as defined in the *Netting Act*). As noted in our Netting

[13] A "trigger event" for a close-out netting contract is defined in the *Netting Act* to mean an event of a kind mentioned in paragraph (a) of the definition of close-out netting contract. Paragraph (a) of that definition provides that "a contract under which, if a particular event happens: (i) particular obligations of the parties terminate or may be terminated; and (ii) the termination values of the obligations are calculated or may be calculated; and (iii) the termination values are netted, or may be netted, so that only a net cash amount (whether in Australian currency or some other currency) is payable". Simply, a trigger event is an event which gives rise to a close-out right under the relevant close-out netting contract.

Opinion and subject to the assumptions and qualifications in our Netting Opinion, we consider that both the 1992 ISDA Master Agreement and the 2002 ISDA Master Agreement are close-out netting contracts for the purposes of the *Netting Act*, provided that, in the case of the 1992 ISDA Master Agreement, "Second Method" is chosen.

6.3 Protection of enforcement of security

The protection provided by the amended *Netting Act* to the enforcement of security is contained in section 14 of the *Netting Act*. That protection is provided in two sections, 14(1) and 14(2). As noted in our Netting Opinion,[14] we will focus on section 14(2).

Section 14(2) applies if a person who is, or who has been, a party to a close-out netting contract goes into "external administration"[15] and:

(a) Australian law governs the close-out netting contract; or

(b) Australian law governs the *external administration*.

Please see paragraph A.6.8 below for further consideration of the application of section 14(2) of the *Netting Act*.

Section 14(2)(fa) of the *Netting Act*, as amended, provides that:

> "security given over financial property, in respect of obligations of a party to the [close-out netting] contract, may be enforced in accordance with the terms of the security, provided the terms of the security are evidenced in writing (but see section 14A);"

This section is designed to protect the enforcement of security given over financial property, in respect of obligations of a party to the close-out netting contract in accordance with the terms of the security, provided the terms of the security are evidenced in writing. The requirement that the terms of the security are evidenced in writing is considered in paragraph A.6.4 below, and the meaning of "financial property" is considered in paragraph A.6.5 below.

The Explanatory Memorandum[16] provides that the reference to "security" in these sections contemplates the traditional forms of security, being the charge, mortgage, pledge and lien and

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14 In summary, this is because we are asked to assume that the relevant Master Agreement is not governed by an Australian law.

15 Section 5 of the *Netting Act* provides that "a person goes into external administration if:

(a) they become a body corporate that is a Chapter 5 body corporate within the meaning of the *Corporations Act 2001*; or

(b) they are an individual who is an insolvent under administration; or

(c) someone takes control of the person's property for the benefit of the person's creditors because the person is, or is likely to become, insolvent; or

(d) an ADI statutory manager takes control of the person's business under the *Banking Act 1959*; or

(e) the person comes under judicial management under the *Insurance Act 1973*; or

(f) the person, or a part of the person's business, comes under judicial management under the *Life Insurance Act 1995*."

The reference to "an externally administered body corporate" in section 5 of the Netting Act will be replaced by a reference to "a Chapter 5 body corporate" on commencement of the relevant part of the *Insolvency Law Reform Act 2016* (Cth).

analogous concepts under foreign law rather than non-traditional forms of "security interest" (as contemplated by the PPSA) such as a conditional sale agreement (including an agreement to sell subject to retention of title).[17]

The enforcement of security which is protected under the *Netting Act* is not to be void or voidable in the *external administration*.

Relevantly, the protection of the enforcement of security (including the protection against the enforcement being void or voidable) applies despite:

(i) the creation of any encumbrance, or any other interest, in relation to the financial property secured; or

(ii) the operation of any encumbrance, or any other interest, in relation to that financial property,

in contravention of a prohibition in the contract or in the protected security.[18]

These protections apply despite any other law (including the "specified provisions"), but subject to applicable "specified stay provisions". The effect of this is considered further in our responses set out in paragraph B.17 below.

Importantly, the protections apply to the enforcement of security over financial property, in respect of obligations of a party to a close-out netting contract, only to the extent that certain safeguards are satisfied. These safeguards are considered in paragraphs A.6.4 to A.6.7 below. There are also specific limitations on these protections which are considered in paragraphs A.6.8 and A.6.9 below.

6.4 Terms of the security evidenced in writing

In order for the enforcement of security to be protected under the amended *Netting Act*, the terms of the security must be evidenced in writing. This requirement would be satisfied where a security arises through an act where the terms of an agreement in writing between the parties provide for the security to arise on the performance or occurrence of such an act.[19]

6.5 Financial property

To have the benefit of the protections available under the *Netting Act*, the property over which security is granted must be "financial property". The "financial property" concept is intended to cover property which is commonly provided as collateral in financial markets transactions.[20]

Based on the assumptions which we have been asked to make for the purposes of this memorandum, the Eligible Credit Support should fall within the definition of financial property in the *Netting Act*. However, it is a question of fact whether any particular Eligible Credit Support would indeed constitute financial property.

For these purposes, financial property is any of the following property:

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16 As defined above in footnote 2.

17 Explanatory Memorandum, [1.105].

18 Section 14(2)(h) of the *Netting Act.*

19 Explanatory Memorandum, [1.106].

20 Explanatory Memorandum, [1.117].

(a) a security;[21]

(b) a derivative;

(c) a financial product that is traded on a financial market that is:

(i) operated in accordance with an Australian market licence; or

(ii) exempt from the operation of Part 7.2 of the *Corporations Act*;[22]

(d) a negotiable instrument;[23]

(e) currency (whether of Australia or of any other country);

(f) gold, silver or platinum;

(g) property declared by the regulations to be financial property for the purposes of the *Netting Act*;

(h) "intermediated financial property" being, the rights of a person in whose name an intermediary maintains an account to which interests in property or rights to payment or delivery of property of a kind mentioned in any of paragraphs (a) to (g) may be credited or debited, to the extent that those rights relate to the interests in that property or the rights to payment or delivery of that property;

(i) a document evidencing ownership of gold, silver or platinum;

(j) cash collateral (including cash, certificates of deposit and bank bills);

(k) property described in paragraph 5(b), (c) or (e), or paragraph 25, of Attachment H to Prudential Standard APS 112 — Capital Adequacy: Standardised Approach to Credit Risk, made by the Australian Prudential Regulation Authority ("**APRA**") under section 11AF of the *Banking Act 1959* (Cth) ("***Banking Act***") and as in force from time to time, as property that may be recognised as eligible collateral (ignoring any conditions set out in the Attachment);[24]

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21 The term "security" has the meaning given in section 92 of the *Corporations Act* (but, for this purpose, sections 92(3) and (4) of the *Corporations Act* are to be disregarded).

22 The terms "financial product", "financial market" and "Australian market licence" have the meaning given in the *Corporations Act*.

23 The term "negotiable instrument" has the meaning given in the PPSA.

24 Those paragraphs of the APRA standard are:

5.(b) gold bullion;

5.(c) subject to paragraph 11 of this Attachment, debt securities rated by an [external credit assessment institution ("**ECAI**")] where these debt securities have a credit rating grade of either:

(i) four (or better) for long-term securities issued by: Commonwealth, State and Territory governments in Australia (including State and Territory central borrowing authorities); central, state and regional governments in other countries; the Reserve Bank of Australia; central banks in other countries; and the international banking agencies and multilateral regional development banks that qualify for a zero per cent risk-weight as detailed in Attachment A; or

(l) property described in paragraph 5(d) of Attachment H to that prudential standard, ignoring:

(i) the words "and the ADI holding the security has no information suggesting that the security justifies a rating below this level"; and

(ii) any conditions set out in the Attachment; and

(m) a covered bond;[25] and

(n) proceeds (including rights and property) of property that is financial property.

The property described in paragraphs (a) to (n) above will constitute financial property regardless of whether the property (or, for paragraph (h), the intermediary or the account) is in Australia or elsewhere.

Although property can be excluded from the definition of "financial property" for the purposes of the *Netting Act* through declaration in the regulations, as at the date of this memorandum there is no such declaration in the regulations.

6.6 Eligible obligations

The protection provided to the enforcement of security under the *Netting Act* applies to the enforcement of security over financial property, in respect of obligations of a party to a close-out netting contract, only to the extent that, the obligations secured by the financial property, and discharged through the enforcement, are:

(a) eligible obligations in relation to the contract; or

(b) obligations under the contract of a party to the contract to pay interest on an eligible obligation; or

(c) obligations of a party to the close-out netting contract to pay costs and expenses incurred in connection with enforcing security given in respect of an eligible obligation.

For these purposes, an obligation is an "eligible obligation" in relation to a close-out netting contract if the obligation is any of the following:

(i) an obligation under the contract of a party to the contract that relates to a derivative[26] or foreign exchange contract[27] or is of another prescribed kind;[28]

(ii) three (or better) for short-term or long-term securities issued by ADIs, overseas banks, Australian and international local governments and corporates;

5.(e) subject to paragraph 11 of this Attachment, units in a listed trust where the unit price of the trust is publicly quoted on a daily basis and the listed trust is limited to investing in the instruments detailed in paragraphs 5(a) to 5(d) of this Attachment [footnote omitted];…

11. Collateral in the form of securities issued by the counterparty to the credit exposure (or by any person or entity related or associated with the counterparty) is considered to have a material positive correlation with the credit quality of the original counterparty and is therefore not eligible collateral.

25. …the following forms of collateral are eligible collateral under the comprehensive approach:

(a) equities (including convertible bonds) that are included in a main index or listed on a recognised exchange;

(b) units in listed trusts that invest in equities as set out in paragraph 25(a) of this Attachment.

25 The term "covered bond" has the meaning given in the *Banking Act*.

(ii) an obligation that results from the netting of 2 or more obligations that are created under the contract that:

(A) must include at least one obligation covered by paragraph (i) immediately above; and

(B) may include one or more incidental obligations that, taken together, do not form a material part of the net obligation;

(iii) an obligation declared by the regulations to be an eligible obligation in relation to a close-out netting contract.[29]

However, for the purposes of this memorandum, none of the following are eligible obligations in relation to a close-out netting contract:

(A) an obligation under a credit facility,[30] including:

(i) a margin lending facility;[31] and

(ii) an obligation under a financial product that is declared by the Australian Securities and Investments Commission under section 761EA(9) of the *Corporations Act* not to be a margin lending facility;

(B) an obligation under a deposit-taking facility; and

(C) an obligation under a reciprocal purchase agreement (otherwise known as a repurchase agreement), a sell-buyback arrangement or securities loan arrangement.[32]

In light of paragraph (cc) above, Buy/Sell-Back Transactions, Repurchase Transactions and Securities Lending Transactions, as described in Appendix A, should not be entered into under a Master Agreement in respect of which Security Documents are used if the Secured Party wishes to rely on the protection given to the enforcement of security under the *Netting Act*, unless legal advice is obtained that the Secured Party would be able to rely on the protection in the particular circumstance.

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26 The term "derivative" in the *Netting Act* has the same meaning as in Chapter 7 of the *Corporations Act*.

27 The term "foreign exchange contract" has the same meaning as in Chapter 7 of the *Corporations Act*.

28 In this regard, the *Payment Systems and Netting Regulations 2001* (Cth) ("***Netting Regulations***") prescribe as an eligible obligation an obligation that relates to an arrangement that is a forward, swap or option, or any combination of those things, in relation to one or more commodities.

29 As at the date of this memorandum, no such declaration has been made.

30 This term has the meaning given in the regulations made for the purposes of subparagraph 765A(1)(h)(i) of the *Corporations Act*.

31 The term "margin lending facility" has the same meaning as in Chapter 7 of the *Corporations Act*.

32 Under the *Netting Regulations*, each of the following obligations have also been declared not to be an eligible obligation: an obligation under a contract of insurance, including a life policy or a sinking fund policy within the meaning of the *Life Insurance Act 1995* (Cth); an obligation under a managed investment scheme (within the meaning of the *Corporations Act*); an obligation under a lease or licence; an obligation under a guarantee; an obligation to pay money under a cheque, an order for the payment of money or a bill of exchange.

6.7 Possession or control of the Secured Party

The protection provided to the enforcement of security under the *Netting Act* only applies to the extent that, before the enforcement, the financial property is transferred or otherwise dealt with so as to be in the possession or under the control of the secured person, or another person (who is not the grantor) on behalf of the secured person under the terms of an arrangement evidenced in writing. The Explanatory Memorandum expressly recognised Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements ("**EU Directive**") and *The Financial Collateral Arrangements (No 2) Regulations 2003* (UK)[33] ("**FCA Regulations**"), and associated commentary by industry associations such as the Financial Markets Law Committee. The EU Directive and FCA Regulations were informative in the development of the Australian approach.[34]

There are specific circumstances for the purposes of the *Netting Act* in which possession and control will *not* exist, and also those in which possession and control will exist. This memorandum provides clarification on the impact of a Secured Collateral Provider having specific rights which are commonly found in financial market transactions on the Secured Party having possession or control of the relevant financial property.[35] Please see paragraph B.5.1 for more detail in relation to the concepts of possession and control for the purposes of the *Netting Act*.

6.8 Circumstances affecting the protection

If security is given over financial property, in respect of obligations to a party to a *Master Agreement*, then there are some limitations on the protections afforded to the enforcement of the security under the *Netting Act*. These limitations apply in relation to rights and obligations under the Security Document in the same way as they apply in relation to rights and obligations under the *Master Agreement*.[36]

The Secured Party may not rely on the protections afforded to the enforcement of security under the *Netting Act* in either of the following two scenarios:

(a) the following two circumstances exist:

(i) at the time of "acquiring"[37] the right or obligation from another person, the person has notice of the fact that that other person, or the other party to the contract, was at that time unable to pay their debts as and when they became due and payable; and

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33 As amended by *The Financial Collateral Arrangements (No 2) Regulations 2003 (Amendment) Regulations 2009* (UK) and *The Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010* (UK).

34 Explanatory Memorandum, [1.145].

35 The Explanatory Memorandum acknowledged that "historical legal concepts of possession and control may need to, but do not currently (or adequately), deal with control structures used in modern financial market[s] and therefore the Bill provides certainty as to specific circumstances in which the control test in paragraph 14A(1)(b) will, and will not, be satisfied. These deeming provisions are intended to be inclusive and are not intended to restrict in any way the general application of the concepts of possession or control to financial market structures": [1.151].

36 Section 14(9) of the *Netting Act.*

37 The Explanatory Memorandum explains that the term "acquired" is intended to mean both obtained by grant or creation and by transfer, [1.174].

(ii) the person acquired the right or obligation otherwise than as a result of the operation of section 22, 35 or 36R of the *Financial Sector (Business Transfer and Group Restructure) Act 1999* (Cth) ("***Business Transfer Act***");[38] or

(b) the following circumstances exist:

(i) the party goes into external administration; and

(ii) the party acquired the obligation otherwise than as a result of the operation of section 22, 35 or 36R of the *Business Transfer Act*; and

(iii) any of the following are satisfied:

(A) the other person did not act in good faith in entering into the transaction that created the terminated obligation;

(B) when that transaction was entered into, the other person had reasonable grounds for suspecting that the party was insolvent at that time or would become insolvent because of, or because of matters including:

- entering into the transaction; or
- doing an act, or making an omission, for the purposes of giving effect to the transaction;

(C) the other person neither provided valuable consideration under, nor changed their position in reliance on, that transaction.

6.9 Manner of enforcement to comply with applicable law

The *Netting Act* protection of enforcement of security only applies to the extent that the enforcement of security is carried out in a manner that complies with section 420A of the *Corporations Act* (if it applies) and any applicable general law duties that are not inconsistent with the terms of the security.[39] Some of these duties are considered in paragraph B.12 of this memorandum below. The Explanatory Memorandum also provides that:

> "Whilst the security may be enforced in accordance with the terms of the security, the protections provided to the enforcement of security under sections 14(1) and 14(2) would not apply to the extent the terms of the security purported to allow a secured person to appropriate or sell financial property at zero, or nominal, value as the enforcement would not

[38] Section 14(4) of the *Netting Act*.

[39] Explanatory Memorandum, [1.159], which also states that, for example, "the duties to which controllers are subject under Part 5.2 of the *Corporations Act* (e.g. section 420A regarding the controller's duty of care in exercising power of sale) may still apply". See also Explanatory Memorandum, [1.168] - [1.169] which states:

> [I]f another law purported to prevent enforcement of the security in accordance with its terms, it would be inconsistent and must yield. Similarly, if any other law purported to impose conditions that must be satisfied before the security can be enforced, that other law would also be inconsistent and must yield…
>
> However, another law which purported to regulate the manner in which the security is enforced (for example, section 420A of the *Corporations Act*, if it applied, as described above) would continue to apply provided that it only impacted the way in which the secured person need to enforce its security and did not in any way inhibit the actual enforcement of security.

> reflect any attempt to calculate, or value, the financial property in good faith or in a commercially reasonable manner."[40]

The Explanatory Memorandum provides that the reforms to the *Netting Act* which protect the enforcement of security in accordance with the *Netting Act* (including the provisions relating to possession and control) should not be interpreted as limiting or otherwise restricting anything which would otherwise be available or protected at law (including any rights which a secured party would otherwise have by virtue of the PPSA, the exercise of those rights and any protection which applies to those rights or the exercise of those rights).[41]

40 Explanatory Memorandum, [1.160].

41 Explanatory Memorandum, [1.109].

PART B: SECURITY INTEREST APPROACH PURSUANT TO THE SECURITY DOCUMENTS

I. Validity of Security Interests

We set out below our analysis of the issues raised under the heading "Validity of Security Interests" in Part 1 of the Instruction Letter. Except and to the extent as noted in each response, our response to the questions in this part applies equally in circumstances where the *Netting Act* protection for the enforcement of security is sought to be relied on and in circumstances where it is not.

1 Law governing contractual and validity aspects of security

Under the laws of Australia, what law governs the contractual aspects of a security interest in the various forms of Eligible Collateral deliverable under the Security Documents? Would the courts of Australia recognise the validity of a security interest created under each Security Document, assuming it is valid under the governing law of such Security Document (taking into account assumptions (b) and (c) in Schedule 1)?

The *Netting Act* does not contain rules to determine the law governing the contractual aspects or the validity of security interests and, consequently, we do not consider there is any inconsistency between that Act and the application of the PPSA in this regard. Accordingly, our answer to this question applies in the same way, irrespective of whether the *Netting Act* applies to protect the enforcement of a security.

(a) The laws governing the contractual aspects of a security interest

Under general Australian Law, the law governing the contractual aspects of a security interest by an Australian Company in the various forms of Eligible Collateral identified is the governing law of the relevant Security Document. The 'governing law' provisions of the PPSA (described in paragraph (b) immediately below) expressly state that those provisions do not affect the law that governs contractual obligations (including any obligations arising under a security agreement).

(b) The laws governing validity

In addition to the provisions which define the jurisdictional reach (described in paragraph A.5.4), the PPSA contains provisions which set out which law, in proceedings in an Australian court, governs the validity of security interests to which the PPSA applies.[42] These 'governing law' provisions apply only to interests that arise on or after 30 January 2012, being the date on which the PPSA commenced operation.

The 'governing law' provisions provide a primary rule, and then secondary rules applicable to different types of personal property if the primary rule does not apply. The effect of these rules is that:

(i) ***(primary rule)*** if the grantor of a security interest is an Australian entity at the time the security interest attaches to the collateral and the security agreement expressly provides that Australian Law governs the security interest, then Australian Law will

[42] There are limited separate provisions dealing with the jurisdictional linkage required for the operation of the enforcement provisions in the PPSA and for priorities of security interests in property which has been relocated to Australia. We do not comment on those in this memorandum.

govern the validity of the security interest. However, this rule does not apply to a security interest in an account or a security interest which is the transfer of an account; and

(ii) ***(secondary rules)*** if the primary rule described in paragraph (i) above does not apply, then if the security interest is in:

(A) ***negotiable instruments and investment instruments***, Australian law will govern the validity of the security interest if the security interest has attached under Australian Law and, if at the time of the attachment, the property was located in Australia and the secured party had sufficient possession or control to perfect the security interest. Otherwise, the validity of the security interest is governed by the law of the jurisdiction in which the grantor is located when the security interest attaches;[43] and

(B) ***an account or intangible property***, the validity of the security interest is governed by the law of the jurisdiction in which the grantor is located when the security interest attaches, under that law, to the property.

The time of attachment is considered in paragraph B.5.3 below.

No secondary rules on the governing law applicable to the validity of a security interest in intermediated securities are contained in the PPSA.[44] There are two possible consequences of this:

- the PPSA automatically applies in respect of the validity of a security interest in intermediated securities if the jurisdictional provisions of the PPSA are satisfied (that is, that the intermediary is located in Australia) (see paragraph A.5.4 above for further detail); or

- the general law of Australia operates to determine the validity of a security interest in intermediated securities.

In our opinion, the better view is that the lack of secondary rules in relation to intermediated securities is not intended to mean that the PPSA always governs the validity of a security interest in intermediated securities. Rather, the jurisdictional provisions are intended to specify when the 'governing law' provisions of the PPSA apply. Given that no express rules on the governing law applicable to the validity of a security interest in intermediated securities are contained in the PPSA, and in the absence of any other legislation determining the law governing the validity of a security interest, the general Australian Law should determine the governing law.[45]

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43 The PPSA does not expressly deal with the consequences if the foreign law has no concept of attachment.

44 No explanation for this is given in the Explanatory Memorandum to the *Personal Property Securities Bill 2009* of Australia ("**PPS Bill**"). Initial drafts of the PPS Bill did include provisions applicable to intermediated securities included which were based on The Hague Conference Convention of 5 July 2006 on the Law Applicable to Certain Rights in respect of Securities held with an Intermediary, which Australia has not signed.

45 The PPSA expressly does not repeal the common law, including in relation to choice of law rules, to the extent that it is capable of operating concurrently with the PPSA. This interpretation is consistent with the statement in paragraph 7.2 of the Explanatory Memorandum for the PPS Bill that:

"As there are connecting factors which must be met before Australian law is able to determine which law governs a security agreement, Part 7.2 should be read together with clause 6, Connection with Australia."

Under general Australian Law, assuming that the choice of law in the relevant Security Document is a valid and proper choice of law (see paragraph B.19), the Australian Courts would recognise the validity of a security interest created under the Security Document if the security interest was valid under the governing law of the Security Document.[46]

In addition to the rules above, the 'governing law' provisions of the PPSA provide that the laws of the jurisdiction which govern the validity of the security interest in collateral also apply to the validity of the security interest in proceeds of that collateral.[47]

2 Law governing perfection of security interest

Under the laws of Australia, what law governs the proprietary aspects of a security interest (that is, the formalities required to protect a security interest in Collateral against competing claims) granted by the Security Collateral Provider under each Security Document (for example, the law of the jurisdiction of incorporation or organisation of the Security Collateral Provider, the jurisdiction where the Collateral is located, or the jurisdiction of the location of the Secured Party's intermediary in relation to Collateral in the form of indirectly held securities)? What factors would be relevant to this question? Where the location (or deemed location) of the Collateral is the determining factor, please briefly describe the principles governing such determination under Australian Law with respect to the different types of Collateral. In particular, please describe how the laws of Australia apply to each form in which securities Collateral may be held under:

(i) the Non-IM Security Documents pursuant to assumption (i) below in Part B, Section I of Schedule 1 to this memorandum;

(ii) the IM Security Documents pursuant to assumption (n) in Part B, Section III of Schedule 1 to this memorandum; and

(iii) the arrangements described in assumption (o) in Part B, Section III of Schedule 1 to this memorandum.

The alternative view would be that the absence of governing law rules in Part 7.2 of the PPSA in relation to a security interest in intermediated securities was intended to result in the validity and perfection requirements in the PPSA applying to all intermediated securities to which the PPSA applies – being those granted by an Australian entity or where the intermediary is located in Australia (see paragraph A.5.4). However, there is no indication that the omission of an express reference to intermediated securities from the governing law rules in the PPSA was intended to produce this result. Taking into account that such a result would have been a significant departure from previously applicable general law principles, and is not mentioned in the explanatory memorandum which accompanied the PPSA, this intention seems unlikely. Also, if this were intended, then it would have been easily achieved by the inclusion of intermediated securities in the rules applying to financial property, such as investment instruments. As noted above, these rules focus on the location of grantors (which is different to whether they are Australian entities as it excludes foreign incorporated companies), the time of attachment and perfection and potentially the location of the property at those times. The implication that the absence of any reference to intermediated securities in Part 7.2 was intended to result in a much less sophisticated rule applying to intermediated securities (which makes no reference to whether the grantor is "located" in Australia) is somewhat difficult to support. Instead, we consider that the intention was for the PPSA to not affect the general law rules on location of property which previously applied to intermediated securities. This is consistent with the absence of any reference to intermediated securities in Part 7.2. Also, it makes sense from a policy perspective if the new rules on intermediated securities evidenced in earlier PPSA drafts were not able to be included until Australia signed the Hague Convention on intermediated securities (referred to in footnote 44 above).

46 Our conclusions in this memorandum would not change if the relevant Security Document were amended to establish a true unilateral collateral arrangement whereby only the Security Collateral Provider would be required to post collateral.

47 Unless the proceeds are an account (unless the account arises from the dealing which gave rise to the proceeds).

The *Netting Act* does not contain rules to determine the law governing the perfection and effect of perfection or non-perfection of security interests and, consequently, we do not consider there is any inconsistency between that Act and the application of the PPSA in this regard. Accordingly, our answer below applies equally irrespective of whether the *Netting Act* applies to protect the enforcement of a security. However, see our comments in respect of the relevance of perfection to the extent that the *Netting Act* applies to the enforcement of security in paragraph B.5 below.

Subject to the following, the 'governing law' provisions described in paragraph B.1(b) above apply under Australian Law in the same way to determining the law governing perfection and effect of perfection or non-perfection of security interests as they do to determining the law governing the validity of the security interest.

The secondary rules that apply to determine the law governing the validity of the security interest if the security interest is in financial property or intangible property are determined by reference to the time when the security interest attached. Likewise, the secondary rules that apply to determine the law governing the perfection and effect of perfection or non-perfection of security interests in those classes of property at a particular time are determined as of that time.

Also there are no secondary rules on the governing law applicable to the perfection and effect of perfection or non-perfection of a security interest in intermediated securities. For the reasons set out in paragraph B.1(b) above, in our opinion, the better view is that, in the absence of any other legislation determining the law governing the validity of a security interest, the general Australian Law will determine the governing law.

Under the general Australian Law (particularly rules of private international law and conflicts of laws), the better view is that the relevant law governing the perfection and effect of perfection or non-perfection of a security interest in a chose in action is the law of the place of its location (lex situs). Generally, the situs of a chose in action is the place where it is properly recoverable or may be enforced.[48] However, this rule is not easily applied in the context of beneficial co-ownership interests held by an intermediary. Although Australian Law is not entirely clear on this issue, the most likely outcome is that the governing law is the law of the place where the intermediary is located (referred to as the *place of the relevant intermediary approach* ("**PRIMA**")).[49] If there is a chain of intermediaries, each of which holds securities in an omnibus holding for another intermediary down the chain, then the relevant intermediary for determining PRIMA is the last one in the chain (ie the one that credits the interest in the securities to an account in the name of the grantor). In Australia, and as a matter of Australian Law, an intermediary generally holds securities as trustee for the person in whose name the securities account is maintained (referred to in this section of our memorandum as the "**account holder**"). The interests of the account holder are generally characterised as a right to a beneficial interest in whatever is held by the intermediary for the account holder (whether it holds the securities directly or indirectly with another intermediary).[50] Where the intermediary holds interests in securities in an omnibus account for all their clients, then

48 *Dicey, Morris and Collins on The Conflict of Laws*, 14th Edition, p 1125.

49 The Hague Conference Convention of 5 July 2006 on the Law Applicable to Certain Rights in respect of Securities held with an Intermediary, which Australia has not signed, recognised PRIMA.

50 In addition to the beneficial interests referred to above, the rights of the account holder may also comprise contractual rights against the intermediary (including, for example, to demand that the security be withdrawn from the securities account). The precise nature of the rights of the holder of the account in respect of indirectly held securities will be determined, among other things, by the law of the agreement between the holder and the intermediary relating to the account and the law generally applicable to the intermediary. Of course, the interest might be characterised differently in a foreign jurisdiction, if applicable pursuant to the choice of law rules of that foreign jurisdiction.

the account holder's interest under Australian Law is generally characterised as a right to a beneficial co-ownership interest in the pool of assets held by the intermediary.[51]

In addition to the rules above, the laws of the jurisdiction which govern the perfection and the effect of perfection or non-perfection of a security interest in collateral also apply to the perfection and effect of perfection or non-perfection of that security interest in the proceeds of that collateral (respectively).

3 Recognition of security interest

Would the courts of Australia recognise a security interest in each type of Eligible Collateral created under each Security Document? In answering this question, please bear in mind the different forms in which securities Collateral may be held, as described in assumption (g) in Part B, Section 1, of Schedule 1 to this memorandum with respect to Non-IM Security Documents, in assumption (n) in Part B, Section IV of Schedule 1 in with respect to IM Security Documents, and in assumption (o) in Part B, Section IV of Schedule 1. Please indicate, in relation to cash Collateral, if your answer depends on the location of the account in which the relevant deposit obligations are recorded and/or upon the currency of those obligations.

In our opinion, irrespective of whether the *Netting Act* applies to protect the enforcement of a security, Australian Courts would recognise a security interest in each type of Eligible Collateral created under each Security Document, provided that:

(a) the security interest was valid under the laws that govern the validity of the security interest (as to which see paragraph B.1(b) above); and

(b) unless the *Netting Act* applies to protect the enforcement of security, any perfection requirements in relation to the Eligible Collateral had been complied with under the laws that govern the perfection and effect of perfection or non-perfection of the security interest (as to which see paragraph B.2 above).

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[51] The following principles support this approach:

(a) if it is true that the nature of the interest is a beneficial co-ownership interest in the pool of assets held by the intermediary, then to determine the location of such a beneficial interest, an Australian Court would apply either the place where the trust assets are located or the place of the trustee. If the beneficiary has an absolute right to call for the delivery of the trust assets in specie, then the beneficial interest will be located at the place of the assets. If the beneficiary does not have such a right, then the location of the interest will be the place of the trustee: *Dicey, Morris and Collins on The Conflict of Laws*, 14th Edition, p 1127. In the case of intermediated book entry securities (such as all those in Austraclear, Euroclear or Clearstream), an investor does not have a right to demand a transfer in specie, but only has a right to call for delivery of equivalent securities. Accordingly, under the application of traditional conflict of law principles, the lex situs should be the place of the intermediary: Moshinsky M; "Securities held through a securities custodian - conflict of laws issues" (1998) *JIBFL* 18;

(b) the principle traditionally applied to determine the (fictional) location of intangibles is that they are located where they may be enforced. It has been argued that this is essentially a question of locating the place where the record that determines the interest is located; and

(c) the alternative approach, being the look-through approach would not produce a result which is consistent with the PPSA framework. This would result in the governing law being determined by the location of the underlying instruments which the intermediated security represents. However, this is a different kind of property under the PPSA, being investment instruments, which have their own choice of law rules. Although it would be possible to argue, it seems highly improbable that the governing law rules for intermediated securities should be determined by reference to the common law rules applicable to investment instruments which are otherwise inapplicable because of the PPSA.

Prior to the commencement of the PPSA there had been some uncertainty under Australian Law as to whether a person may take a security interest in respect of their own indebtedness. The PPSA clarifies that it is possible for a person who owes an obligation to another person to take a security interest over the other person's right to that performance, dispelling concerns with the effectiveness of "charge-backs" in Australia. The amended *Netting Act* also clarifies that it is possible for a person who owes payment or performance of an obligation to another person to take security over the other person's right to require the payment or performance of the obligation.

4 Effect of fluctuating exposures or Collateral

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

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

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

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

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

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

In relation to (a), it is understood that the security interest in any specific Collateral would only be relevant in relation to future obligations, if ever, at the time such future obligations arise and then only in relation to Collateral held at that time. This question concerns whether it would be necessary for either party to perform any action at such time in order to ensure the effectiveness of the security interest as security for such obligations or whether the security interest would take effect in relation to those future obligations without further action by either party.

In relation to (b), it is understood that the security interest in Collateral to be delivered at some point in the future after the time of entry into the relevant Security Document would not take effect in relation to such Collateral until the Collateral had been delivered to the Secured Party in accordance with the Security Document. This question concerns whether it would be necessary for either party to perform any action at such time in order to ensure the effectiveness of the security interest in relation to such Collateral or whether the security interest would take effect in relation to such Collateral without further action (other than the delivery) by either party.

In relation to (c), you may assume that each specific delivery to the Secured Party and return by the Secured Party of Collateral under the Security Document from time to time would be properly recorded by the Secured Party, so that, while the pool of Collateral would change from time to time,

at any specific time the composition of the pool of Collateral could be clearly identified by the Secured Party.

As a matter of Australian Law there are no adverse consequences arising from the fact that the amount secured or the amount of Eligible Collateral subject to the security interest will fluctuate under the Master Agreement and the relevant Security Document, provided it does so in accordance with the terms agreed between the parties. Other than as set out in paragraph B.4(c) below, our answer applies equally irrespective of whether the *Netting Act* applies to protect the enforcement of the security.

Subject to the proviso above, and in answer to the specific questions on this point:

(a) Future Obligations

The security interest would be valid in relation to future obligations of the Security Collateral Provider, provided the future obligations are able to be identified as and when they arise, by reference to the terms of the Security Document (which will include future obligations arising under Section 6 of the Master Agreement). The PPSA provides that a security agreement may provide for future advances, and that a security interest provided for by a security agreement has the same priority in respect of all advances (including future advances) and obligations secured by the agreement.[52] [53]

(b) Future Collateral

The security interest would be valid in relation to future Collateral, provided the future Collateral is able to be ascertained as and when it is provided as Collateral. The PPSA provides that a security agreement may provide for security interests in after-acquired property and that a security interest in after-acquired property attaches without specific appropriation by the grantor. As a matter of Australian Law, the security interest would not be created until the collateral is provided.

(c) Fluctuating pool of assets

There is no difficulty with the concept of creating a security interest over a fluctuating pool of assets, provided the pool of assets is identified with sufficient clarity to identify the collateral at any given time. However, in order for the *Netting Act* protection to apply to the enforcement of the security, a number of conditions need to be met, including that the Collateral must be transferred or otherwise dealt with before enforcement so as to be in the possession or under the control of the Secured Party, or another person (who is not the Security Collateral Provider) on behalf of the Secured Party. For these purposes, this condition will not be satisfied if, under the security, the Security Collateral Provider is free to deal with the Collateral in the ordinary course of business until the Secured Party's interest

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[52] An "*advance*" is broadly defined to mean the payment of currency, the provision of credit or the giving of value and includes any liability of a debtor to pay interest, credit costs and other charges or costs payable by the debtor in connection with the advance or the enforcement of a security interest securing the advance. A "*future advance*" is defined broadly to mean an advance secured by a security interest (whether or not made pursuant to an obligation), if the advance is made after the security agreement was made or expenses in relation to the enforcement of a security interest that are secured by the security interest.

[53] Our conclusion is not altered by the fact that specific Transactions to which the collateral relates will change over time as the counterparties enter into new Transactions under a particular Master Agreement and as Transactions terminate according to their terms.

in the Collateral becomes fixed and enforceable. Please see our response set out in paragraph B.5.1 for more detail in this regard.

(d) Necessity for Fixed Amount

It is not necessary under Australian Law for the amount secured by each Security Document to be a fixed amount or subject to a fixed maximum amount.

(e) Excess Collateral

It is permissible under Australian Law for the Secured Party as Secured Party to hold Collateral in excess of its actual exposure to the Security Collateral Provider under the related Master Agreement.

In regards to the effect of the recent amendments to the *Netting Act* on the above, the Explanatory Memorandum provides as follows:

> The protections provided under this Bill provide a facilitative protective regime (subject to the safeguards set out in the Bill) and do not adversely affect existing Australian laws. For example, it is noted that under existing Australian law, security may be valid notwithstanding the fact that the security secures future obligations or fluctuating obligations, or that the security is granted over a fluctuating but identified and identifiable pool of property (provided it does so in accordance with the terms agreed between the parties), or that the grantor may provide financial property in excess of the secured obligations. Additionally, the Bill does not impose a requirement for the amount secured to be subject to a fixed amount or fixed maximum amount which does not otherwise exist under Australian law.[54]

5 Steps for attachment and perfection

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

As discussed in paragraph A.6 of this memorandum, the *Netting Act* protection of enforcement of security applies despite any other law (including the additional perfection requirements under the PPSA) but subject to certain safeguards being met. However, the steps for attachment and perfection under the PPSA continue to be relevant to an enforcement of security if the Security Collateral Provider is not subject to *external administration* governed by an Australian law (as discussed in paragraph A.4 of this memorandum). On this basis, our response to this question considers the requirements for enforceability of security interests against the grantor and third parties:

(a) under the *Netting Act* in paragraph B.5.1 below, that the Collateral must be transferred or otherwise dealt with before enforcement so as to be in the possession or under the control

[54] Explanatory Memorandum, [1.105].

of the Secured Party, or another person (who is not the Security Collateral Provider) on behalf of the Secured Party;[55] and

(b) under the PPSA (which are relevant when the *Netting Act* protection does not apply but which we recommend compliance with) in paragraphs B.5.2 to B.5.4 below, being the requirements of attachment and perfection (which defines when the security interest sets its priority against other interests in the same collateral).

5.1 Possession and control requirements under the *Netting Act*

As noted above, for the *Netting Act* protection to apply to the enforcement of security, a number of conditions need to be met, including that the Collateral must be, before enforcement, transferred or otherwise dealt with so as to be in the possession or under the control of the Secured Party, or another person (who is not the Security Collateral Provider) on behalf of the Secured Party under the terms of an arrangement evidenced in writing. Whilst some aspects of the possession and control concepts are questions of law, it is also a question of fact as to whether Collateral has been transferred or otherwise dealt with so as to be in the possession or under the control of the Secured Party or another person (who is not the Security Collateral Provider) on behalf of the Secured Party, under the terms of an arrangement evidenced in writing. To that end, there are specific circumstances in which possession and control will, and will *not*, exist for the purposes of the *Netting Act* as set out below (although these are not intended to be an exhaustive list).

Circumstances where the financial property is not in the possession or control of the Secured Party (or person acting on their behalf)

Financial property is taken to *not* be in the possession or control of a person if, under the security, the Security Collateral Provider is free to deal with the financial property in the ordinary course of business[56] until the Secured Party's interest in the financial property becomes fixed and enforceable.[57] This applies even if the Secured Party's interest in the financial property becomes fixed and enforceable before the enforcement of the security over that property.[58] Accordingly, a security which was historically considered to be a "floating charge" over all present and after-acquired property (or all present and after-acquired property of a particular class) should not, without more, satisfy the possession or control test for the purposes of the *Netting Act*.[59]

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55 We assume for these purposes that:

(a) the enforcement of the security is within the scope of application of the *Netting Act* (as set out in paragraph A.6.2);

(b) the *Netting Act* requirements considered in paragraphs A.6.4, A.6.5 and A.6.6 are met; and

(c) that the limitations to the *Netting Act* protection considered in paragraph A.6.8 do not apply.

56 The Explanatory Memorandum states that this concept reflects the "ordinary course of business" concept set out in *In re Yorkshire Woolcombers Association Limited; Houldsworth v Yorkshire Woolcombers Association Limited* [1903] 2 Ch 284 in respect of floating charges.

57 The Explanatory Memorandum states that the reference to an interest in the financial property being "fixed and enforceable" means that circumstances arise such that the floating charge attaches to specific property and the grantor ceases to be able to deal with the property and the secured person has a presently exercisable right to take enforcement action in respect of the secured property: [1.147].

58 Section 14A(3) of the *Netting Act* has the effect that security under which the grantor was free to deal with the financial property in the ordinary course of business at some time on or after creation of the security is taken not to be in the possession or under the control of a person even if the interest in the financial property becomes fixed and enforceable before the enforcement of the security over financial property which is described in paragraph 14A(1)(b) of the *Netting Act*: Explanatory Memorandum, [1.147].

59 Explanatory Memorandum, [1.147].

Circumstances where the financial property is in the possession or control of the Secured Party (or the person acting on their behalf)

Where there is an issuer of the financial property, that property is in the possession or control of the Secured Party (or relevant person acting on its behalf), if they are registered by, or on behalf of, the issuer as the registered owner of the financial property.[60] In a case where the financial property is intermediated financial property, that property is in the possession or control of the Secured Party (or relevant person acting on its behalf), if they are the person in whose name the intermediary maintains the account.[61]

In addition, intermediated financial property would be under the possession or control of the Secured Party (or relevant person acting on its behalf), if:

(a) the intermediary is not the Security Collateral Provider (but may be the Secured Party or any other person); and

(b) there is an agreement in force between the intermediary and one or more other persons, one of which is the Secured Party or the Security Collateral Provider, which has one or more of the following effects:

(i) the person in whose name the intermediary maintains the account is not able to transfer or otherwise deal with the financial property;

(ii) the intermediary must not comply with instructions given by the Security Collateral Provider in relation to the financial property without seeking the consent of the Secured Party (or relevant person acting on its behalf);

(iii) the intermediary must comply, or must comply in one or more specified circumstances, with instructions (including instructions to debit the account) given by the Secured Party in relation to the intermediated financial property without seeking the consent of the Security Collateral Provider (or any person who has agreed to act on the instructions of the Security Collateral Provider).

Further, the fact that the Security Collateral Provider has one or more (or all) of the rights described below does *not* of itself mean that the Secured Party (or relevant person acting on its behalf) does not have possession or control or that the Security Collateral Provider is free to deal with the financial property in the ordinary course of business:

(A) right to receive and withdraw income in relation to the financial property;

(B) right to receive notices in relation to the financial property;

(C) right to vote in relation to the financial property;

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60 The Explanatory Memorandum provides that the "first limb of section 14A(4) is intended to cover the situations where the secured person or third party is registered by, or on behalf of, the issuer as the registered owner of the financial property, including where such registration happens on the Clearing House Electronic Sub register System (CHESS) sub register, maintained by ASX Settlement, or the issuer sponsored sub register, maintained by the issuer or a share registry on the issuer's behalf".

61 The Explanatory Memorandum provides that: "Due to the breadth of the concept of 'intermediary', this would include circumstances where, if the financial property is traded or settled through a clearing house or securities depository, the clearing house or securities depository, as the case may be, records the interest of the person in the financial property".

(D) right to substitute other financial property that the parties agree is of equivalent value for the financial property;

(E) right to withdraw excess financial property;

(F) right to determine value of financial property.

For completeness, we note that the regulations may also prescribe circumstances in which financial property is, or is not, transferred or dealt with so as to be in the possession or under the control of a person for the purposes of the *Netting Act*. As at the date of this memorandum, there are no regulations prescribing such circumstances.

5.2 PPSA provides for enforceability against grantor and third parties

If Australian Law governs the validity of the security interest (the rules for which are described in paragraph B.1(b) above), then the PPSA provides that the security interest in collateral:

(a) is enforceable against a grantor only if the security interest has attached to the collateral; and

(b) is enforceable against a third party only if:

(i) the security interest is attached to the collateral; and

(ii) one of the following applies:

(A) the secured party possesses the collateral;

(B) the secured party has perfected the security interest by control (see below); or

(C) a written security agreement that provides for the security interest covers the collateral.

These concepts are discussed below. In relation to the requirement for a written security agreement, this would be satisfied by the Security Document.[62]

5.3 PPSA requirement of attachment

Once a security interest is attached to personal property, it is referred to as "**collateral**" under the PPSA. A security interest attaches to collateral under the PPSA when:

(a) the grantor has rights in the collateral, or the power to transfer rights in the collateral to the secured party; and

(b) either:

(i) value is given for the security interest; or

[62] Provided that the Security Document is signed by the grantor of the security interest or otherwise adopted or accepted by the grantor by an act or omission that reasonably appears to be done with the intention of adopting or accepting the writing.

(ii) the grantor does an act by which the security interest arises.

Under the Security Documents, value, in most cases, should be seen as given because of the continuing reciprocal obligations of the parties under the Transactions and the entering into of new Transactions subject to the terms of the Security Documents.

If collateral gives rise to proceeds, the security interest attaches to the proceeds unless the security agreement provides otherwise.

5.4 PPSA requirement of perfection

If Australian law governs the perfection of the security interest (the rules for which are described in paragraph B.2 above), then the PPSA provides that a security interest is perfected under the PPSA if (relevantly):

- the security interest is temporarily perfected, or otherwise perfected, by force of the PPSA;[63] or
- all of the following apply:
  - (i) the security interest is attached to the collateral;
  - (ii) the security interest is enforceable against a third party; and
  - (iii) any of the following applies:
    - (A) a registration is effective with respect to the collateral;
    - (B) the secured party has possession of the collateral (other than possession as a result of seizure or repossession); or
    - (C) the secured party has control of the collateral, provided that the collateral is, relevantly, an intermediated security, an investment instrument or an uncertificated negotiable instrument.

Registration, possession and control are considered below.

While the PPSA does not require a secured party to "perfect" its security interest in the collateral, if the secured party does not do so:

- another security interest may take priority (see paragraph B.16 and Schedule 2 below);
- another person may acquire an interest in the collateral free of the secured party's security interest (see paragraph B.16 and Schedule 2 below); and
- it may not be able to enforce the security interest against a grantor who becomes insolvent (see paragraph B.18 and Schedule 3 below).

(a) Perfection by registration

[63] An example of this is in relation to proceeds, see paragraph (d) below.

A security interest can be perfected by the registration of a financing statement with respect to the security interest on the Personal Property Securities Register ("**PPS register**") maintained by the Registrar of Personal Property Securities.

A financing statement may be registered whether or not the personal property to which the statement relates, or any person who owns or has rights in that property, is located in Australia. Security interests can be registered before the security agreement is entered into and before or after a security interest attaches to the property described in the financing statement. A person may apply to register a financing statement if they believe on reasonable grounds that the person described in the financing statement as the secured party is, or will become, a secured party in relation to the collateral.

A copy of the security agreement need not be lodged but certain persons may request a copy of the agreement from the secured party and the secured party must comply with this request within 10 business days unless exceptions apply.[64]

Transitional provisions with respect to registration

The PPSA has an effect on security interests and security agreements arising before 30 January 2012 ("**transitional security interests**"). The priority rules in the PPSA will apply to these security interests subject to the transitional provisions.

The transitional provisions provide that security interests registered on certain existing registers were to be migrated to the PPS register (for example, charges registered on the ASIC Register of Company Charges).[65] However, this is likely to be effective only to the extent that the charges were required to be registered under the *Corporations Act*.

Transitional security interests which were not migrated, or which were not registered on any existing registers, will need to be registered on the PPS register (or otherwise perfected) before the end of the two year transitional period in order to preserve priority (although before that time, they may be subject to "taking free" rules which may affect their priority, depending on the type of personal property).[66] This means that transactions which were not regarded as security interests under previous Australian law but may be security interests under the PPSA, either because they are "in substance" security interests or deemed security interests, will need to be registered (or otherwise perfected).

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64 It is possible that some additional wording in relation to confidentiality would be beneficial if registration were undertaken (if the contents of the security document are to be confidential). The PPSA allows certain interested persons to request a copy of the security agreement that provides for a security interest (together with other information) from a secured party. Interested persons include other secured creditors. The secured party must respond to the request within 10 business days of receiving the request unless various exceptions apply. One of the exceptions is that the secured party need not provide that information if the secured party has a confidentiality agreement with the debtor in writing which provides that neither of them will disclose information of the kind required to be provided. However, the confidentiality agreement will not apply if:

- the confidentiality agreement was made after the security agreement providing for the security interest is made;
- at the time the request is received, the debtor is in default under the security agreement;
- the debtor has given written authorisation for the disclosure of the information; or
- the information has been requested by the grantor or its auditor.

65 See http://www.ppsr.gov.au/www/ppsr/ppsr.nsf/Page/AboutPPS_AboutPPS#security.

66 See paragraph B.16 and Schedule 2 below for further information on "taking free" rules.

Please see paragraph B.16 and Schedule 2 below with respect to the priority of security interests under the transitional provisions.

(b) Perfection by possession

In most cases, a security interest can only be perfected by possession if physical possession of the collateral is possible, ie there is some tangible evidence of the collateral which can be possessed. For example, possession is possible for:

(i) negotiable instruments that are not evidenced by an electronic record;[67] and

(ii) investment instruments if they are evidenced by a certificate.[68]

The PPSA states that a secured party cannot have possession of personal property if the property is in the actual or apparent possession of the grantor or debtor or another person on their behalf. By contrast, the PPSA also states that a grantor or debtor cannot have possession of the personal property if the property is in the actual or apparent possession of the secured party or another person on their behalf. This suggests that third party custodian arrangements will be sufficient to give the secured party possession where the custodian is acting on behalf of the secured party.

(c) Perfection by control

A security interest in certain types of collateral can be perfected by the secured party taking control of the collateral. They are, relevantly, an uncertificated negotiable instrument, an investment instrument or an intermediated security. Perfection by control confers greater priority than perfection by registration or possession.

The manner by which a secured party can take control depends on the type of personal property which is subject to the security interest:

(i) ***(negotiable instruments)*** control is taken over negotiable instruments which are not certificated if the instruments are able to be transferred in accordance with the operating rules of a clearing and settlement facility and there is an agreement in force under which the secured party (or a person who has agreed to act on the instructions of the secured party) controls the sending of some or all electronic messages or other electronic communications by which the instruments could be transferred. It is not possible to perfect by control a security interest in negotiable instruments which are certificated (but they can be perfected by possession);

(ii) ***(investment instruments)*** control is taken over investment instruments if:

(A) the issuer registers the secured party as the owner of investment instruments; or

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67 Such possession requires that the person, or another person on its behalf, takes physical possession of the instrument.

68 Such possession requires that the certificate specifies the person who is entitled to the investment instrument and that the transfer of the investment instrument may be registered on books maintained for that purpose by or on behalf of the issuer and either the possessor (or someone on its behalf) has possession of the certificate or the registered owner acknowledges in writing that it is holding possession on behalf of the possessor.

(B) where the investment instruments are evidenced by a certificate, the secured party has possession of the instruments and the secured party (or a person who has agreed to act on the instructions of a secured party) is able to transfer the instrument to the secured party (or another person) or otherwise deal with the instruments. We consider that this control test will be satisfied if the grantor gives the relevant certificates together with executed blank transfer forms with an authority to complete them or a power of attorney to the secured party (or a person who has agreed to act on the instructions of the secured party); or

(C) where the investment instruments are not evidenced by a certificate, one of the following circumstances applies:

(I) the secured party has an agreement with the grantor to the effect that the secured party (or a person who has agreed to act on the instructions of the secured party) is able to initiate or control sending instructions by which the investment instrument could be transferred or otherwise dealt with; or

(II) the issuer registers another person (not the grantor or debtor) as the owner of the investment instrument on behalf of the secured party, or another person (not the grantor or debtor) acknowledges in writing that it holds the instrument on behalf of the secured party, and in each case there is an agreement with the secured party under which the secured party (or a person who has agreed to act on the instructions of the secured party) is able to initiate or control sending some or all electronic messages or other electronic communications by which the instrument could be dealt with;

(iii) ***(intermediated securities)*** control is taken over intermediated securities if:

(A) there is an agreement between the grantor and either or both of the intermediary and the secured party (of which the intermediary has notice, if it is not a party to it) which has the effect that:

(I) the intermediary must not comply with instructions given by the grantor in relation to the intermediated securities without seeking the consent of the secured party (or a person who has agreed to act on the instructions of the secured party); or

(II) the intermediary must comply, or must comply in one or more specified circumstances, with instructions (including instructions to debit the account) given by the secured party in relation to the intermediated securities without seeking the consent of the grantor (or any person who has agreed to act on the instructions of the grantor).

For securities held by a licensed custodian or nominee, these control tests would require the secured party to enter into a control agreement with the relevant licensed custodian or nominee; or

(B) there is an agreement in force under which the secured party (or a person who has agreed to act on the instructions of the secured party) is able to initiate or control the sending of some or all electronic messages or other electronic communications by which the intermediated securities could be transferred or otherwise dealt with; or

(C) the securities account is maintained in the secured party's name or is maintained in the name of another person (other than the debtor or grantor) and that person acknowledges in writing that it holds the intermediated securities on behalf of the secured party; and

(iv) ***(intangible property)*** security interests over relevant intangible property including accounts may not be perfected by control.

(d) Perfection of proceeds

While control is sufficient to perfect a security interest in uncertificated negotiable instruments, investment instruments and intermediated securities, control is not sufficient to perfect the proceeds of such collateral.[69]

A security interest will be temporarily perfected over proceeds of the original collateral, but only for a period of 5 business days after such proceeds arise. The secured party will have to act to separately perfect the security in relation to these proceeds within this period. If they fail to do this, then they may lose priority, or may lose the benefit of the proceeds altogether.

(e) Continuous perfection

A security interest currently perfected by control will have priority over a security interest perfected in another way regardless of when the control was established. However, priority between two security interests perfected by control is determined according to the time of perfection by control, provided that perfection has been continuous.

(f) Summary on the need for registration

If the secured party under the Security Documents receives and holds investment instruments and intermediated securities in its own name (or with their custodian in its own name) then this should satisfy the requirements of control for investment instruments and intermediated securities in the PPSA. However, other relevant forms of collateral cannot be perfected by control. Furthermore, as noted in the paragraphs above, control provides only limited perfection in relation to proceeds and needs to be continuous to be effective. Finally, to the extent that the Security Document creates a security interest in circulating assets (see paragraphs B.11) control is insufficient to protect against the insolvency-related matters set out in paragraph B.18 and Schedule 3. Accordingly, although control is an effective perfection method under the PPSA, we suggest that secured parties consider the relevance of these risks and whether registration should be conducted in addition to perfecting by control.

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69 A security interest in proceeds is perfected if the security interest in the original collateral is perfected by a registration which describes the proceeds in a manner compliant with the regulations or which covers the original collateral (if the proceeds are of a kind that are within the description of the original collateral or if the proceeds consist of currency, cheques or an ADI account, or a right to an insurance payment or any other payment as indemnity or compensation for loss or damage to the collateral or proceeds).

5.5 The need for stamping

Previously, a liability for stamp duty in respect of a Security Document may have arisen if the Security Document affected property located or taken to be located in New South Wales at relevant times. This type of stamp duty was abolished on and from 1 July 2016 and as a result, a stamp duty liability should not arise in respect of a Security Document on or after this date.

6 Other requirements for valid security interests

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

Irrespective of whether the *Netting Act* applies, there are no particular additional requirements or formalities to ensure the validity or perfection of security interests in relation to the contemplated Eligible Collateral, other than those contemplated by the Security Documents. It is not necessary as a matter of formal validity that the Security Documents be expressed to be governed by Australian Law or that they be translated into another language or for them to include specific wording.

7 Action required to maintain security interest

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

Once any additional Collateral is transferred to the Secured Party and is subject to the security interest in favour of the Secured Party in accordance with the Security Document, the validity, continuity, perfection or priority will be determined in the manner considered above. Where the *Netting Act* applies, this will be in accordance with the conditions set out under that Act and considered in paragraphs A.6 and B.5.1 above, where it does not, these will include the considerations outlined in paragraphs B.5.2 to B.5.4 above. Otherwise, no additional actions of this kind will be required, provided any additional Eligible Collateral is within the scope of the relevant Security Document.

8 Requirements where Australian Law is not the governing law for validity and perfection

Assuming that (a) pursuant to the laws of Australia, the laws of another jurisdiction govern the creation and/or perfection of a security interest in the Eligible Collateral transferred by way of security pursuant to each Security Document (for example, because such Collateral is located or deemed to be located outside Australia) and (b) the Secured Party has obtained a valid and perfected security interest in the Eligible Collateral under the laws of such other jurisdiction, will the Secured Party have a valid security interest in the Collateral so far as the laws of Australia are concerned? Is any action (filing, registration, notification, stamping or notarisation or any other

action or the obtaining of any governmental, judicial, regulatory or other order, consent or approval) required under the laws of Australia to establish, perfect, continue or enforce this security interest? Are there any other requirements of the type referred to in question 6 above?

Subject to the one PPSA rule specified below, if the Secured Party has obtained a valid and perfected security interest pursuant to the laws of that other jurisdiction, then an Australian Court will recognise that the Secured Party has a valid and perfected security interest in the Eligible Collateral. There are no actions required under Australian Law to perfect or enforce this security interest or other requirements of the type referred to in question 6 above. However, certain procedural requirements would need to be met if a foreign judgment was sought to be enforced in an Australian Court.

Where the *Netting Act* does not apply, there is one PPSA rule which applies if:

(a) the jurisdictional provisions of the PPSA are satisfied (described in paragraph A.5.5 above);

(b) pursuant to the rules in the PPSA, Australian law does not govern the validity of the security interest (the rules for which are described in paragraph B.1(b) above); and

(c) the laws of the jurisdiction that govern the perfection of a security interest in the Eligible Collateral do not provide for the public registration or recording of the security interest or a notice relating to the security interest.[70]

In these circumstances, the PPSA provides that the security interest will have priority, in proceedings in an Australian Court, over another interest in personal property if:

(i) that security interest is perfected by registration under the PPSA before the other interest attaches to the personal property; and

(ii) except in the case of accounts (in which case only (a) above applies), when the other interest arises in the personal property, that property is located in Australia and the Secured Party does not have possession or control of it.

This priority rule does not apply if (i) and (ii) are not satisfied.

This priority rule is not relevant to the extent that the *Netting Act* applies to protect the enforcement of a security where the Collateral Provider or Secured Party is subject to *external administration* governed by Australian law.[71] However, the priority rule continues to be relevant to an enforcement of security where the *Netting Act* protection does not apply, including prior to any such *external administration*.

Further, it is possible that further action would be needed if, as a result of relocation of the grantor or the property, Australian Law becomes applicable to perfection (and the effect of perfection or non-perfection).

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70 It should be noted that with certain types of collateral this may not be relevant in the context of this memorandum. For example, in the case of a security interest in an account granted by an Australian Company the rules described in paragraph B.1(b) above will provide that Australian law governs validity and perfection.

71 Where applicable, the *Netting Act* applies despite any other law (including, relevantly, the additional requirements imposed by the PPSA in relation to the enforceability, validity and perfection of security interests, the PPSA's priority framework and any vesting which could otherwise occur under the PPSA or *Corporations Act* due to non-perfection or a delay in perfection), albeit subject to the specified stay provisions.

9 Secured party duties

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

The PPSA does not impose any duties on Secured Parties in relation to the care of collateral except in the exercise of enforcement rights provided for by the PPSA (in respect of which, please see paragraph B.12 below).

Under general Australian Law, the Secured Party is under an obligation to take reasonable steps to ensure the safe custody of any secured property in its possession.[72] Further, in our opinion an Australian Court would recognise any contractual duty to exercise reasonable care to assure safe custody as set out in the Security Documents.

10 Dealings with Collateral

Please note that pursuant to the terms of each Deed and the IM NY Annex, the Secured Party is not permitted to use any Collateral securities it holds. This is because, (a) at the time that the Deed was published, it was thought, as a matter of English law, that any such use is or may be incompatible with the limited nature of the interest that the Secured Party has in the Collateral[73], and (b) the rules promulgated by various regulators prohibit the use of any Collateral securities held by the Secured Party due to the Collateral being "initial margin". On the other hand, unless otherwise agreed to by the parties, Paragraph 6(c) of the 1994 NY Annex and the VM NY Annex grants the Secured Party broad rights with respect to the use of Collateral, provided that it returns equivalent Collateral when the Pledgor is entitled to the return of Collateral pursuant to the terms of the 1994 NY Annex or the VM NY Annex, as applicable. Such use might include pledging or rehypothecating the securities, disposing of the securities under a securities repurchase (repo) agreement or simply selling the securities. Do the laws of Australia recognise the right of the Secured Party so to use such Collateral pursuant to an agreement with the Pledgor? In particular, how does such use of the Collateral affect, if at all, the validity, continuity, perfection or priority of a security interest otherwise validly created and perfected prior to such use? Are there any other obligations, duties or limitation imposed on the Secured Party with respect to its use of the Collateral under the laws of Australia?

If Australian Law does not govern the validity, perfection and effect of perfection or non-perfection of security interests to which the PPSA applies (as to which, please see paragraphs B.1(b) and B.2 above), then in our view there is no reason in principle why an Australian Court would seek to interfere with such arrangements if they were valid as a matter of New York law. Please see paragraph B.19 below for discussion of the Australian position in relation to the recognition of New York law as the governing law of the Security Document.

If Australian Law governs the validity and perfection of security interests to which the PPSA applies (as to which, please see paragraphs B.1(b) and B.2 above) then, we note that:

(a) the PPSA does not contain provisions which expressly authorise a Secured Party to deal with the Collateral except where the Secured Party seizes the Collateral pursuant to the exercise of a right to do so on default by the debtor; and

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72 Although this obligation is usually applied in the context of tangible assets, if it were to be applied to intangible assets in the nature of dematerialised securities, we consider that a holding by a custodian of the relevant interests would satisfy these requirements.

73 We understand that these concerns remain as a matter of English law unless the Deed falls within the scope of the Financial Collateral Arrangements (No. 2) Regulations 2003, which implement in the United Kingdom Directive 2002/47/EC of the European Parliament and Council of 6 June 2002 on financial collateral arrangements.

(b) the PPSA provides that a security agreement is effective in accordance with its terms; and

(c) any dealing with the Collateral by the Secured Party authorised by Paragraph 6(c) of the 1994 NY Annex or the VM NY Annex is expressly agreed to be "free from any claim or right of any nature whatsoever of the [Security Collateral Provider], including any equity or right of redemption". This may be characterised under Australian Law as constituting a prospective release by the Security Collateral Provider of its interests in the affected Collateral, intended to take effect on the occurrence of such a dealing.

As noted in paragraph B.5.1 above, a condition to protection under the *Netting Act* requires that the Collateral must be, before enforcement, transferred or otherwise dealt with so as to be in the possession or under the control of the Secured Party, or another person (who is not the Security Collateral Provider) on behalf of the Secured Party under the terms of an arrangement evidenced in writing. Although this means that the Security Collateral Provider cannot be free to deal with the Collateral in the ordinary course of its business, the fact that the Security Collateral Provider has one or more (or all) of the following rights does *not* of itself mean that the Secured Party or relevant third party does not have possession or control or that the Security Collateral Provider is free to deal with the financial property in the ordinary course of business:

(a) right to receive and withdraw income in relation to the financial property;

(b) right to receive notices in relation to the financial property;

(c) right to vote in relation to the financial property;

(d) right to substitute other financial property that the parties agree is of equivalent value for the financial property;

(e) right to withdraw excess financial property;

(f) right to determine value of financial property.

The enforceability of any contractual obligations on a Secured Party to return equivalent Collateral to the Security Collateral Provider is a matter of New York law, being the governing law of the 1994 NY Annex and the VM NY Annex.

11 Substitution of Collateral[74]

What is the effect, if any, under the laws of Australia on the validity, continuity, perfection or priority of a security interest in Eligible Collateral under each Security Document of the right of the Pledgor to substitute Collateral pursuant to Paragraph 4(d) (or in the case of the IM Deed, Paragraph 4(e)) of each Annex and Deed? How does the presence or absence of consent to substitution by the Secured Party affect your response to this question? Please comment specifically on whether the Pledgor and the Secured Party are able validly to agree in the Security Document that the Pledgor may substitute Collateral without specific consent of the Secured Party and whether and, if so, how this may affect the nature of the security interest or otherwise affect your conclusions regarding the validity or enforceability of the security interest. Note that the parties may also give upfront consent in the IM Security Documents to any substitution made by the Security Collateral Provider and/or the

[74] We note that question 11 refers to Pledgor as reflected below. However, as the Deeds use the term "Chargor", we have drafted our response with reference to Security Collateral Provider, which encompasses both terms.

the Custodian in accordance with the terms of the agreement described in assumption (n) in Part B, Section I, of Schedule 1 of this memorandum.

The right of substitution granted to the Security Collateral Provider should not, of itself, affect the validity, continuity, perfection or priority of a security interest in Eligible Collateral, provided the transfer is not void or voidable (in respect of which, please see paragraph B.18 and Schedule 3 below). In particular, the Security Collateral Provider and the Secured Party are able validly to agree in the Security Document that the Security Collateral Provider may substitute Collateral without specific consent of the Secured Party. The PPSA contains provisions which will release a security interest over personal property which is disposed of with the consent of the Secured Party.

However, if the Australian Company which is the grantor of the security interest is subject to insolvency proceedings then, to the extent that the right of substitution causes the security interest to be characterised as a security interest over a "circulating asset" under the PPSA, it will rank behind *Corporations Act* preferred creditor claims (for example, employee entitlements, auditor's fees and administrator's indemnity for costs) and may be void as against a liquidator in certain circumstances (see paragraph B.18 and Schedule 3 below). There are two tests under the PPSA for whether an asset is, or is not, a circulating asset (which means that the security interest over the asset will also be circulating). For certain assets (such as certain accounts and negotiable interests), the secured party must control the asset and register that it has control. For all other assets, the secured party must not have given the grantor express or implied authority to dispose of the assets.

Once the substituted Collateral is transferred to the Secured Party and is subject to the security interest in favour of the Secured Party in accordance with the Security Document, the validity, continuity, perfection or priority will be determined in the manner considered above.

As noted in paragraph B.5.1 above, a condition to protection under the *Netting Act* requires that the Collateral must be, before enforcement, transferred or otherwise dealt with so as to be in the possession or under the control of the Secured Party, or another person (who is not the Security Collateral Provider) on behalf of the Secured Party under the terms of an arrangement evidenced in writing. In that regard, the *Netting Act* explicitly provides that the fact that the Security Collateral Provider has the right to substitute other Collateral that the parties agree is of equivalent value for the Collateral does not itself stop the Secured Party from satisfying that condition.

II. Enforcement of rights under the Security Documents by the Secured Party in the absence of an insolvency proceeding

We set out below our analysis of the issues raised under the heading "Enforcement of rights under the Security Documents by the Secured Party in the absence of insolvency proceedings" in Part 1 of the Instruction Letter.[75] The different types of insolvency proceedings to which an Australian Company may be subject under Australian Law are described in Part I of our Netting Opinion and, as noted in Part C of our Netting Opinion, each of these insolvency proceedings falls within the definition of *external administration* for the purposes of the *Netting Act.* We assume in this Part B.II that neither the Collateral Provider nor the Secured Party is subject to such insolvency proceedings and, accordingly, that the *Netting Act* does not apply to the enforcement of security under the Security Documents.

[75] We assume in this memorandum that the proceeds of any enforcement by a Secured Party of a security interest in Collateral created by a Security Collateral Provider under a Security Document are applied to discharge obligations that are secured by the security.

12 Formalities in exercising enforcement rights

Please note that the assumption in (l) in Part B, Section II, of Schedule 1 of this memorandum applies to questions 12 to 15.

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

The specific PPSA 'governing law' provisions with respect to the validity and perfection of a security interest do not extend to enforcement issues.[76] For the reasons set out in paragraph B.1(b) above, in our opinion the better view is that, in the absence of any other legislation determining the law governing the enforcement of a security interest, the general Australian Law will determine the governing law.

If Australian Law governs the enforcement of a security interest and the PPSA applies, then the PPSA sets out a series of rules on the enforcement of security interests in personal property. These rules regulate how a secured party seizes, disposes of and retains collateral and procedural requirements and duties that the secured party may need to comply with if it exercises those rights under the PPSA. Some, but not all of these, can be contracted out of.[77] However, the rights, powers and remedies of a secured party under the enforcement provisions in the PPSA are in addition to, and do not replace, those under the Security Document and the general law. In our view, if a Secured Party exercises enforcement rights under a Security Document that are identical to the rights it is entitled to exercise under the PPSA and which the parties have not contracted out of, there is only a low risk that the Secured Party would have to comply with the PPSA procedural requirements and duties.[78] Also, with limited exceptions the enforcement provisions do not apply to a security interest over an investment instrument or intermediated security which is perfected by possession or control and do not apply to security granted by an Australian Company which is subject to a receiver, receiver and manager or a controller.[79] The most significant of the enforcement provisions is that which requires that personal property or proceeds of collateral received by or on behalf of a secured party as a result of enforcing a security interest in collateral

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76 As noted in paragraph B.1 above, the PPSA contains provisions which set out which law, in proceedings in an Australian court, governs the validity, perfection and effect of perfection or non-perfection of security interests to which the PPSA applies.

77 Those which cannot be contracted out of include: that rights, duties and obligations must be exercised honestly and in a commercially reasonable manner, the duty to exercise all reasonable care to obtain at least the market value for collateral and the order of application of money received on enforcement.

78 The reasons for this include that, traditionally, in the context of considering the enforcement of securities, enforcement under a security agreement has been distinguished from enforcement under rights conferred by the *Conveyancing Act 1919* of New South Wales (and its equivalent in other jurisdictions). By parity of reasoning, a similar conclusion should be reached in the context of the PPSA enforcement provisions. Also, there is no provision in the PPSA deeming that if a secured party exercises rights that are available under both the enforcement provision and the general law or contract it is deemed to be exercising the former.

79 A controller is defined under the *Corporations Act* to mean a receiver, receiver and manager or anyone else who is in possession, or has control, of a corporation's property for the purpose of enforcing a charge.

must be applied in the following order whether the security interest was enforced under the PPSA or otherwise:

- higher ranking interests (other than security interests)
- reasonable enforcement expenses
- higher ranking security interests
- secured party
- lower ranking security interests
- grantor.

This provision may not be contracted out of and it does apply to a secured party who has perfected an investment instrument or intermediated security by taking possession or control. This means that a secured party cannot avoid this provision by taking possession or control.

The PPSA procedural requirements and duties that apply in respect of the enforcement of a security interest are not considered further in this memorandum.

Under the general Australian Law, it is not necessary for any particular formalities to be followed in order to exercise the rights contemplated by each Security Document, including the right to "liquidate" the Collateral by selling it. Accordingly, the Secured Party may, on enforcement of the Security Document, sell the Collateral. In particular, a court order or auction is not required and notice of sale need not be given to the Security Collateral Provider, although in practice secured creditors do often give a short period of notice before selling Collateral. This does not differ depending on the type of Collateral involved.

In exercising its power of sale under the Security Document, the majority of Australian cases suggest that a Secured Party has a duty to act in good faith and not to wilfully or recklessly sacrifice the interests of the Security Collateral Provider. However, in considering the Secured Party's duty at equity, judicial statements have been made to the effect that an absence of good faith may be evidenced where the mortgagee:

(a) has acted "without taking reasonable steps to obtain a proper price";[80] and

(b) has acted without "a genuine primary desire to obtain for the mortgaged property the best price obtainable consistently with the right of the mortgagee to realise his security".[81]

This duty is owed not only to the Security Collateral Provider, but also to the Security Collateral Provider's guarantors and subsequent security providers. On the other hand, a security holder is not required to delay the realisation of security in the expectation that a higher price may be obtained in the future. Generally, and subject to the principles just quoted, a security holder is free to determine when to exercise a power of sale.[82]

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80 Mason J in *Forsyth v Blundell* (1973) 129 CLR 477.

81 Jacobs J in *ANZ Banking Group v Bangadilly Pastoral* (1978) 52 ALJR 529.

82 *China & South Sea Bank Ltd. v Tan Soon Gin* [1990] 1 AC 536; *Tse Kwong Lam v Wong Chit Sen* [1983] 1 WLR 1349.

A controller of a company also owes a statutory duty under section 420A of the *Corporations Act*. In exercising a power of sale, a controller has a duty to take all reasonable care to sell the property for its market value (if, when sold, it has a market value) or otherwise the best price that is reasonably obtainable, having regard to the circumstances existing when the property is sold. This duty is a duty owed to the company. The controller may also owe duties to others under the general law. It is also possible for a person other than the company to take action to restrain the sale by applying for an injunction under section 1324 of the *Corporations Act* for a breach of section 420A. Section 1324 entitles a person whose interest would be affected by a contravention of the *Corporations Act* to apply for an injunction to prevent the contravention.

While there is no prohibition on the Secured Party appropriating the Collateral to itself and applying the value of the Collateral to meeting the Security Collateral Provider's obligations, it may have a harder time discharging the burden of proof that it complied with its equitable and statutory duties for the Collateral than it would have had selling the securities to a third party. However, it will, of course, be somewhat easier to establish that it acted reasonably and fairly in the circumstances, in relation to Collateral in the form of liquid securities, where a market price at the time of the Secured Party's appropriation of the Collateral can be objectively established.[83]

13 Formalities where Australian Law is not the law governing the validity and perfection

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

If the laws of another jurisdiction govern the enforcement of the security interest (as to which, please see our response to question paragraph B.12 above), there are no other formalities, notifications or other procedures that the Secured Party must observe or undertake in Australia in exercising its rights as a Secured Party under each Security Document.

14 Special limitations on enforcement

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

In relation to entities of the kind covered by this memorandum, there are no rules or regulations of the kind mentioned in paragraphs (a), (b) or (c) of this question, although certain restrictions may apply in relation to other types of entities (such as the Crown and statutory corporations referred to in paragraph A.2(c) above read with Appendix B), particularly in relation to their power to enter into particular transactions and the assets of those entities available to satisfy particular kinds of obligations. Except as noted in paragraph B.12 above, the types of Eligible Collateral involved should not have any effect on enforcement rights considered in paragraph B.12.

83 Also, if the PPSA enforcement provisions apply, the purchase must be by public sale and the secured party must pay market value.

In certain circumstances certain claims may rank in priority (either in whole or in part) to a security interest including, without limitation:

(a) claims for the costs of administration and realisation;

(b) certain claims mandatorily preferred by law; and

(c) certain claims arising by operation of law or specifically charged by statute (including, without limitation, local government rates and land tax),

but in this regard the position of the Secured Party is no different from any person taking similar security interests under Australian Law. Subject to such claims and the comments in paragraph B.21 below, there are no general "statutory liens" or preferred claims in relation to a security interest over Eligible Collateral of the kind under review.

15 Secured Party in default

How would your responses to questions 12 to 14 above change, if at all, assuming that an Event of Default, exists with respect to the Secured Party rather than or in addition to the Security Collateral Provider (for example, would this affect this ability of the Secured Party to exercise its enforcement rights with respect to the Collateral)?

If an Event of Default is subsisting in relation to the Secured Party rather than the Security Collateral Provider, our responses to questions 12 to 14 above would not change.

However, under the terms of the Security Documents, the Secured Party is only permitted to exercise its enforcement rights if, relevantly, there is an Event of Default subsisting in relation to the Security Collateral Provider or any Early Termination Date has been designated (or deemed to occur) as the result of an Event of Default in relation to the Security Collateral Provider. In any other case, the Secured Party may not enforce its security.

III. Enforcement of rights under the Security Documents by the Secured Party after commencement of an insolvency proceeding

We set out below our analysis of the issues raised under the heading "Enforcement of rights under the Security Documents by the Secured Party after commencement of an insolvency proceeding" in Part 1 of the Instruction Letter.

The different types of insolvency proceedings to which an Australian Company may be subject under Australian Law are described in Part I of our Netting Opinion. As noted in Part C of our Netting Opinion, each of these insolvency proceedings falls within the definition of *external administration* for the purposes of the *Netting Act.* We assume in this Part B.III that the Collateral Provider is subject to such insolvency proceedings and that the *Netting Act* does apply to the enforcement of security under the Security Documents. We note that the relevant protection given to enforcement of security applies only to the extent that the enforcement is carried out in a manner that complies with section 420A of the *Corporations Act* (if it applies) and any applicable general law duties that are not inconsistent with the terms of the security. In that regard, please see paragraphs A.6.9 and B.12 above.

This analysis also proceeds on the assumption that the Security Collateral Provider's assets are located in Australia. If any of its assets are located outside Australia, then the analysis will need to be supplemented by advice on the cross border insolvency regime that operates in the country in

which the assets are located (ie there might be similar types of proceedings in that other country to the proceedings which can apply in Australia which are referred to in Part C of our Netting Opinion).

16 Competing claims

Note that the assumption in (m) in Part B, Section III, of Schedule 1 to this memorandum applies to questions 16 to 18 below.

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

As discussed in paragraph A.6, where specified safeguards are met, the protection under the *Netting Act* of the enforcement of security (including the protection against the enforcement being void or voidable) applies despite:

(a) the creation of any encumbrance, or any other interest, in relation to the financial property secured; or

(b) the operation of any encumbrance, or any other interest, in relation to that financial property,

in contravention of a prohibition in the contract or in the protected security.[84]

These protections apply despite any other law (including the "specified provisions"), but subject to applicable "specified stay provisions". The effect of this is considered further in our responses set out in paragraph B.17 below. The protections apply to the enforcement of security over financial property, in respect of obligations of a party to a close-out netting contract, only to the extent that certain safeguards are satisfied. These are considered in paragraph A.6 above.

Where the enforcement of security under a Security Document is not protected under the *Netting Act*,[85] there are priority rules under the PPSA and the *Corporations Act* which apply to determine:

(i) the priority between competing security interests attached to the same collateral;

(ii) in some cases, the priority between a security interest and another interest (such as that of a purchaser); and

(iii) the priority of transitional securities.

Please see Schedule 2 for a more detailed description of these provisions.

17 Stay on rights

Would the Secured Party's rights under each Security Document, such as the right to liquidate the Collateral, be subject to any stay or freeze or otherwise be affected by commencement of the

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84 Section 14(2)(h) of the *Netting Act*. The amendment to section 14(2)(h) of the *Netting Act* made by the *Collateral Protection Act* do not apply to disposals of rights or property, or the creation or operation of encumbrances or interests, before 1 June 2016 (*Collateral Protection Act*, Part 3).

85 Please see our comments in paragraph A.4.

insolvency (that is, how does the institution of an insolvency proceeding change your responses to questions 12 and 13 above, if at all)?[86]

Stay during administration

The effect of section 440B of the *Corporations Act* is that during the administration of an Australian Company, a security interest over the Australian Company's property cannot be enforced[87] except with the leave of the court or the administrator's written consent. A secured creditor holding security over substantially all of the assets of the Australian Company can effectively block the appointment of an administrator (this is because such a secured creditor has a 13 business day period after the appointment of an administrator to decide whether to enforce the security interest), but this would not apply in the case of the Security Documents (assuming that the Eligible Collateral provided by the Security Collateral Provider does not comprise substantially all its assets).

However, to the extent that the *Netting Act* protects the enforcement of the security under a Security Document, the protection applies despite any other law (including the specified provisions), but subject to applicable specified stay provisions. The specified provisions include the moratorium on the enforcement of security during the administration of an Australian Company under section 440B of the *Corporations Act* (and this is not a specified stay provision). Accordingly, the moratorium on enforcement during the administration of an Australian Company would not restrict the Secured Party enforcing security to the extent that the *Netting Act* protects that enforcement.

Specified stay provisions

The *Collateral Protection Act* amended a number of stays which already existed in other Australian Acts to restrict the enforcement of security under a contract and set out a new framework in the *Netting Act* for the way in which these stays would cease to apply to close-out netting contracts and the security given over financial property in respect of close-out netting contracts. These stays, and the new framework, are considered in Part J of our Netting Opinion. The analysis in paragraphs 3.1 and 3.2 of Part J in respect of the circumstances in which non direction stays (as defined in the Netting Opinion) may cease in relation to a close-out netting contract applies in relation to a security given over financial property, in respect of an obligation of a party to a close-out netting contract to which a regulated body (as defined in the *Netting Act*) is a party,[88] in a substantially similar manner to the way in which it is described to apply in relation to a close-out netting contract.

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86 For example, under the US Bankruptcy Code certain creditors are subject to an automatic stay, which limits a creditor's ability to take actions to enforce or collect upon a claim (subject to certain exceptions).

87 "Enforce" is defined broadly by the *Corporations Act* to include, among other things, the exercise in relation to property of a right, power or remedy existing because of the security interest that arises (a) under an agreement or instrument relating to the security interest; (b) under an agreement or instrument relating to a transaction or dealing giving rise to the security interest (in the case of a PPSA security interest); (c) under a written or unwritten law; or (d) in any other way. Therefore, a secured party cannot resort to self-help measures that fall within the definition of "enforce" without the administrator's consent or leave of the court. This prohibition means that, amongst other restrictions, a Secured Party may not "liquidate" Collateral which is under its control at the time administration commences. This prohibition does not, however, prevent a person from giving a notice under the provisions of an agreement or instrument under which a security interest is created or arises.

88 Section 15A(2) of the *Netting Act* provides that section 15A of the *Netting Act* (which sets out the circumstances in which a non-direction stay may cease) "applies in relation to a security given over financial property, in respect of an obligation of a party to a close-out netting contract to which a regulated body is a party, if (a) the obligation is an eligible obligation in relation to the contract, or an obligation of a prescribed kind; and (b) a specified stay provision (other than a direction stay provision) applies to a trigger event that happens in relation to the contract". For these purposes, in paragraph 3.1(a) of Part J of our Netting Opinion, the reference to "an obligation under the contract of a party to the contract" should be a reference to "the obligation".

The analysis in that Part J applies equally to our response to this question as if the references to closing out *transactions* under a *close-out netting contract* or to whether a party may or may not close out *transactions* under a *close-out netting contract* to which a regulated body (as defined in the *Netting Act*) is a party in Part J of our Netting Opinion were to enforcing security given over financial property, in respect of an obligation of a party to a *close-out netting contract* or to whether the party may or may not enforce security under a security given over financial property in respect of an obligation of a party to a close-out netting contract (as applicable).

18 Clawback

Will the Security Collateral Provider (or its administrator, provisional liquidator, conservator, receiver, trustee, custodian or other similar official) be able to recover any transfers of Collateral made to the Secured Party during a certain "suspect period" preceding the date of the insolvency as a result of such a transfer constituting a "preference" (however called and whether or not fraudulent) in favour of the Secured Party or on any other basis? If so, how long before the insolvency does this suspect period begin? If such a period exists, would the substitution of Collateral by a counterparty during this period invalidate an otherwise valid security interest if the substitute Collateral is of no greater value than the assets it is replacing? Would the posting of additional Collateral pursuant to the mark-to-market provisions (or the IM calculation provisions in the case of the IM Security Documents) of the Security Documents during the suspect period be subject to avoidance, either because the Collateral was considered to relate to an antecedent or pre-existing obligation or for some other reason?

Under Australian insolvency laws, transactions may be void, voidable or vest in the grantor in certain circumstances, which are considered in Schedule 3 to this memorandum. In addition, please note the application of the circumstances affecting the *Netting Act* protection as described in paragraph A.6.8.

However, to the extent that the *Netting Act* protects the enforcement of the security under a Security Document, the protection of enforcement applies despite any other law (including the specified provisions), but subject to applicable specified stay provisions. The specified provisions are defined in the *Netting Act* to include many of the Australian insolvency laws referred to above. Further, even where such laws are not specified provisions, the *Netting Act* protection applies 'despite any other law'. Consequently, the *Netting Act* protection applicable to enforcement of security applies despite those Australian insolvency laws.

In addition, the enforcement of security which is protected under the *Netting Act* is not to be void or voidable in the *external administration*, subject to the application of either of the two limitations set out in paragraph A.6.8 above.

IV. Miscellaneous

We set out below our analysis of the issues raised under the heading "Miscellaneous" in Part 1 of the Instruction Letter.

19 Governing law of Security Document

Would the parties' agreement on the governing law of each Security Document and submission to jurisdiction be upheld in Australia, and what would be the consequences if it were not?

The IM NY Annex forms part of and is subject to the ISDA Master Agreement. Where the relevant ISDA Master Agreement is governed by English law, but the parties will provide in paragraph 13 of

the IM NY Annex that the Annex is governed by and construed in accordance with New York law, the governing law of the ISDA Master Agreement will accordingly be split (i.e., dépeçage) – English law will govern the pre-printed ISDA Master Agreement, the Schedule and the Transactions but New York law will govern the IM NY Annex. The English jurisdiction provision of the ISDA Master Agreement would apply to the entire agreement including the IM NY Annex. Would the split governing law affect your answer above?

The IM Deed may be entered into in connection with either an English law ISDA Master Agreement or a New York law governed ISDA Master Agreement but as it as a separate agreement and does not form part of the relevant ISDA Master Agreement we assume that the differences in governing law between the relevant ISDA Master Agreement and the IM Deed will not affect your answer above.

In any proceedings properly commenced by the Secured Party against the Security Collateral Provider in an Australian Court claiming enforcement of a Security Document governed by a law other than Australian Law, the choice of that other law as the law by which the relevant Security Document is to be governed would be upheld as a valid choice of law and would be applied by the Australian Court, provided that:

(a) the choice of law had been made in good faith and was not intended to evade the provisions of another legal system with which the Security Document had a closer connection; and

(b) none of the terms of the relevant Security Document or any provision of that law applicable to the Security Document is contrary to Australian public policy (we consider that it is very unlikely that an Australian Court would reach such a conclusion where the governing law is English or New York law).

We express no opinion as to whether a court will give effect to a choice of laws to govern the Security Document to the extent that the choice of laws applies to non-contractual obligations arising out of, or in connection with, the Security Document (including, without limitation, non-contractual obligations within the meaning of Regulation No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (known as "Rome II")).

If the parties' agreement on the governing law and their submission to jurisdiction were not upheld, the relevant Security Document would have to be examined by an Australian Court on the basis of Australian Law.

These types of proceedings are unusual and it is difficult to be precise about rules a court will adopt because much depends on the facts and the court has a wide discretion.

IM Security Documents

We assume that the matters referred to in paragraphs (a) and (b) of our response immediately above apply in respect of the IM Security Documents.

In respect of the IM Deed, on the basis of our understanding that the IM Deed does not form a part of the relevant Master Agreement, we confirm that the differences in governing law between the Master Agreement and the IM Deed will not affect our answer immediately above.

In respect of the IM NY Annex entered into in connection with an English law governed Master Agreement, we assume that, as a matter of English law:

(i) the IM NY Annex forms part of and is subject to the Agreement (as defined in the Master Agreement); and

(ii) in respect of the construction of the IM NY Annex for the purpose of interpretation, regard would be had to the laws of New York.

On this basis, we expect that in respect of the construction of the IM NY Annex for the purpose of interpretation, an Australian Court should have regard to the laws of New York or the purpose of interpretation of the IM NY Annex.

20 Other issues

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

Please see paragraph B.16 above and Schedule 2 below with respect to the relevance of the priority rules in the *Corporations Act* to the priority of transitional securities in circumstances where the *Netting Act* protection does not apply.

Custodial arrangements

Where, under the custodial arrangements, the Custodian, Euroclear or Clearstream holds its interest in the Collateral as trustee, we note the following:

(a) as a general matter, a trustee has a right to be indemnified out of, and an equitable lien over, trust assets in respect of debts and liabilities properly incurred by it as trustee, and those rights normally have priority over, and must be satisfied and discharged prior to, the claims of the beneficiary;

(b) our conclusions above do not mean that a Collateral Taker can never suffer loss or fail to recover the Collateral. Without limitation, such a loss arising as a result of fraud or breach of trust on the part of the Custodian, Euroclear or Clearstream.

21 Other circumstances that might affect enforcement

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

General comments applicable to all Australian Companies

Other factors which might affect the Secured Party's ability to enforce its security in Australia include the provisions of the *Corporations Act* dealing with transactions with related parties, the presence of fiduciary duties, whether or not the Security Documents have been entered into for bona fide commercial reasons and on arms-length terms, the discretions of an Australian Court with respect to the availability of equitable remedies (including, without limitation, injunction and specific performance) and the effect of other rules of law and equity. Also, the rights of a party to enforce a document may be limited or affected by its own breaches or misrepresentations and its own unlawful conduct (for example, if it did not hold authorisations which it is required to hold in order to conduct its business). In addition, claims of certain creditors are mandatorily preferred by law.

ADIs and insurers

Specific priority regimes apply to the assets of ADIs, life insurance companies and general insurers under sections 13A(3) of the *Banking Act*, section 86 of the *Reserve Bank Act*, section 116(3) of the *Insurance Act 1973* (Cth) ("***Insurance Act***") and section 187 of the *Life Insurance Act 1995* (Cth) ("***Life Insurance Act***"). These are considered further in Schedule 4 to this memorandum.

However, as noted above, to the extent that the *Netting Act* protects the enforcement of the security under a Security Document, it applies despite any other law (including the specified provisions), but subject to applicable specified stay provisions. Some of the sections referred to above are included in the amended definition of 'specified provisions'. However, even where such sections are not specified provisions, the *Netting Act* protection applies 'despite any other law'. Consequently, the *Netting Act* protection applies despite those Australian insolvency laws.

Also, as noted above in our answer to paragraph B.17 above, the *Netting Act* protection of enforcement of security applies subject to the specified stay provisions, which are particularly relevant to ADIs, general insurers and life insurance companies.

Superannuation trustees and life companies

Superannuation trustees and life companies are restricted by the *Superannuation Industry (Supervision) Regulations 1994* (Cth) and the *Life Insurance Act* from granting charges over regulated superannuation funds or approved deposit funds, or its statutory funds (respectively). Those restrictions are subject to limited exceptions, which were amended by the *Collateral Protection Regulation*. The Explanatory Statement to the *Collateral Protection Regulation* states the following:

> The [*Collateral Protection Regulation*] will:
>
> a) enable trustees of superannuation funds and approved deposit funds (Superannuation Funds) regulated under the SIS Act and life companies regulated under the Life Insurance Act to provide margin by way of security in relation to derivatives in the manner required to access international capital markets and liquidity; and
>
> b) update the list of approved bodies (being domestic and foreign exchanges and clearing houses) to whom trustees of Superannuation Funds and life companies may grant security.
>
> This is intended to allow those entities to access liquid global markets such as the United States cleared over-the-counter (OTC) derivatives market through Futures Commission Merchants (FCMs).

The amended exceptions apply only where certain requirements that are set out in them are satisfied, consideration of which is beyond the scope of this memorandum on enforceability of valid security arrangements. However, by way of summary, we note that these conditions include that the security is required by applicable law, or the rules of an "approved body" (which are markets and clearing houses listed in the regulations). There is also a further extension to allow charges to be given to secure obligations under derivative contracts over "financial property" which links to the changes made in the reform package to address global derivative margining requirements.

Accordingly, the Security Documents should not be used when the Security Collateral Provider is a superannuation trustee or life company unless legal advice is obtained that the type of security interest proposed is permissible under the applicable Australian statutes.

22 Collateral held with a Custodian under an IM Security Document

For the IM Security Documents only, assume that the Collateral will be held in a Custodial Account with a Custodian as described in assumption (n) and not pursuant to the assumptions in (i)(i) to (iv) and (j) or the assumption (o) in Part B of Schedule 1 of this memorandum.

(i) Would any of your responses to questions 1 through 21 above with respect to Collateral held pursuant the custodial arrangement described in assumption (n) be different than the responses to such questions as a result of the holding of the Collateral pursuant to one of the custodial arrangements described in (n)? If so, please comment specifically on any such changes.

In our view, the conclusions in our responses to questions 1 through 21 above relating to the IM Security Documents are not materially adversely affected if the Collateral is held in a Custodial Account with a Custodian as described in assumption (n).

(ii) Please describe any requirements that the custodial arrangements described in assumption (n) must meet to permit the Collateral Taker to exercise its rights as secured party.

As noted paragraph A.6.7 above, the protection provided by the amended *Netting Act* to the enforcement of security applies only if, relevantly, before the enforcement, the financial property is transferred or otherwise dealt with so as to be in the possession or under the control of another person (who is not the grantor) on behalf of the secured person, under the terms of an arrangement evidenced in writing. It is therefore important that that the custodial arrangement is evidenced in writing, and that the other related requirements in the *Netting Act* (including in respect of possession or control) are satisfied. Please paragraph B.5.1 regarding possession and control for the purposes of the *Netting Act*.

With respect to the PPSA, as noted in paragraph A.5.2 above, if securities and cash collateral are recorded in the same securities account, and the custodian holds an Australian financial services licence or a licence under a foreign jurisdiction permitting them to maintain securities accounts, then the relevant PPSA collateral class should be intermediated securities. We refer, without limitation, to paragraphs B.5.2 to B.5.4 regarding the requirements of attachment and perfection under the PPSA.

23 Collateral held with Euroclear or Clearstream

Assume that the Collateral will be held by Euroclear or Clearstream, as contemplated by assumption (o) and not pursuant to assumptions (I)(i)-(iv) and (j) or assumption (n) in Part B of Schedule 1 of this memorandum.

(i) Would any of your responses to questions 1 through 9 and 12 through 21 above with respect to Collateral held pursuant the arrangement described in assumption (o) be different than the responses to such questions as a result of the holding of the Collateral pursuant to one of the arrangements described in (o)? If so, please comment specifically on any such changes. As noted in assumption (o), you may assume that the securities documents and other agreements referred to in assumption (o) are enforceable in accordance with their terms under applicable law (which may be different than the law of your jurisdiction).

Subject to the following, our responses to questions 1 through 9 and 12 through 21 apply as if references to:

(i) the IM Security Document were to the Euroclear Security Agreement or Clearstream Security Agreement (as applicable);

(ii) "English or New York law" were to "Luxembourg or Belgian law".

We assume that the effect of the arrangements described in assumption (o) is that the Collateral Provider grants to the Collateral Taker a first priority continuing security interest in all Collateral in the "Pledged Securities Account" or "Pledged Cash Account" (in the case of Euroclear) or the "Collateral Account" (in the case of Clearstream), as referred to in assumption (o).

In accordance with assumption (o) we also assume that the Collateral is held in the relevant account:

(a) in the case of Clearstream, in the name of the Collateral Provider;

(b) in the case of Euroclear, in the name of Euroclear acting in its own name but for the account of the Collateral Taker.

In the case of Clearstream, on the basis of our assumption that Collateral comprised of cash and securities is held in the same securities account, the relevant PPSA collateral class should be intermediated security.

In the case of Euroclear, on the basis that cash Collateral will not be held in the securities account, we expect that the relevant PPSA collateral classes will be intermediated security and account.

Please also see our response to question (ii) immediately below.

(ii) *Please describe any requirements that the arrangements described in assumption (o) must meet to permit the Collateral Taker to exercise its rights as secured party*

Our comments in our response to question (ii) of paragraph 22 above apply equally to the arrangements described in assumption (o).

As noted in paragraph B.5.1 above in respect of the protection provided by the amended *Netting Act* to the enforcement of security, section 14A(4) provides that financial property is taken to be in the possession of a person if, in a case where the financial property is intermediated financial property, the person is the person in whose name the intermediary maintains the account. We note that in the case of Clearstream, the account in which the Collateral is held is in the name of the Collateral Provider. Please paragraph B.5.1 regarding possession and control for the purposes of the *Netting Act*.

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

Our responses to questions (i) and (ii) above apply as if references to the Euroclear Documents were to the Euroclear Documents as amended by the Euroclear Japanese Amendments.

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

Our responses to questions (i) and (ii) above apply as if references to the Clearstream Documents were to the Clearstream Documents as amended by the Clearstream Japanese Amendments.[89]

We assume that the Collateral is held in the relevant account in the case of Clearstream, in the name of the Collateral Taker. On this basis, the final paragraph of our response to question (ii) above is not relevant in respect of the Clearstream Japanese Amendments.

24 IM NY Annex Japanese Amendments

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

Subject to the following, our responses to questions 1 through 21 apply as if references to the IM Security Document and the IM NY Annex were to the IM NY Annex, as amended by the IM NY Annex Japanese Amendments.

We assume that the effect of the IM NY Annex, as amended by the IM NY Annex Japanese Amendments and the custodial arrangements, is that Collateral is held in an account of the Custodian in the name of the Collateral Taker.

25 VM NY Annex IA Amendments

Please assume that the VM NY Annex is amended by the VM NY Annex IA Amendments. Would any of your responses to questions 1 through 21 be different as a result of the inclusion of the VM NY Annex, as amended by the VM NY Annex IA Amendments, in this opinion? If so, please comment specifically on any such changes.

Subject to the following, responses to questions 1 through 21 apply as if references to the Security Documents and the VM NY Annex were to the VM NY Annex, as amended by the VM NY Annex IA Amendments.

26 IM Deed Japanese Amendments

Notwithstanding assumptions (g) and (n) in Part B, in Schedule 1 of this memorandum, please assume that the IM Deed is amended by the IM Deed Japanese Amendments. Would any of your responses to questions 1 through 21 below with respect to Collateral held pursuant to the custodial

[89] We have assumed that the Recommended Amendment Provisions for the ISDA 2017 Clearstream Security Agreement with respect to Japanese Collateral (as referred to in the Clearstream Japanese Amendments) do not adversely affect our conclusions.

arrangement described in the IM Deed Japanese Amendments be different than the responses to such questions as a result of (a) the inclusion of the IM Deed, as amended by the IM Deed Japanese Amendments, in this opinion or (b) the holding of the Collateral pursuant to one of the custodian arrangements described in the IM Deed Japanese Amendments? If so, please comment specifically on any such changed.

Our response to question 24 above applies as if references to the IM NY Annex and the IM NY Annex Japanese Amendments were to the IM Deed and IM Deed Japanese Amendments, respectively.

PART C: TITLE TRANSFER APPROACH PURSUANT TO THE TRANSFER ANNEX

We set out below our analysis of the issues raised in Part 2 of the Instruction Letter. This analysis proceeds on the assumption that, immediately before and after a transfer, the Eligible Credit Support is located in Australia. If, at either of those points in time, the Eligible Credit Support is not located in Australia, then the analysis will need to be supplemented by advice on the cross border issues that operate in the country in which the assets are located.

1 Nature of transfers

Would the laws of Australia characterise each transfer of Eligible Credit Support as effecting an unconditional transfer of ownership in the assets transferred? Is there any risk that any such transfer would be re-characterised as creating a security interest? If so, is there any way to minimise such risk? What would be the specific consequences of such a re-characterisation (referring back to issues related to perfection, priority and formal requirements for establishing both as discussed with regard to the Security Documents in Part I above)?

General law

In our opinion, the transfers of Eligible Credit Support contemplated by the Transfer Annex would be characterised for the purposes of the general law of Australia as unconditional transfers of title to the Eligible Credit Support, for the reasons described in Schedule 5 of this memorandum. In our opinion, there is no material risk that any such transfer would be re-characterised by the Australian Courts as being in substance a secured loan unless the intention of the parties (evidenced in writing or by conduct) was that the transfers of Eligible Credit Support would take effect other than by way of unconditional transfers of title. There is nothing on the face of the Transfer Annex to indicate that this is the case, so in the absence of any other agreement or conduct to the contrary, transfers of Eligible Credit Support under the Transfer Annex should not be re-characterised in this way.[90]

PPSA

(a) Close-out netting contracts exclusion

As noted in paragraph A.4 above and subject to the assumptions and qualifications in our Netting Opinion, we consider that both the 1992 ISDA Master Agreement and the 2002 ISDA Master Agreement are close-out netting contracts for the purposes of the *Netting Act*, provided that, in the case of the 1992 ISDA Master Agreement, "Second Method" is chosen.

Were it not for applicable exclusion for close-out netting contracts from the PPSA, the breadth of the definition of security interest could encompass the rights and interests under the Transfer Annex.

However, the PPSA does not apply to:

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90 The decision in *Beconwood Securities Pty Ltd v Australia and New Zealand Banking Group Limited* [2008] FCA 594 ("***Beconwood***"), which confirmed the validity of the absolute transfer provisions in security lending documents, supports this conclusion. The conclusions drawn in *Beconwood* regarding the validity of the absolute transfer provisions in security lending documents were cited with approval in *ABN AMRO Clearing Sydney Ltd (formerly known as Fortis Clearing Sydney Pty Ltd) v Primebroker Securities Ltd* (receivers and managers appointed)(in liquidation) [2012] VSCA 287.

"any right or interest held by a person, or any interest provided for by any transaction, under any of the following (as defined in section 5 of the *Netting Act)*:

(i) an approved netting arrangement;

(ii) a close-out netting contract;

(iii) a market netting contract;"

The close-out netting contracts exclusion is not limited only to the right to close-out and net obligations. However, in our view, the close-out netting contracts exclusion does not exclude every interest which happens to be created under either the terms of a close-out netting contract or a transaction under that close-out netting contract. Such an interpretation would, for example, exclude from the operation of the PPSA interests created under a charge if the terms of that charge were included within the body of a close-out netting contract. Rather, we consider that the close-out netting contract exclusion excludes from the operation of the PPSA:

- rights and interests which are created, and held, solely under and as an elemental part of a close-out netting contract; and
- interests created by transactions under a close-out netting contract ***if*** those transactions (and therefore those interests) are subject to the close-out netting process contained in that close-out netting contract.

Another way of describing this is that a provision within the body of a close-out netting contract which creates a security interest in relation to personal property which is "outside" of the close-out netting contract and which survives close-out netting should fall outside of the close-out netting contract exclusion, and thus is capable of being a security interest for the purposes of the PPSA.[91]

We consider that this interpretation is consistent with the wording and purpose of the close-out netting contract exclusion whilst also avoiding an operation of the provision which could frustrate the operation of the PPSA.

It is also important to note that it is possible for particular transactions to themselves give rise to a security interest under the PPSA. An example of this is if a transaction gave rise to a deemed security interest such as the absolute transfer of an account (we mentioned this deemed security interests in paragraph A.5.1 above).

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91 For example, the security interest under each Security Document survives the close-out netting under the *Master Agreement*. If there is a default by a party then the other party can take enforcement action against the property which has been secured in its favour. Such action does not affect the close-out netting under the *Master Agreement*, instead the close-out netting determines the amount owing for the purpose of enforcement.

In our view, neither of the Security Documents benefits from the close-out netting exclusion, even though each can be argued to form part of the *Master Agreement*, which is a close-out netting contract. This is because the security interest which they create is not in property which is under the close-out netting contract, nor is it subject to close-out netting itself. The security interest is in property which is outside of the close-out netting contract and therefore does not benefit from the close-out netting exclusion.

(b) Transfer Annex

The Transfer Annex is a Transaction for the purposes of the Master Agreement. The terms of that Transaction provide for payments and deliveries to be made between the parties by reference to the valuations and calculations made under the terms of the Transfer Annex.

If an Event of Default exists with respect to either party and the Non-defaulting Party elects to terminate the outstanding Transactions, the obligations of the parties to continue to make those payments and deliveries are terminated and an amount equal to the Value of the Credit Support Balance is deemed to be an Unpaid Amount under the Master Agreement and included in the calculation of the termination amount payable under Section 6(e) of the Master Agreement.

It is important to note that it is only through this inclusion of the Value of the Credit Support Balance in the close-out netting process under the Master Agreement that the terms of the Transfer Annex has the effect of "securing" the payment of future amounts owing in respect of other Transactions. The actual Eligible Credit Support which has been already transferred is not part of this process. There is no "enforcement" against that Eligible Credit Support and it may or may not be in the possession or control of the Transferee. For this reason, the Transferor has no interest in the Eligible Credit Support which has been transferred. The payments and deliveries of Eligible Credit Support made under the Transfer Annex are made in the *performance* of contractual obligations to do so, not as *security* for other obligations which are yet to be performed. Instead, any *security* provided by the terms of the Transfer Annex is provided through the right to include the value of the obligation of the Transferee to transfer Equivalent Credit Support to the Transferor in the close-out netting under the Master Agreement, which benefits from the close-out netting exclusion from the PPSA described above. Accordingly, in our view, the Transfer Annex comprises both rights and interests which are created, and held, solely under and as an elemental part of a close-out netting contract and created by transactions under a close-out netting contract. Consequently, the interests under the Transfer Annex which might otherwise amount to security interests under the PPSA should be excluded from the PPSA's operation by the exclusion of rights and interests under close-out netting contracts contained in the provisions of the PPSA.[92]

2 Action needed to perfect transfers

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

Under Australian Law, there are no ongoing actions of this kind that are required to ensure a continuation of title. There are no filing or perfection requirements of this kind that are necessary or desirable, and no consents or regulatory approvals would be required subject to any registration or notification requirements applicable under the terms of the Eligible Credit Support.[93]

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92 In addition the PPSA expressly provides that the *Netting Act* prevails over it to the extent of any inconsistency.

93 We have assumed that the Eligible Credit Support which is actually transferred is not an account or chattel paper under the PPSA. If it were then some form of perfection of the transfer may be needed. This is a different matter to taking a security interest over an account which arises because of the transfer.

However, there may be stamp duty liability payable on transfers of Eligible Credit Support. Whether there is stamp duty payable on the transfer of Eligible Credit Support depends on the type of property comprising the Eligible Credit Support and the State or Territory with which the Transfer Annex has a territorial connection (for example, if the document is entered into in that jurisdiction or relates to property in that jurisdiction). There are stamp duty exemptions in certain jurisdictions which relate to transfer of corporate debt securities (such as debentures, bonds and notes issued by a corporation, government or government authority). Transfers of cash will not be liable to any transfer stamp duty. The stamp duty provisions in connection with the transfer of property differ amongst the Australian Jurisdictions. Please note that we do not opine in this memorandum on taxation consequences (other than our comments above in relation to stamp duty), including but not limited to, capital gains tax on transfers of Eligible Credit Support, interest withholding tax on Distributions and the goods and services tax.

3 Substitutions

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

In our opinion, the provisions of Paragraph 3(c) of the Transfer Annex relating to the exchange of Eligible Credit Support do not change the characterisation of the transaction effected under the Transfer Annex from that of transfers by way of unconditional transfers of title. Paragraph 3(c) of the Transfer Annex requires the return of equivalent securities rather than the return of the same securities. On that basis, our opinion is that an exchange under the Paragraph would be characterised by an Australian Court as an unconditional transfer of title, whether or not consent is required for the substitution and, accordingly, the Transferor and Transferee may agree that no consent is required.

4 Enforceability of CSA being a "Transaction"

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

In our opinion, Paragraph 6 of the Transfer Annex would also be valid to the extent that it provides for the Value of the Credit Support Balance to be included in the calculation of the net amount payable under Section 6(e) of the Master Agreement. The availability of netting provisions under Section 6(e) of the Master Agreement in insolvency is subject to the same considerations as in our Netting Opinion.

It is our opinion that the obligations under the Transaction comprised in the Transfer Annex will not be treated differently to obligations arising under other Transactions governed by the Master Agreement. As a result, the inclusion and netting of an amount equal to the Value of the Credit Support Balance pursuant to Section 6(e) of the Master Agreement will be effective due to the operation of section 14 of the *Netting Act* subject to the issues discussed in Part D.3 of the Netting

Opinion (which includes the provisions of the *Netting Act* equivalent to the voidable transaction provisions in the *Corporations Act*). Particular attention should be paid to the operation of the limitations to the *Netting Act* protection set out in paragraph A.6.8 and the requirements of good faith, no reasonable grounds for suspecting insolvency and valuable consideration.

This view is supported by the Explanatory Memorandum, which provides:

> The Bill does not address title transfer arrangements or close-out netting provisions, as Parts 4 and 5 of the PSN Act already provides robust protection to the process under a close-out netting contract … These protections already allow for transactions under a close-out netting contract such as an ISDA Master Agreement to be closed-out and for an outstanding obligation of the transferee to transfer equivalent collateral under a title transfer credit support arrangement (e.g. an obligation to pay an amount equivalent to the value of the credit support balance under an English law governed Credit Support Annex) to be the subject of the close-out netting process and included in the net amount which arises as a result of that process in accordance with the protections available under the PSN Act…
>
> … The current provisions in the PSN Act therefore facilitate the termination of obligations to make payments and deliveries of margin under the close-out netting contract and the inclusion of the value of margin provided by way of title transfer in the calculation of the net amount payable under the relevant close-out netting contract. The reforms in the Bill to subsections 14(1) and 14(2) do not derogate from, or otherwise limit, the existing protections provided to the close-out netting process which occurs under close-out netting contracts (e.g. the process which occurs under subsection 6(e) of the ISDA Master Agreements and related title transfer credit support arrangements such as paragraph 6 of the English law governed Credit Support Annex).[94]

5 Effect of insolvency of the Transferor

Would the rights of the Transferee be enforceable in accordance with the terms of the Master Agreement and the Transfer Annex, irrespective of the insolvency of the Transferor?

The insolvency of the Transferor would affect the rights of the Transferee to the extent that netting was unavailable (see our Netting Opinion), to the extent there is a clawback (see below), or to the extent that there was a stay on rights (see paragraph B.17). However, such a stay on rights would not interfere with the ability of the Transferee to use cash or sell securities transferred to it absolutely.

6 Clawback

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

[94] Explanatory Memorandum, [1.11] and [1.19]. There are other paragraphs of the Explanatory Memorandum which support our opinion, for example Explanatory Memorandum, [1.21].

The analysis set out in paragraph B.18 above and Schedule 3 of this memorandum (except where it specifically relates to enforcement of security) would apply equally to transfers of Eligible Credit Support under the Transfer Annex. This means that it is important that the defence to a voidable preference claim can be satisfied in respect of subsequent transfers of Eligible Credit Support at the time of a transfer of substitute Eligible Credit Support or additional Eligible Credit Support.[95]

In respect of this defence, it is of particular importance to show that the transfer has been made for valuable consideration.[96] Although it may be argued that the transfer of Eligible Credit Support under the Transfer Annex is without consideration, we consider sufficient valuable consideration will exist in that the transfer is a payment or delivery made in satisfaction of an obligation incurred at the time of entering into the Transfer Annex.[97] It is then relevant to ensure that consideration is present at the time the Transferor agreed to undertake those obligations, being the time of entry into the Transfer Annex. This consideration could be present where:

(a) the Transfer Annex was entered into at the same time as the *Master Agreement* (meaning that the obligations undertaken under the Transfer Annex are part of the consideration for entering into the trading relationship); or

(b) either party may be obliged to deliver Eligible Credit Support under the Transfer Annex (meaning that the obligations undertaken by the Transferor were consideration for the obligations undertaken by the Transferee); or

(c) some other consideration is provided.

7 Agreements on governing law

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

Our analysis in paragraph B.19 above applies equally to the Transfer Annex.

8 Validity of outright transfer concept

Is the Transfer Annex in an appropriate form to create the intended outright transfer of ownership in the Eligible Credit Support to the Transferee? If there are any other requirements to ensure the validity of such transfer in each type of Eligible Credit Support created by the Transferor under the Transfer Annex, please indicate the nature of such requirements. For example, are there any requirements of the type referred to in question 6 in Part B above?

The Transfer Annex is in an appropriate form to create the intended outright transfer of ownership in Eligible Credit Support located in Australia. There are no particular requirements under Australian Law other than those specified in the Transfer Annex. If, however, the Eligible Credit Support is located outside Australia, it would be necessary to ensure that the appropriate local requirements for the formal validity of the transfer of that Eligible Credit Support have been satisfied.

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95 See Schedule 3 for more detail on voidable preference claims,

96 See Schedule 3 for our analysis as to where we consider the provision of Collateral will be considered to be for valuable consideration.

97 *PT Garuda Indonesia Ltd v Grellman* (1992) 107 ALR 199 at 215. Also see our comments at footnote 102.

9 Additional questions in relation to the VM Transfer Annex

For Transfer Annexes, would any of your responses to questions 1 through to 8 of this Part C be different as a result of the inclusion of the VM Transfer Annex in this opinion that was not previously included? If so, please comment specifically on any such changes.

The conclusions in our Collateral Opinion relating to the Transfer Annexes are not materially adversely affected as a result of the inclusion of the VM Transfer Annex in this memorandum.

10 VM Transfer Annex IA Amendments

Please assume that the VM Transfer Annex is amended by the VM Transfer Annex IA Amendments. Would any of your responses to questions 1 through 9 of this Part C above be different than the responses to such questions that you provided as of the last date such responses were provided with respect to your jurisdiction as a result of the inclusion of the VM Transfer Annex, as amended by the VM Transfer Annex IA Amendments, in this opinion? If so, please comment specifically on any such changes.

Our conclusions in our responses to questions 1 through 9 of this Part C would not be different as a result of the inclusion of the VM Transfer Annex, as amended by the VM Transfer Annex IA Amendments.

PART D: CLOSE-OUT AMOUNT PROTOCOL AND COLLATERAL AGREEMENT NEGATIVE INTEREST PROTOCOL

1 Close-out Amount Protocol

We have reviewed the Close-out Amount Protocol published by ISDA on 27 February 2009 (the "**Close-out Amount Protocol**"). On the assumption that the changes intended by the Protocol are effective as a matter of the governing law of the Covered Master Agreement (as defined in the Protocol) and the relevant Credit Support Document, we confirm that the changes made by the Protocol are not material to and do not affect the conclusions reached in the Collateral Opinion. This means that the conclusions reached in the Collateral Opinion which relate to the calculation of amounts payable on close-out under the 2002 ISDA Master Agreement will apply to a 1992 ISDA Master Agreement (and its Credit Support Document) amended by the Protocol.

2 Collateral Agreement Negative Interest Protocol

We have reviewed the Collateral Agreement Negative Interest Protocol published by ISDA on 12 May 2014 (the "**Negative Interest Protocol**"). On the assumption that the changes intended by the Protocol are effective as a matter of the governing law of the Protocol and each Protocol Covered Collateral Agreement (as defined in the Protocol), we confirm that the changes made by the Protocol are not material to and do not affect the conclusions reached in our Collateral Opinion.

Yours faithfully

SCHEDULE 1
ASSUMPTIONS

Following are the assumptions set out in the Instruction Letter which we have been instructed to assume in preparing this memorandum.

Part B, Section I

Please make the following assumptions:

(a) *The Security Collateral Provider has entered into a Master Agreement and a Security Document with a Secured Party. Please assume that the parties have entered into either (i) a Master Agreement governed by New York law and or (ii) a Master Agreement governed by English law. If your answers differ depending upon whether (i) or (ii) applies, or as a result of assumption (b) or (c) below, please indicate that clearly in your responses, distinguishing the position for each set of documents.*

(b) *In respect of answering the questions in respect of the 1994 NY Annex, the 2016 VM NY Annex and the 1995 Deed, the parties will enter into (i) the 1994 NY Annex and/or the 2016 VM NY Annex in connection with a New York law governed ISDA Master Agreement; and (ii) the 1995 Deed in connection with an English law governed ISDA Master Agreement.*

(c) *In respect of answering the questions in respect of IM Security Documents, each IM Security Document could be entered into in connection with either a New York law or English law governed ISDA Master Agreement and may be subject to a different governing law than the relevant ISDA Master Agreement (depending on whether the parties choose to align the governing law of the IM Security Document to (i) the Location of the relevant Custodial Account; or (ii) the governing law of the ISDA Master Agreement). The IM NY Annex forms a part of the relevant ISDA Master Agreement and therefore, unless revised by the counterparties, is subject to the same governing law as the relevant ISDA Master Agreement. In respect of an IM NY Annex entered into in connection with an English law governed ISDA Master Agreement, the parties will provide in paragraph 13 of the IM NY Annex that the Annex is governed by and construed in accordance with New York law.*

(d) *Although each of the Security Documents (other than the IM Security Documents) is a bilateral form in that it contemplates that either party may be required to post Collateral to the other depending on movements in Exposure under the relevant Credit Support Document, you should assume, for the sake of simplicity, that the same party is the Security Collateral Provider at all relevant times under the applicable Security Document. In the case of the IM Security Documents, both parties will be required to post Collateral to the other (either under the same IM Security Document or under separate IM Security Documents) in an amount that depends on the IM calculation provisions. For the sake of simplicity you are only asked to consider the Collateral posting leg of one party – issues relating to the insolvency of the Collateral Taker are considered in a separate opinion.*

(e) *Please assume that each party is either (i) a corporation or (ii) a bank or other similar financial institution. However, if your opinion would also be applicable (without additional legal analysis) to other types of legal entities, arrangements or associations (such as trusts or partnerships), please so indicate, as requested above in relation to scope of counterparty type. Please indicate clearly if any type of financial institution that may be established in your jurisdiction is not covered by your opinion. Please set out all of this information, to the extent possible, in Appendix B as requested above.*

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

(g) *You may assume that any provisions of the Master Agreement and the relevant Security Document that you deem crucial to your opinion have not been altered in any material respect. Please state whether and how any selections contemplated by the Master Agreement or the relevant Security Documents would change the substance of your opinion.*

(h) *Pursuant to the relevant Security Document, the counterparties agree that Eligible Collateral will include cash credited to an account (as opposed to physical notes and coins) and certain types of securities (as further described below) that are located or deemed located either (i) in your*

jurisdiction or (ii) outside your jurisdiction.[98]

(i) *Please assume that any securities provided as Eligible Collateral are denominated in either the currency of your jurisdiction or any freely convertible currency and consist of:*

(i) *corporate debt securities whether or not the issuer is organised or located in your jurisdiction;*

(ii) *debt securities issued by the government of your jurisdiction; and*

(iii) *debt securities issued by the government of a member of the "G-10" group of countries; and*

(iv) *corporate equity securities whether or not the issuer is organized or located in your jurisdiction, and in the case of the 1994 NY Annex, the VM NY Annex and the 1995 Deed is held in one of the following forms:*

(A) ***directly held bearer securities****: by this we mean securities issued in certificated form in bearer form (meaning that ownership is transferable by delivery of possession of the certificate) and, when held by a Secured Party as Collateral under a Security Document, held directly in this form by the Secured Party (that is, not held by the Secured Party indirectly with an Intermediary (as defined below));*

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

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

(D) ***intermediated securities****: by this we mean a form of interest in securities recorded in fungible book-entry form in an account maintained by a financial intermediary (which could be a central securities depository ("**CSD**") or a custodian, nominee or other form of financial intermediary, in each case an ("**Intermediary**") in the name of the Secured Party where such interest has been credited to the account of the Secured Party in connection with a transfer of Collateral by the Security Collateral Provider to the Secured Party under a Security Document.*[99]

The precise nature of the rights of the Secured Party in relation to its interest in intermediated debt securities and as against its Intermediary will be determined, among other things, by the law of the agreement between the Secured Party and its Intermediary relating to its account with the Intermediary, as well as the law generally applicable to the Intermediary, and possibly by other considerations arising under the general law or the rules of private international law of your jurisdiction. The Secured Party's Intermediary may itself hold its interest in the relevant securities indirectly with another Intermediary or directly in one of the three forms mentioned in (A), (B) and (C). In practice, there is likely to be a number of tiers of Intermediaries between the Secured Party and the issuer of such securities, at least one of which will be an Intermediary that is a national or international CSD.

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[98] *This locational dichotomy presumes that the location of the Collateral will be the relevant inquiry for purposes of determining what is required in your jurisdiction to create, perfect and enforce a security interest in Collateral. If under the laws of your jurisdiction the relevant inquiry is based on some other factor, please modify the locational dichotomy reflected in this assumption when answering each question to reflect such other factor, as applicable.*

[99] *When responding to a question under the assumption that the Collateral is located or deemed to be located in your jurisdiction, you should assume that the relevant intermediary is located in your jurisdiction (or are held in another manner such that they are deemed to be so located under the laws of your jurisdiction).*

Our expectation is that the Secured Party will normally hold securities in the form of intermediated securities rather than directly in one of the three forms mentioned in (A), (B) and (C) above.

(j) Please assume that cash Collateral is denominated in a freely convertible currency and is held in an account under the control of the Secured Party. The assumptions made in paragraphs (i) and (j) will be subject to modification as discussed below in:

(i) paragraph (n) in respect of the IM Security Documents and

(ii) paragraph (o) in respect of Collateral held in a central securities depository.

(k) Pursuant to the terms and conditions of the Master Agreement, the Security Collateral Provider enters into a number of Transactions with the Secured Party. Such Transactions include any or all of the transactions described in Appendix A. Under the terms of each Security Document, the security interest created in the relevant Collateral secures the Obligations of the Security Collateral Provider arising under the Master Agreement as a whole, including the net amount, if any, that would be due from the Security Collateral Provider under Section 6(e) of the Master Agreement if an Early Termination Date were designated or deemed to occur as a result of an Event of Default in respect of the Security Collateral Provider.

Part B, Section II

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

Part B, Section III

(m) In the case of questions 16 to 18 below, please assume that an Event of Default under Section 5(a)(vii) of the Master Agreement with respect to the Security Collateral Provider has occurred and a formal bankruptcy, insolvency, liquidation, reorganisation, administration or comparable proceeding (collectively, the "insolvency") has been instituted by or against the Security Collateral Provider. If there are different types of insolvency proceedings under the laws of your jurisdiction (for example, bankruptcy or liquidation proceedings where an entity does not emerge as a going concern, on the one hand, and a reorganisation or administration proceeding where an entity is restructured and does continue as a going concern, on the other hand), please briefly describe the different types of proceedings and answer each question with respect to each such proceeding.

Part B, Section IV

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

(o) In certain circumstances, "initial margin" Collateral may be held at a central securities depository. In these circumstances, the parties will not enter into an IM Security Document. Instead please assume that (w) the Collateral is held in an account within Euroclear or Clearstream; (x) the parties have entered into the Euroclear Documents or the Clearstream Documents (as applicable) and other relevant documentation with Euroclear or Clearstream, which collectively establish collateral

arrangements within Euroclear or Clearstream (as applicable) and set forth (i) the manner in which the Collateral is held in Euroclear or Clearstream and (ii) the manner in which the automated transfers of Collateral by Euroclear or Clearstream will be effected (i.e., upon receipt of matching instructions from the Collateral Provider and Collateral Taker as to the overall amount of initial margin Collateral that is required in respect of such Collateral Provider's posting obligation, Euroclear or Clearstream, as applicable, will calculate any excess or deficit and make the relevant transfers accordingly on behalf of the parties in discharge of their obligations to one another); and (y) the Euroclear Documents or the Clearstream Documents and the other documents referred to in (x) (as applicable)are enforceable in accordance with their terms under applicable law (which may be different than the law of your jurisdiction).

With regard to the foregoing, you should be aware that:

(I) in the case of Euroclear, the Collateral is held in a "Pledged Securities Account" and a "Pledged Cash Account" opened in the Euroclear System in the name of Euroclear acting in its own name but for the account of the Collateral Taker (as pledgee under the pledge granted under the Euroclear Security Agreement) and to be operated in accordance with the relevant Euroclear documents referred to at (x) above;[100] *and*

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

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

Part C

Please assume the same facts as set forth in Part B but on the assumption that the parties have entered into a Transfer Annex in connection with a Master Agreement rather than a Security Document. For this purpose, assumptions (a) to (k) should be read as modified by the following: references to the "Security Document(s)" should be deemed to be references to the "Transfer Annex"; references to the "Security Collateral Provider" and "Secured Party" should be deemed to be references to "Transferor" and "Transferee", respectively; and references to "Eligible Collateral" should be deemed to be references to "Eligible Credit Support".

You may make the following additional assumptions:

1 *The Transferor has entered into a Master Agreement governed by English law and a Transfer Annex with the Transferee.*[101] *Pursuant to the terms of the Transfer Annex, and as a matter of English law, transfers of Eligible Credit Support involve an outright transfer of title, free and clear of any liens, claims, charges or encumbrances or any other interest of the transferring party or of any third person (other than a lien routinely imposed on all securities in a relevant clearance system). If an Event of Default exists with respect to either party, an amount equal to the Value of the Credit Support Balance is deemed to be an Unpaid Amount under the Master Agreement and therefore is taken into account for purposes of determining the amount due upon close-out of the Transactions pursuant to Section 6(e) of the Master Agreement. Although such arrangement has an economic effect similar to the Collateral arrangements evidenced by the Security Documents, the Transfer Annex is not intended to create any form of security interest. There are also significant differences to the rights of the parties under the Transfer Annex, as further described in the "Summary of the Credit Support Documents" section of the Instruction Letter.*

2 *You may assume that transfers under the Transfer Annex would not be re-characterised as creating*

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100 We assume that, for the purposes of the definition of "securities account" in the PPSA and "intermediated financial property" in the *Netting Act*, the person in whose name Euroclear maintains the "Pledged Securities Account" or "Pledged Cash Account" is the Collateral-taker. The definition of "securities account" in the PPSA is set out in paragraph A.5.2 and the definition of "intermediated financial property" is set out in paragraph A.6.5(h).

101 *Please assume for purposes of your analysis of the Transfer Annex that it is being used together with either the 1992 version of the Master Agreement or the 2002 ISDA Master Agreement.*

a form of security interest by an English court, provided that the Transfer Annex was not amended in any material way and provided that the parties by their conduct did not otherwise clearly evidence an intention to create a security interest in transferred Collateral.

General assumptions and qualifications

Apart from other assumptions set out in various parts of this analysis, the conclusions set out in this memorandum are based on the assumptions that:

(a) each Master Agreement, Credit Support Document, Euroclear Document and Clearstream Document (including as amended in the manner contemplated in this memorandum) is completed and executed, so as to render each Master Agreement, Credit Support Document, Euroclear Document and Clearstream Document valid and in all respects enforceable in accordance with the terms of its governing law;

(b) the terms of the Master Agreement, including each Transaction under the Master Agreement, the Credit Support Document, the Euroclear Document and the Clearstream Document (including as amended in the manner contemplated in this memorandum) are agreed at arm's length by the parties so that there is no element of unfair preference of one party against the other party's other creditors;

(c) no party is insolvent at the time of entering into the Master Agreement, a Transaction under it, the Credit Support Document, the Euroclear Document, the Clearstream Document (in each case, including as amended in the manner contemplated in this memorandum), or delivering credit support under any of them, or becomes insolvent as a result of any of them;

(d) each Security Collateral Provider and Transferor has full legal and beneficial title to any credit support at the time that it delivers it under a Credit Support Document, Euroclear Document or Clearstream Document (including as amended in the manner contemplated in this memorandum);

(e) the statutory regime governing personal property securities and the enforcement of security given over financial property, in respect of obligations of a party to a close-out netting contract, in Australia incorporates new concepts into Australian Law many of which, as of the date of this memorandum, have not been the subject of detailed analysis in the Superior Courts of Australia;

(f) where the governing law of the Master Agreement, Credit Support Document, Euroclear Document or Clearstream Document (including as amended in the manner contemplated in this memorandum) is not Australian Law, the rights and obligations of the parties to the Master Agreement, Credit Support Document, Euroclear Document or Clearstream Document would be determined on the basis of the plain meaning of the text of the Master Agreement, Credit Support Document, Euroclear Document or Clearstream Document;

(g) any *external administration* of the Secured Party or the Security Collateral Provider commences after 1 June 2016.

Each of the general qualifications expressed in Part K of our Netting Opinion is applicable to the Credit Support Documents, Euroclear Documents and Clearstream Documents (including as amended in the manner contemplated in this memorandum) in the same manner as they are to the "Master Agreements".

SCHEDULE 2
COMPETING CLAIMS

Priority rules

The PPSA includes priority rules which determine the priority between competing security interests attached to the same collateral (and in some cases, they determine priority between a security interest and another interest such as that of a purchaser). These priority rules replace existing common law and equitable rules.

Generally speaking:

(a) a secured creditor has priority over an unsecured creditor;

(b) a perfected security interest has priority over an unperfected security interest;

(c) the first secured party to perfect its security interest has priority;

(d) priority between unperfected security interests is determined by the order of attachment; and

(e) an unperfected security interest vests in a grantor that is a company if an order is made or resolution is passed for its winding up, an administrator is appointed or the company executes a deed of company arrangement.[102]

However, there are exceptions, including:

(i) that perfection by control confers greater priority than perfection by registration or possession; and

(ii) that the interest of a judgement creditor has priority over any unperfected security interest at the time when the collateral is seized by or on behalf of the judgement creditor or when the relevant judgement order or garnishee order is made in relation to the judgement creditor.

Taking free rules

The PPSA also includes rules on when personal property can be acquired free of a security interest. Most of the rules apply to a security interest whether or not it is perfected. For example, a purchaser of an investment instrument (other than the secured party) takes the instrument free of a security interest in the instrument if the purchaser gives value for the instrument and the purchaser takes possession or control of the instrument. A similar rule applies in relation to an intermediated security provided that instead of taking possession or control the transferee for value takes its interest in the underlying financial product in accordance with a consensual transaction. Further, if a secured party does not perfect a security interest, a buyer or lessee of the collateral may take the personal property free of the security interest.

Transitional arrangements

The transitional provisions are intended to ensure that transitional security interests which were migrated from existing registers retain the priority they had prior to migration. They do this by providing that the migrated security interest will be taken to be perfected from immediately before 30 January 2012, being the date on which the PPSA commenced operation. Please see paragraph B.5.4(a) above with respect to the migration of security interests registered on certain existing registers to the PPS register.

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[102] The time at which this is tested (the "**critical time**") is in the case of a company or body corporate:

(i) that is being wound up, the time when the winding up is taken to have begun or commenced;

(ii) the 'section 513C day' which, in relation to the administration of a company, is the day the administration began or, if there was a prior liquidation, the day when the winding up is taken to have begun.

Priority between two or more security interests in collateral that are currently perfected is determined by the order in which the priority time for each security interest occurs. The priority time for a migrated security interest will be the time the security interest is perfected by force of the PPSA. This time will be the time from immediately before the registration commencement time.

All migrated security interests will have the same priority time for the purposes of the priority rules (that is, from immediately before the registration commencement time). This means that all migrated security interests will have priority over any security interests perfected **at or after** the registration commencement time. However, it also means that it will not be possible to determine priority between two migrated security interests because they have the same priority time. In these circumstances, the PPSA provides that the migrated security interests have the priority between themselves that they would have had under the law that applied to such priority immediately before the registration commencement time and as if the PPSA had not been enacted. In other words, priority will be determined under the priority rules in the *Corporations Act* that were in force immediately prior to 30 January 2012.[103]

[103] This is reinforced by sections 1502 and 1506 of the *Corporations Act*. Section 1502 provides that the repeal of Chapter 2K by the *Personal Property Security (Corporations and Other Amendments) Act 2010* of Australia does not apply in relation to registrable charges for a period of 7 years after the registration commencement time. Section 1506 further provides that at and after the registration commencement time, registrable charges have the priority between themselves that they would have had under the *Corporations Act* immediately before the registration commencement time subject to the transitional provisions in the PPSA.

SCHEDULE 3
CLAWBACK

Under section 588FE of the *Corporations Act*, the following types of transactions may, by order of the court, be set aside or modified on application of a liquidator of an Australian Company within the following suspect periods (such transactions are described as *voidable transactions*):

Type	**Suspect period***
Insolvent transaction which is an unfair preference	6 months
Insolvent transaction which is an uncommercial transaction	2 years
Insolvent transaction (which is also an unfair preference or an uncommercial transaction) and which is for the purpose of defeating, delaying or interfering with creditor's rights on a winding-up	10 years
Insolvent transaction where a "related entity"[104] of the Security Collateral Provider is a party to the transaction	4 years
Unreasonable director-related transaction	4 years
Unfair loan	whenever made

* Transaction entered into, or act done for the purposes of giving effect to transaction, within this period before the date ("**relation-back day**") which is the date determined in accordance with section 91 of the *Corporations Act*.[105]

The definition of "transaction" in section 9 of the *Corporations Act* is very wide and includes transfers of property, making payments, incurring obligations and granting releases. Section 588FE also extends to acts done for the purpose of giving effect to a transaction.

A transaction will be an "insolvent transaction" if it is an unfair preference given by an Australian Company or an uncommercial transaction of an Australian Company where at the time of entering into the transaction the Australian Company is insolvent or where the Australian Company becomes insolvent because of the transaction. The word "insolvent" means an inability to pay debts as and when they become due and payable. Unfair preferences and uncommercial transactions are discussed in turn below.

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104 The definition of a "related entity" of the Security Collateral Provider means (see section 9 of the *Corporations Act*):

(a) a promoter of the Security Collateral Provider, a relative, spouse or de facto spouse of any such promoter, and a relative of a spouse or of a de facto spouse of any such promoter;

(b) a director or member of the Security Collateral Provider or a related body corporate of the Security Collateral Provider, a relative, spouse or de facto spouse of any such director or member, and a relative of a spouse or of a de facto spouse of any such director or member;

(c) a body corporate that is related to the Security Collateral Provider;

(d) a beneficiary under a trust of which the Security Collateral Provider is or has at any time been the trustee, a relative, spouse or de facto spouse of any such beneficiary, and a relative of a spouse or of a de facto spouse of any such beneficiary;

(e) a body corporate one of whose directors is also a director of the Security Collateral Provider; and

(f) a trustee of a trust of which a person is a beneficiary, where the person is a related entity of the Security Collateral Provider because of the application of one or more of paragraphs (a) to (e).

105 The *Insolvency Law Reform Act 2016* (Cth) inserted section 91 into the *Corporations Act*, commencing 1 March 2017. Section 91 specifies the particular relation-back day which will apply depending on the specific circumstances.

Unfair preference

Under section 588FA of the *Corporations Act* a transaction is an unfair preference if it is a transaction to which an Australian Company and the creditor are parties and which results in the creditor receiving a larger number of cents in the dollar in respect of an unsecured debt than it would have received in respect of the debt if the transaction were set aside and the creditor were to prove for the debt in the winding up of the company. It is to be noted that it is not necessary for the Australian Company to intend that the creditor receive a preference in order for the transaction to be voidable under section 588FE. One example of an unfair preference is security being granted to an unsecured creditor just prior to the Australian Company's insolvency.

Special rules apply to transactions which are an integral part of a continuing business relationship, such as a running account. Transactions in the course of that relationship are only regarded as an unfair preference if, taken as a whole, they constitute an unfair preference. Only the amount (if any) by which the debit balance is reduced during the suspect period, or during any part of that period, is recoverable. The liquidator can choose any date during the suspect period. Thus the date of peak indebtedness can be chosen and the amount claimed can be the amount by which the debit balance was reduced between the chosen date and the date of the relation-back day.

Uncommercial transactions

Under section 588FB of the *Corporations Act*, a transaction is an uncommercial transaction if it may be expected that a reasonable person in the circumstances of the company would not have entered into the transaction having regard to the benefit for the company, the detriment to the company, the respective benefits to other parties to the transaction and other relevant matters.

An unreasonable director-related transaction includes, among other things, a payment made by an Australian Company, and a conveyance, transfer or other disposition of property in an Australian Company, where the payment, conveyance, transfer or disposition is made to a director of the company, close associate of a director of the company or a person on behalf of, or for the benefit of, a director of the company. We assume this would not be applicable to a transfer of Collateral by the Security Collateral Provider to the Secured Party.

Exceptions to voidability

However, if an Australian Company goes into liquidation, a transaction entered into during the suspect period which may be voidable (ie any of the "Types" of transaction referred to above other than an unfair loan or unreasonable director-related transaction) would not be voidable against a creditor if certain conditions are satisfied. Under section 588FG(2) of the *Corporations Act*, an Australian Court cannot make an order in respect of an unfair preference or an uncommercial transaction which materially prejudices a right or interest of a person if it is proved that:

(a) the person became a party to the transaction in good faith. Good faith would be absent if there were fraud or if there subsisted an intention on the part of the creditor to obtain an advantage vis-à-vis the other creditors of the Australian Company. A transaction entered into as part of the ordinary course of business would not of itself result in the inference that there was an absence of good faith; and

(b) at the time when the person became a party to the transaction:

(i) the person had no reasonable grounds for suspecting that the Australian Company was insolvent (in the sense that the Australian Company was unable to pay all its debts as and when they become due and payable) or would become insolvent if it entered into the transaction; and

(ii) a reasonable person in their circumstances would have had no grounds for so suspecting.

The notion "reasonable grounds for suspecting" embodies something which, in all the circumstances, would create in the mind of a reasonable person in the position of the creditor an actual apprehension or fear that the Australian Company was unable to pay its

debts when they became due and payable. The notion also embodies a mistrust of the Australian Company's ability to pay its debts as they become due, and an appreciation of the advantage which the creditor's acceptance of the payment would have as between the creditor and other creditors of the Australian Company; and

(c) the person provided valuable consideration under the transaction or changed its position in reliance on the transaction. In this context the valuable consideration must be real and not colourable in the sense of being contrived or without substance.

The Australian Courts will take a substantive approach on these issues. If the transaction effects the satisfaction of obligations subsisting under an earlier transaction, at a time when the obligor is insolvent, then the second transaction could be preferential unless the defences set out above are established.

Having regard to the above matters, it is difficult to see how the provision of Collateral at or about the same time that a Transaction is entered into under the Master Agreement would be regarded as an unfair preference where it is not referable to any existing indebtedness. We also think that the provision of Collateral which effects:

(a) improvements in the value of Eligible Collateral for existing Transactions pursuant to substitution (that is, where the substituted Collateral was more valuable than the Collateral it replaced); or

(b) the provision of additional Eligible Collateral to maintain the required Credit Support Amount in respect of Transactions that were in existence before the provision of the additional Eligible Collateral (that is, in commercial parlance, "top up Collateral"),

in most cases would be considered to be for valuable consideration.[106] Therefore, provided the substitution or additional Collateral is received in good faith without knowledge or suspicion of insolvency, it should not be regarded as an unfair preference.

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[106] There is no authority that we have been able to find which is directly on point. Keay, *McPherson - The Law of Company Liquidation* (4th Edn, LBC Information Services) p 482 states:

> "In most claims by a liquidator in which it is alleged that the transaction was an unfair preference the defendant will have little difficulty in establishing valuable consideration (Historically, "valuable consideration" has not been an issue in cases involving defences to preferences under s122(2) of the *Bankruptcy Act*: Purcell, "Banks and the Recovery of Voidable Preferences" (1990) 2 Bond LR 107 at 112).

This is because, in the normal course of things, the debtor company will have paid the defendant the price, or part thereof, for services rendered or goods supplied and prior indebtedness is good consideration for a payment made in discharge of that indebtedness (*Taylor v White* (1964) 110 CLR 129 at 139; *Kyra Nominees Pty Ltd (in liq) v National Australia Bank Ltd* (1964) 4 ACLC 400 at 407).

Where the company entered into a transaction that involved something other than a payment, the issue of valuable consideration may be a live one. As an example, if the company grants to the creditor security for an existing debt, the creditor must demonstrate that some valuable consideration was given for the security (Rose, *Lewis' Australian Bankruptcy Law* (10th ed, Law Book Co, Sydney, 1994), p 183)."

There is very little authority as to what consideration the holder of a security interest which secures an antecedent debt must provide in order for the holder to have provided valuable consideration for it within section 588FG(2)(c). (One example is a forbearance to sue for the antecedent debt (*Re Hyams* (1970) 19 FLR 232: *PT Garuda Indonesia Ltd v Grellman* (1992) 107 ALR 199, which concern a similar defence in relation to voidable settlements under the Bankruptcy Act). In *N. A. Kratzmann Pty Ltd v Tucker* (1966) 123 CLR 257 the issue was whether a mortgage given by a company as security for money owing to a mortgagee company was void as a preference. The mortgage was executed within the six months before the winding up of the company but the mortgagee argued that the mortgage was executed in pursuance of an agreement to do so entered into before the commencement of the six month period. The court found that such an agreement was not supported on the facts. However, the reasoning proceeded on the assumption that if such an agreement had existed, the transaction would not have been viewed as a preference on the basis of absence of valuable consideration.

The difference between the facts in that case and the Security Documents is that the Security Documents are entered into at the beginning of the trading relationship (or at some point in time in respect of future transactions - these comments only apply to exposures which arise under transactions entered into on or after the time the Security Document is entered into). The agreement to provide additional Eligible Collateral once a Delivery Amount arises is not a new agreement made at the time the additional Eligible Collateral is provided, which would require fresh consideration eg a forbearance to sue, at that time. Rather the provision of additional Eligible Collateral

It is unlikely that Collateral provided in connection with a Transaction under the Master Agreement entered into at a commercial rate as part of an arm's length dealing would be characterised as an uncommercial transaction. The provision of any Collateral may only be used to discharge Obligations and any excess must be returned.

Void dispositions

Section 468 of the *Corporations Act* renders void any disposition of property of an Australian Company[107] effected after the commencement of the winding up by an Australian Court (see footnote 101 above). Section 468 does not apply to exempt dispositions, which include dispositions by a liquidator, an administrator or a payment on or prior to the date of the winding up order by an Australian bank in good faith and in the ordinary course of banking business.

Section 437D also renders void any transaction or other dealing affecting the property of an Australian Company under administration, unless the administrator entered into it on the Australian Company's behalf, the administrator consented to it in writing before it was entered into, or it was entered into under an order of an Australian Court, subject to limited exceptions.

Voluntary alienation to defraud creditors

Under section 37A of the *Conveyancing Act 1919* (NSW) (and its equivalent in other Australian Jurisdictions such as section 172 of the *Property Law Act 1958* (Vic)), alienation of property made with intent to defraud creditors is rendered voidable by any person prejudiced by the alienation. In New South Wales, this law does not apply to any interest in property alienated to a purchaser in good faith not having, at the time of the alienation, notice of the intent to defraud creditors. Equally, in Victoria, the relevant law does not extend to any interest in property alienated for valuable consideration and in good faith or upon good consideration and in good faith to any person not having, at the time of the alienation, notice of the intent to defraud creditors.

Disclaimer of unprofitable contracts

Under section 568 of the *Corporations Act,* any property of an Australian Company at any time, including any unprofitable contract entered into by the Australian Company, may be subject to disclaimer by the liquidator. However, a liquidator requires leave of an Australian Court to disclaim a contract (other than an unprofitable contract). Where it is effective, the disclaimer is taken to have terminated the Australian Company's rights, interests, liabilities and property in respect of the disclaimed property, but does not affect any other person's rights or liabilities except so far as necessary in order to release the company and its property from liability.

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constitutes the performance of an obligation agreed to, and supported by consideration at the time the Security Document is entered into. Accordingly, we have concluded that the provision of additional Eligible Collateral constitutes a discharge by the Security Collateral Provider of their pre-existing obligation to provide the additional Eligible Collateral. It is therefore analogous to a debtor discharging a debt for services rendered previously to the debtor by the creditor.

In the case of substitutions, the analysis is that:

(a) if the substitution is permitted without consent, there is a pre-existing agreement to provide substitute collateral if the Security Collateral Provider calls for the return of Collateral. So under the same analysis as for top up collateral, the Security Collateral Provider is performing a pre-existing obligation in providing the substitute collateral; and

(b) if the substitution requires consent, consideration is given at the time of the substitution (ie the Secured Party's agreement to release the security over the substituted Collateral).

The consideration provided need not be equal to the value of the substitute Collateral.

The above analysis assumes that the parties are dealing at arms' length on ordinary commercial terms for transactions of this nature. If they are not, an analysis should take place as to whether the consideration is real and not colourable in the sense of being contrived or without substance.

107 Section 468 applies only to dispositions by the Australian Company itself. It does not apply to action taken by a Secured Party to exercise rights in relation to property the subject of a Security Document.

Circulating assets

Under section 588FJ of the *Corporations Act*, if the Australian Company is being wound up then a circulating security interest which is created within 6 months before the relation-back day (or after that date) is void as against the Australian Company's liquidator except so far as it secures, essentially, the giving of some new benefit to the Australian Company (such as an advance at or after the time the security interest was created) or if it is proved that the Australian Company was solvent immediately after that time.

Late registration

Section 588FL of the *Corporations Act* describes the impact of late registration of a security interest if a company is subject to winding up, administration or a deed of company arrangement. Under Section 588FL of the *Corporations Act* a security interest which is perfected only by registration vests in the grantor (defeating the secured party) if the registration takes place after the latest of the date which is (a) 6 months before the critical time (the critical time relates to the time at which winding up or administration is taken to commence);[108] (b) the end of 20 business days after the security agreement comes into force or if earlier, the critical time; or (c) in the case of a security interest which came into force under a foreign law but first became enforceable against third parties under the law of Australia after 6 months before the critical time, 56 days after it became enforceable under Australian Law (or if earlier, the critical time).

[108] The time at which this is tested (the "**critical time**") is in the case of a company or body corporate:

(i) that is being wound up, the time when the winding up is taken to have begun or commenced;

(ii) the 'section 513C day' which, in relation to the administration of a company, is the day the administration began or, if there was a prior liquidation, the day when the winding up is taken to have begun.

SCHEDULE 4
OTHER CIRCUMSTANCES THAT MIGHT AFFECT ENFORCEMENT WHERE THE *NETTING ACT* DOES NOT APPLY

In circumstances where the *Netting Act* does not apply, legislation including the following may affect the enforcement of a security interest:

(a) ADIs (which would include building societies and credit unions) for the purposes of the *Banking Act*.

If the Security Collateral Provider is one of these entities, the *Banking Act* and the *Reserve Bank Act 1959* of Australia ("***Reserve Bank Act***") are potentially relevant to the enforceability of security provided by them.

No provision of the *Banking Act* or the *Reserve Bank Act* prohibits an ADI from granting security over its assets.

In respect of ADIs, the claims mandatorily preferred by law include the claims referred to in sections 13A(3) and 16 of the *Banking Act* and section 86 of the *Reserve Bank Act*, as summarised below.

(i) Section 13A(3) of the *Banking Act* provides that in the event an ADI becomes unable to meet its obligations or suspends payment, the assets of the ADI in Australia are to be available to satisfy:

(A) first, certain obligations of the ADI to APRA (if any) arising under Division 2AA of Part II of the *Banking Act* in respect of amounts payable by APRA to holders of "protected accounts" (as defined in the *Banking Act*) in connection with the Financial Claims Scheme ("**FCS**") established under the *Banking Act*;

(B) second, APRA's costs (if any) in exercising its powers and performing its functions relating to the ADI in connection with the FCS;

(C) third, the ADI's liabilities (if any) in Australia in relation to protected accounts that account-holders keep with the ADI;

(D) fourth, the ADI's debts (if any) to the Reserve Bank of Australia ("**RBA**"); and

(E) fifth, the ADI's liabilities (if any) under an industry support contract that is certified under section 11CB of the *Banking Act*,

in each case, in priority to all other liabilities of the ADI. The assets of the ADI are taken for the purposes of section 13A(3) not to include any interest in an asset (or a part of an asset) in a cover pool for covered bonds for which the ADI is the issuer.

(ii) Section 16 of the *Banking Act* provides that certain other debts of an ADI due to APRA shall, in the winding up of the ADI, have, subject to section 13A(3) of the *Banking Act*, priority over all other unsecured debts of the ADI.

(iii) Section 86 of the *Reserve Bank Act* provides that, subject to section 13A(3) of the *Banking Act*, debts of a bank due to the RBA shall, in a winding up of the bank, have priority over all other debts of the ADI.

In addition, under the *Banking Act*, any other party to a contract to which the ADI is a party may not deny any obligations under that contract, accelerate any debt under that contract, close out any transaction relating to that contract or enforce any security under that contract on the grounds that:

(I) the ADI is subject to a direction by APRA under the *Banking Act* (see sections 11CD and 13N of the *Banking Act*); or

(II) an ADI statutory manager (as defined in the *Banking Act*):

(A) is in control of the ADI's business (see section 15C of the *Banking Act*); or

(B) takes various actions in respect of any shares in the ADI (see section 14AC of the *Banking Act*).

Division 2 of Part 4 of the *Netting Act* sets out the circumstances in which non-direction stays (including sections 14AC and 15C of the *Banking Act*) may cease in relation to:

(A) a close-out netting contract to which a regulated body (as defined in the *Netting Act*) is a party (and which satisfies the requirements in section 15A(1) of the *Netting Act*); or

(B) a security given over financial property, in respect of an obligation of a party to a close-out netting contract to which a regulated body is a party (and which satisfies the requirements in section 15A(2) of the *Netting Act*).

The circumstances in which non-direction stays may cease is considered further in our Netting Opinion.

(b) Insurance companies

Section 187 of the *Life Insurance Act* provides that in a winding up, the assets of the statutory funds are to be applied:

(i) first, in discharging preferred creditors as identified in section 556(1) of the *Corporations Act*; and

(ii) second, in discharging of liabilities to policy holders; and

(iii) third, in discharging of other liabilities that are referrable to the business of the statutory fund; and

(iv) if there are any assets remaining, as the Court directs.

Under section 116(3) of the *Insurance Act*, in the winding up of a general insurance company, its assets in Australia may not be applied to discharge its liabilities other than its liabilities in Australia unless it has no liabilities in Australia.

In addition, under the *Life Insurance Act* and *Insurance Act*, a counterparty to a contract to which the life company or general insurer (as applicable) is a party may not deny any obligations under that contract, accelerate any debt under that contract, close out any transaction relating to that contract or enforce any security under that contract on the grounds that:

(I) the life company or general insurer (as applicable) is subject to a direction by APRA under the *Life Insurance Act* or *Insurance Act* (as applicable) (see sections 103K and 105 of the *Insurance Act* and sections 230AJ and 230C of the *Life Insurance Act*); or

(II) in respect of a judicial manager (as defined in the *Life Insurance Act* or *Insurance Act* (as applicable)):

(A) the management of the life company, or of part of the business of the life company is vested in the judicial manager (see section 165B of the *Life*

Insurance Act) or the management of the general insurer is vested in the judicial manager (see section 62V of the *Insurance Act*); or

(B) the judicial manager takes various actions in respect of any shares in the life company or general insurer (see section 168C of the *Life Insurance Act* and section 62ZB of the *Insurance Act*).

Division 2 of Part 4 of the *Netting Act* sets out the circumstances in which non-direction stays (including, relevantly, sections 165B and 168C of the *Life Insurance Act* and sections 62V and 62ZB of the *Insurance Act*) may cease in relation to:

(A) a close-out netting contract to which a regulated body (as defined in the *Netting Act*) is a party (and which satisfies the requirements in section 15A(1) of the *Netting Act*); or

(B) a security given over financial property, in respect of an obligation of a party to a close-out netting contract to which a regulated body is a party (and which satisfies the requirements in section 15A(2) of the *Netting Act*).

The circumstances in which non-direction stays may cease is considered further in our Netting Opinion.

(c) *Business Transfer Act*

Under the *Business Transfer Act*, if a body corporate that is, or is proposed to become, a transferring body (as defined in the *Business Transfer Act*) is or was party to a contract, the fact that an act is done for the purposes of Division 2 or 3 of the *Business Transfer Act*, or that a certificate of transfer comes into force under Division 3 of the *Business Transfer Act*, in connection with the body does not allow the contract, or any other party to the contract, to deny any obligations under that contract, accelerate any debt under that contract, close out any transaction relating to that contract or enforce any security under that contract.[109]

Division 2 of Part 4 of the *Netting Act* sets out the circumstances in which non-direction stays (including, relevantly, section 36AA of the *Business Transfer Act*) may cease in relation to:

(aa) a close-out netting contract to which a regulated body (as defined in the *Netting Act*) is a party (and which satisfies the requirements in section 15A(1) of the *Netting Act*); or

(bb) a security given over financial property, in respect of an obligation of a party to a close-out netting contract to which a regulated body is a party (and which satisfies the requirements in section 15A(2) of the *Netting Act*).

The circumstances in which non-direction stays may cease is considered further in our Netting Opinion.

[109] *Business Transfer Act*, section 36AA.

SCHEDULE 5
RE-CHARACTERISATION AS A CHARGE

It is a critical element of the operation of the Transfer Annex that the transfers of Eligible Credit Support are "absolute transfers". This is described in paragraph 5(a) of the Transfer Annex which provides that:

> "…all right, title and interest in and to any Eligible Credit Support, Equivalent Credit Support, Equivalent Distributions or Interest Amount which it transfers to the other party under the terms of this Annex shall vest in the recipient free and clear of any liens, claims, charges or encumbrances or any other interest of the transferring party or of any third person (other than a lien routinely imposed on all securities in a relevant clearance system)."

Essentially it is necessary that the Eligible Credit Support is dealt with in the same manner as if it were the subject of a true sale. The principles from relevant cases which have described this in more detail are set out below. Key indicators of an absolute transfer include that:

- the transferee may deal with the transferred property as its absolute owner;
- the transferee is under no obligation to return the same property to the transferor;
- the transferee does not have to account to the transferor for profits on the sale of the transferred property.

In the case of Australian Dollars, we would expect an absolute transfer to be evidenced by a deposit being made into an Australian bank account of the Transferee over which the Transferor has no rights or control.

In the case of Australian Government Securities, we would expect the absolute transfer to be evidenced by a registration of the Transferee as the holder of the securities in the relevant register or clearing system (or in a custodial register of the Transferee's custodian) without the Transferor having any rights in or ability to control the Transferee's holding. Ultimately this is determined by the terms and conditions of the securities and the rules and regulations of the relevant clearing system or arrangements with the Transferee's custodian.

Assuming that the conduct of the parties and other surrounding circumstances are not inconsistent with the terms of the Transfer Annex, we consider that a transfer of Eligible Credit Support under the Transfer Annex will be construed as an absolute transfer and not be characterised as being made by way of security on the basis that:

(a) Paragraphs 5(a) and (b) of the Transfer Annex clearly indicate that transfers of Eligible Credit Support and Equivalent Credit Support are intended to be absolute transfers;

(b) where a Return Amount is determined under Paragraph 2(b) of the Transfer Annex, there is no obligation on the Transferee to re-transfer the original Eligible Credit Support; rather there is an obligation to transfer Eligible Credit Support of the same type, nominal value etc as the Eligible Credit Support originally transferred;

(c) where a party defaults under the Transfer Annex, there is no secured property against which the party to which Eligible Credit Support has been delivered can enforce. Rather, an amount equal to the Value of the Credit Support Balance becomes part of the Unpaid Amount;

(d) the reference to interest payable under Paragraph 5(c) of the Transfer Annex is not to loan interest, but to accrued and unpaid interest in respect of the relevant Eligible Credit Support.

APPENDIX A

(AUGUST 2015)

CERTAIN TRANSACTIONS UNDER
THE ISDA MASTER AGREEMENTS

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Cross Currency Rate Swap. A transaction in which one party pays periodic amounts in one currency based on a specified fixed rate (or a floating rate that is reset periodically) and the other party pays periodic amounts in another currency based on a floating rate that is reset periodically. All calculations are

determined on predetermined notional amounts of the two currencies; often such swaps will involve initial and or final exchanges of amounts corresponding to the notional amounts.

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

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

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

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

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

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

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

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

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

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

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

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

Fund Option Transaction: A transaction in which one party grants to the other party (for an agreed payment or other consideration) the right, but not the obligation, to receive a payment based on the redemption value of a specified amount of an interest issued to or held by an investor in a fund, pooled investment vehicle or any other interest identified as such in the relevant Confirmation (a "Fund Interest"), whether i) a single class of Fund Interest of a Single Reference Fund or ii) a basket of Fund Interests in relation to a specified strike price. The Fund Option Transactions will generally be cash settled (where settlement occurs based on the excess of such redemption value over such specified strike price (in the case of a call) or the excess of such specified strike price over such redemption value (in the case of a put) as measured on the valuation date or dates relating to the exercise date).

Fund Forward Transaction: A transaction in which one party agrees to pay an agreed price for the redemption value of a specified amount of i) a single class of Fund Interest of a Single Reference Fund or ii) a basket of Fund Interests at a future date and the other party agrees to pay a price for the redemption value of the same amount of the same Fund Interests to be set on a specified date in the future. The payment calculation is based on the amount of the redemption value relating to such Fund Interest and generally cash-settled (where settlement occurs based on the difference between the agreed forward price and the redemption value measured as of the applicable valuation date or dates).

Fund Swap Transaction: A transaction a transaction in which one party pays periodic amounts of a given currency based on a fixed price or a fixed rate and the other party pays periodic amounts of the same currency based on the redemption value of i) a single class of Fund Interest of a Single Reference Fund or ii) a basket of Fund Interests.

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

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

Longevity/Mortality Transaction. (a) A transaction employing a derivative instrument, such as a forward, a swap or an option, that is valued according to expected variation in a reference index of observed demographic trends, as exhibited by a specified population, relating to aging, morbidity, and mortality/longevity, or (b) A transaction that references the payment profile underlying a specific portfolio of longevity- or mortality- contingent obligations, e.g. a pool of pension liabilities or life insurance policies (either the actual claims payments or a synthetic basket referencing the profile of claims payments).

Physical Commodity Transaction. A transaction which provides for the purchase of an amount of a commodity, such as oil including oil products, coal, electricity or gas, at a fixed or floating price for actual delivery on one or more dates.

Property Index Derivative Transaction. A transaction, often structured in the form of a forward, option or total return swap, between two parties in which the underlying value of the transaction is based on a rate or index based on residential or commercial property prices for a specified local, regional or national area.

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

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

Swap Deliverable Contingent Credit Default Swap. A Contingent Credit Default Swap under which one of the Deliverable Obligations is a claim against the Reference Entity under an ISDA Master Agreement with respect to which an Early Termination Date (as defined therein) has occurred.

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

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

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

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

APPENDIX B

(SEPTEMBER 2009)

CERTAIN COUNTERPARTY TYPES

Description	**Covered by Memorandum**
Bank/Credit Institution. A legal entity, which may be organized as a corporation, partnership or in some other form, that conducts commercial banking activities, that is, whose core business typically involves (a) taking deposits from private individuals and/or corporate entities and (b) making loans to private individual and/or corporate borrowers. This type of entity is sometimes referred to as a "commercial bank" or, if its business also includes investment banking and trading activities, a "universal bank". (If the entity only conducts investment banking and trading activities, then it falls within the "Investment Firm/Broker Dealer" category below.) This type of entity is referred to as a "credit institution" in European Community (**EC**) legislation. This category may include specialised types of bank, such as a mortgage savings bank (provided that the relevant entity accepts deposits and makes loans), or such an entity may be considered in the local jurisdiction to constitute a separate category of legal entity (as in the case of a building society in the United Kingdom (**UK**)).	Yes, covered by Memorandum provided it is an Australian Company. Partnerships are not covered by Memorandum.
Central Bank. A legal entity that performs the function of a central bank for a Sovereign or for an area of monetary union (as in the case of the European Central Bank in respect of the euro zone).	No, not covered by Memorandum.
Corporation. A legal entity that is organized as a corporation or company rather than a partnership, is engaged in industrial and/or commercial activities and does not fall within one of the other categories in this Appendix B.	Yes, covered by Memorandum provided it is an Australian Company.
Hedge Fund/Proprietary Trader. A legal entity, which may be organized as a corporation, partnership or in some other legal form, the principal business of which is to deal in and/or manage securities and/or other financial instruments and/or otherwise to carry on an investment business predominantly or exclusively as principal for its own account.	Yes, covered by Memorandum provided it is an Australian Company. Partnerships and individuals are not covered by Memorandum.
Insurance Company. A legal entity, which may be organised as a corporation, partnership or in some other legal form (for example, a friendly society or industrial & provident society in the UK), that is licensed to carry on insurance business, and is typically subject to a special regulatory regime and a special insolvency regime in order to protect the interests of policyholders.	Yes, covered by Memorandum provided it is an Australian Company. Partnerships and individuals are not covered by Memorandum.
International Organization. An organization of Sovereigns established by treaty entered into between the Sovereigns, including the International Bank for Reconstruction and Development (the World Bank), regional development banks and similar organizations established by treaty.	No, not covered by Memorandum.

Description	Covered by Memorandum
Investment Firm/Broker Dealer. A legal entity, which may be organized as a corporation, partnership or in some other form, that does not conduct commercial banking activities but deals in and/or manages securities and/or other financial instruments as an agent for third parties. It may also conduct such activities as principal (but if it does so exclusively as principal, then it most likely falls within the "Hedge Fund/Proprietary Trader" category above.) Its business normally includes holding securities and/or other financial instruments for third parties and operating related cash accounts. This type of entity is referred to as a "broker-dealer" in US legislation and as an "investment firm" in EC legislation.	Yes, covered by Memorandum provided it is an Australian Company. Partnerships and individuals are not covered by Memorandum.
Investment Fund. A legal entity or an arrangement without legal personality (for example, a common law trust) established to provide investors with a share in profits or income arising from property acquired, held, managed or disposed of by the manager(s) of the legal entity or arrangement or a right to payment determined by reference to such profits or income. This type of entity or arrangement is referred to as a "collective investment scheme" in EC legislation. It may be regulated or unregulated. It is typically administered by one or more persons (who may be private individuals and/or corporate entities) who have various rights and obligations governed by general law and/or, typically in the case of regulated Investment Funds, financial services legislation. Where the arrangement does not have separate legal personality, one or more representatives of the Investment Fund (for example, a trustee of a unit trust) contract on behalf of the Investment Fund, are owed the rights and owe the obligations provided for in the contract and are entitled to be indemnified out of the assets comprised in the arrangement.	Yes, covered by Memorandum to the extent that the relevant entity is a legal entity which is an Australian Company.
Local Authority. A legal entity established to administer the functions of local government in a particular region within a Sovereign or State of a Federal Sovereign, for example, a city, county, borough or similar area.	No, not covered by Memorandum.
Partnership. A legal entity or form of arrangement without legal personality that is (a) organised as a general, limited or some other form of partnership and (b) does not fall within one of the other categories in this Appendix B. If it does not have legal personality, it may nonetheless be treated as though it were a legal person for certain purposes (for example, for insolvency purposes) and not for other purposes (for example, tax or personal liability).	No, not covered by Memorandum.
Pension Fund. A legal entity or an arrangement without legal personality (for example, a common law trust) established to provide pension benefits to a specific class of beneficiaries, normally sponsored by an employer or group of employers. It is typically administered by one or more persons (who may be private individuals and/or corporate entities) who have various rights and obligations governed by pensions legislation. Where the arrangement does not have separate legal personality, one or more representatives of the Pension Fund (for example, a trustee of a pension scheme in the form of a common law trust) contract on behalf of the Pension Fund and are owed the rights and owe the obligations provided for in the contract and are entitled to be indemnified out of the assets	Yes, covered by Memorandum to the extent that the relevant entity is a legal entity which is an Australian Company.

Description	Covered by Memorandum
comprised in the arrangement.	
Sovereign. A sovereign nation state recognized internationally as such, typically acting through a direct agency or instrumentality of the central government without separate legal personality, for example, the ministry of finance, treasury or national debt office. This category does not include a State of a Federal Sovereign or other political sub-division of a sovereign nation state if the sub-division has separate legal personality (for example, a Local Authority) and it does not include any legal entity owned by a sovereign nation state (see "Sovereign-owned Entity").	No, not covered by Memorandum.
Sovereign Wealth Fund. A legal entity, often created by a special statute and normally wholly owned by a Sovereign, established to manage assets of or on behalf of the Sovereign, which may or may not hold those assets in its own name. Such an entity is often referred to as an "investment authority". For certain Sovereigns, this function is performed by the Central Bank, however for purposes of this Appendix B the term "Sovereign Wealth Fund" excludes a Central Bank.	No, not covered by Memorandum.
Sovereign-Owned Entity. A legal entity wholly or majority-owned by a Sovereign, other than a Central Bank, or by a State of a Federal Sovereign, which may or may not benefit from any immunity enjoyed by the Sovereign or State of a Federal Sovereign from legal proceedings or execution against its assets. This category may include entities active entirely in the private sector without any specific public duties or public sector mission as well as statutory bodies with public duties (for example, a statutory body charged with regulatory responsibility over a sector of the domestic economy). This category does not include local governmental authorities (see "Local Authority").	No, not covered by Memorandum.
State of a Federal Sovereign. The principal political sub-division of a federal Sovereign, such as Australia (for example, Queensland), Canada (for example, Ontario), Germany (for example, Nordrhein-Westfalen) or the United States of America (for example, Pennsylvania). This category does not include a Local Authority.	No, not covered by Memorandum.