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May 30, 2000

To: The Institutions that are Members of the Foreign
Exchange Committee and/or the Financial
Markets Lawyers Group (organizations independent
of but sponsored by the Federal Reserve Bank of New York),
33 Liberty Street,
New York, New York 10045.

Re: 1999 Collateral Annex to the International Foreign Exchange
and Options Master Agreement, International Foreign Exchange
Master Agreement and International Currency Options Market
Master Agreement published by the Foreign Exchange Committee
(the "*Collateral Annex*")

Ladies and Gentlemen:

You have asked for our opinion under the laws of the State of New York and the Federal laws of the United States of America as to certain matters relating to provisions of a Collateral Annex forming a part of an agreement entered into upon the terms of the February 1997 International Foreign Exchange and Options Master Agreement ("*FEOMA*"), International Foreign Exchange Master Agreement ("*1997 IFEMA*") or International Currency Options Market Master Agreement ("*1997 ICOM*"), the 1993 International Foreign Exchange Master Agreement ("*1993 IFEMA*") or the 1992 International Currency Options Market Master Agreement ("*1992 ICOM*") published by The Foreign Exchange Committee, in association with the British Bankers Association, the Canadian Foreign Exchange Committee and the Tokyo Foreign Exchange Market Practices Committee. In particular, we have considered (1) the validity and enforceability

of the form of Collateral Annex, (2) the effectiveness of the terms of the form of Collateral Annex to create in favor of the pledgee under a Collateral Annex (the "Secured Party") a valid and perfected security interest in Collateral consisting of U.S. Dollar-denominated deposits ("U.S. Dollar Collateral") and security entitlements in U.S. Treasury securities ("U.S. Treasury Securities Collateral" and, together with the U.S. Dollar Collateral, "Collateral"), posted under a Collateral Annex, (3) whether a transfer of such Collateral to the Secured Party could be avoided or rescinded as a fraudulent conveyance or preference in an insolvency proceeding in respect of the pledgor of such Collateral (the "Pledgor"), and (4) whether foreclosure by the Secured Party on Collateral pledged pursuant to a Collateral Annex would be prevented by operation of a stay or similar provision under the applicable insolvency law.

In this opinion, we refer to a master agreement entered into pursuant to the terms of the FEOMA, the 1997 IFEMA, the 1997 ICOM, the 1993 IFEMA or the 1992 ICOM as a "Master Agreement". As used in this opinion, (i) "UCC" means the Uniform Commercial Code as in effect on the date hereof in the State of New York; (ii) "adverse claim", "certificated security", "control", "investment property", "proceeds" and "security entitlement" have the meanings ascribed to such terms in Articles 8 and 9 of the UCC and, to the extent defined or incorporated into the Federal Book-Entry Regulations, also as defined or incorporated therein; and (iii) "Federal Book-Entry Regulations" means the Federal regulations contained in Subpart B ("Treasury/Reserve Automated Debt Entry System (TRADES)") governing Book-Entry Securities consisting of U.S. Treasury bonds, notes and bills and Subpart D ("Additional Provisions") of 31 C.F.R. Part 357, 31 C.F.R. § 357.10 through § 357.14 and § 357.41 through § 357.44 (including related defined terms in 31 C.F.R. § 357.2). Other capitalized terms used in this opinion and not otherwise defined are used with the meanings given to them in the form of Collateral Annex.

This opinion is limited to the Federal laws of the United States and the laws of the State of New York, and we are expressing no opinion as to the effect of the laws of any other jurisdiction.

1. *Parties Covered by This Opinion*

This opinion addresses the matters presented below with respect to the following insolvency laws and proceedings in respect of the following types of Parties:

(a) *Bankruptcy Code Entities.* A bankruptcy proceeding under Title 11 of the U.S. Code (the "Bankruptcy Code") with respect to an individual, partnership or corporation with a domicile, place of business or property in the United States (each, a "Bankruptcy Code entity"), but not

with respect to a municipality, governmental unit, small business investment company, trust (other than a trust that constitutes a "business trust"), a railroad or a domestic or foreign bank or insurance company.¹

(b) *Insured Depository Institutions.* A conservatorship or receivership conducted by the Federal Deposit Insurance Corporation (the "FDIC") under the Federal Deposit Insurance Act, as amended (the "FDIA"), in respect of a national bank, a District bank (*i.e.*, a bank formed under the laws of the District of Columbia), a federally licensed branch of a foreign bank (a "federal branch"), a federally chartered savings association, a state-chartered bank, a state-licensed branch of a foreign bank (a "state branch") or a state-chartered savings association, the deposits of which, in each case, are insured by the FDIC. Each of the foregoing types of institution is referred to in this opinion as an "insured depository institution".

(c) *Uninsured National Banks.* A conservatorship or receivership conducted by the Office of the Comptroller of the Currency (the "OCC") under the Bank Conservation Act, as amended, or the receivership provisions of the National Bank Act, as amended (collectively, the "National Bank Act"), in respect of (i) an uninsured national bank, or (ii) an insured national bank when the FDIC is not appointed and does not appoint itself as conservator or receiver.

¹ Subchapter III of Chapter 7 of the Bankruptcy Code, together with the provisions of the Securities Investor Protection Act, as amended ("SIPA"), establish special provisions applicable to the insolvency of a broker or dealer that carries customer accounts insured by the Securities Investor Protection Corporation ("SIPC"). SIPA provides that, to the extent consistent with SIPA, "a liquidation proceeding shall be conducted in accordance with, and as though it were being conducted under chapters 1, 3 and 5 and subchapters I and II of chapter 7 of" the Bankruptcy Code. 15 U.S.C. § 78fff(b). We are unaware of any cases that address the application of the provisions of the Bankruptcy Code governing the treatment of agreements and transactions such as a Master Agreement or Collateral Annex in the context of a proceeding conducted under SIPA. However, we do not believe that those provisions would be inconsistent with SIPA. Furthermore, in contrast to other provisions of the Bankruptcy Code addressing the treatment of certain types of trading transactions in bankruptcy, such as Section 555 of the Bankruptcy Code (relating to securities contracts) and Section 559 of the Bankruptcy Code (relating to repurchase agreements), Section 560 of the Bankruptcy Code, which relates to swap agreements, does not contain a provision permitting SIPC to bar the exercise of termination and setoff rights by a counterparty following the commencement of a bankruptcy proceeding in respect of a broker-dealer. Accordingly, we believe that those portions of this opinion that address the treatment of Bankruptcy Code entities should be equally applicable to brokers and dealers that are liquidated under SIPA.

(d) *Non-U.S. Banks with Uninsured Federal Branches and Federal Agencies of Foreign Banks.* A receivership conducted by the OCC under Section 4(j)(2) of the International Banking Act of 1978, as amended (the "IBA") in respect of an uninsured federal branch or a federally licensed agency of a non-U.S. bank (a "federal agency") or an insured federal branch or agency when the FDIC is not appointed and does not appoint itself as conservator or receiver.

(e) *Uninsured New York-Chartered Banks.* A receivership conducted by the New York State Superintendent of Banks (the "Superintendent") under Article XIII of the New York Banking Law (the "NYBL") in respect of (i) a New York state-chartered depository institution that does not hold deposits that are insured by the FDIC, or (ii) an insured state-chartered bank when the FDIC is not appointed and does not appoint itself as conservator or receiver.

(f) *Non-U.S. Banks with Uninsured New York-Licensed Branches and New York-Licensed Agencies of Foreign Banks.* A receivership conducted by the Superintendent under Article XIII of the NYBL in respect of a New York-licensed branch of a foreign bank (a "New York branch") that does not hold deposits that are insured by the FDIC or a New York-licensed agency of a non-U.S. bank (a "New York agency") or an insured New York branch or agency when the FDIC is not appointed and does not appoint itself as conservator or receiver.²

2. *Assumptions*

In connection with the opinions set forth in this letter, we have, with your approval, assumed that:

² If a foreign bank maintains both a federally licensed branch or agency and a state-licensed branch or agency, any receivership initiated by the OCC in respect of the federally licensed branch or agency would supersede any state law proceeding in respect of the state-licensed branch or agency. Accordingly, the discussion in this opinion with respect to uninsured state-licensed branches and agencies assumes that no receivership has been initiated by the OCC with respect to any federal branch or federal agency of the same foreign bank.

Similarly, it is possible that an ancillary proceeding under the Bankruptcy Code may be commenced in respect of a non-U.S. banking organization that maintains branches or agencies in the United States, and that the ancillary proceeding would supersede the specialized receivership provisions described in this letter. Accordingly, the discussion of federal and state receivership provisions with respect to U.S. branches and agencies of non-U.S. banks assumes that no ancillary proceeding has been commenced that would supersede the branch or agency receivership proceedings.

(a) Each Party has been duly incorporated and is existing and, to the extent applicable, in good standing under the laws of the jurisdiction of its formation.

(b) The Master Agreement and each FX Transaction or Option Transaction (collectively, "*Transactions*") constitute valid and legally binding obligations of each of the Parties enforceable in accordance with their terms under applicable law.

(c) The Collateral Annex is within the capacity of, and has been duly authorized and validly executed and delivered by, each of the Parties and, except for purposes of the opinions set forth in paragraph 3 below, the Collateral Annex constitutes a valid and legally binding obligation of each of the Parties enforceable in accordance with its terms under applicable law.

(d) In the case of a Master Agreement or Collateral Annex to which an insured depository institution is a party, (i) such Master Agreement, each Transaction and such Collateral Annex are evidenced by a writing sent reasonably contemporaneously with the Parties' agreement to enter into the Master Agreement, Transaction or Collateral Annex, as applicable; (ii) the insured depository institution is authorized under applicable non-insolvency law to enter into the Master Agreement, Transaction or Collateral Annex, as applicable, as evidenced by a resolution (or extract thereof) certified to the other Party by a secretary or assistant secretary of the insured depository institution or a written representation to the other Party of a bank officer of the level of vice president or above relied on by the other Party in good faith, (iii) such Master Agreement, Transaction and Collateral Annex are maintained by the insured depository institution among its official books and records, and (iv) the other Party has maintained a copy of the written agreements and evidence of authority referred to in (i) and (ii) above.

(e) The U.S. Treasury Securities Collateral is held by the Secured Party in a securities account with a securities intermediary pursuant to an agreement between the Secured Party and such securities intermediary that (i) specifies that such agreement is to be governed by New York law, or (ii) does not specify a governing law but expressly specifies that the securities account is to be maintained in the State of New York, or (iii) otherwise causes New York law to be the law of the "securities intermediary's jurisdiction" as provided in Section 8-110(e) of the UCC.

(f) The U.S. Dollar Collateral is held by the Secured Party in a bank account with a bank located within the State of New York over

which the Secured Party has exclusive dominion and control, as described in *Annex B* to this opinion.

(g) As represented by each Party in the Master Agreement, the Master Agreement (including the Collateral Annex) and each Transaction are entered into, and each delivery of Collateral made under the Collateral Annex is made, by each Party acting as principal and, as a result, all of the obligations under the Master Agreement (including the Collateral Annex) are mutual.

(h) The Master Agreement (including the Collateral Annex) and each Transaction are entered into, and all deliveries of Collateral made under the Collateral Annex are made, prior to the commencement of any insolvency proceedings against either Party.

(i) Each Transaction is a foreign exchange spot, forward or option transaction that constitutes a "swap agreement" for purposes of the Bankruptcy Code and the FDIA and a "qualified financial contract" for purposes of the NYBL and the FDIA (a "QFC").

(j) No substantive modifications have been made by the Parties to the Master Agreement or the Collateral Annex except for completion of the Schedules thereto and, in the case of any Master Agreement entered into on the 1993 IFEMA or 1992 ICOM form of agreement, the making of the modifications to the Collateral Annex specified in *Annex A* to this opinion required to accommodate the terms of such forms.

(l) The Schedules to the Master Agreement and the Collateral Annex have been properly completed by both Parties and do not include any provisions that modify, limit or add to the substantive provisions of the Collateral Annex.

(m) At the time of execution and delivery of the Master Agreement, the Collateral Annex and each Transaction, there will not have occurred any change in law affecting the validity, legally binding character or enforceability of the Master Agreement, Collateral Annex or Transaction or the security interests created thereby.

(n) The performance by each Party of its obligations under the Master Agreement, the Collateral Annex and any Transaction and the delivery of any Collateral under the Collateral Annex will comply with applicable law and with any requirement or restriction imposed by any court or governmental body having jurisdiction over such Party and will

not result in a default under or a breach of any agreement or instrument then binding upon such Party.

(o) Neither the Master Agreement, the Collateral Annex nor any Transaction is entered into, and no transfer of Collateral is made, by either Party with the intent to hinder, delay or defraud the creditors of either Party.

(p) With respect to the opinions set forth in paragraph 7, all conditions necessary to the termination of the Transactions in accordance with the terms of the Master Agreement have occurred, including, in the case of an insured depository institution, the conditions applicable under the FDIA.

3. *Enforceability of the Collateral Annex*

Based on and subject to the foregoing and subject also to the comments and qualifications set forth below, it is our opinion that, if the Parties have entered into a Collateral Annex governed by New York law, the Collateral Annex will constitute the valid and legally binding obligation of each Party enforceable against such Party in accordance with its terms, subject to bankruptcy, insolvency, conservatorship, receivership, fraudulent transfer, reorganization, moratorium and similar laws of general applicability relating to or affecting creditors' rights and to general equity principles.

4. *Validity of Security Interest*

Based on and subject to the foregoing and subject also to the comments and qualifications set forth below, it is our opinion that, if the Parties have entered into a Collateral Annex governed by New York law, the Collateral Annex will be effective to create in favor of the Secured Party a valid security interest in all right, title and interest of the Pledgor in and to the Collateral, except that, in the case of U.S. Treasury Securities Collateral, such security interest will continue in such Collateral after its sale, exchange or other disposition and in any proceeds thereof to the extent, but only to the extent, provided in Sections 9-306 of the UCC.³

³ If any of such proceeds consist of U.S. Dollars and such U.S. Dollars are held by the Secured Party in the manner described in *Annex B*, the security interest of the Secured Party in such proceeds would be valid and perfected in the same manner as any other U.S. Dollar Collateral held by the Secured Party under the Collateral Annex, as described in this opinion.

5. *Perfection of Security Interests in U.S. Treasury Securities Collateral*

(a) Based on and subject to the foregoing and subject also to the comments and qualifications set forth below, it is our opinion that, the security interest referred to in paragraph 4 above in the types of Collateral described below will be perfected:

(i) in the case of U.S. Treasury Securities Collateral, upon the attachment thereof, when the Transfer of such security entitlement to the Secured Party is effective as provided in Section 2.2(b) of the Collateral Annex; and

(ii) to the extent not expressly covered by subparagraph (i) above, in that portion of the Collateral consisting of proceeds, as and to the extent provided in Section 9-306 of the UCC of any such U.S. Treasury Securities Collateral.⁴

(b) Based on and subject to the foregoing and subject also to the comments and qualifications set forth below, it is our opinion that, with respect to the security interest referred to in paragraph 4 above in any Collateral perfected as described in paragraph 5(a)(i) above, if such security interest is perfected by the Secured Party in the manner specified in paragraph 5(a)(i) above without notice of any adverse claim to such Collateral,⁵ such perfected security interest will have priority over all other security interests created in such Collateral under the UCC in favor of any creditor that has not obtained control of such Collateral, and will rank equally with the security interest of any other creditor in such Collateral that has also obtained control (except any creditor that is the securities intermediary on whose books a security entitlement has been created or a securities account established, which, in the absence of agreement to the contrary, will have priority over any other creditor with control of such Collateral).

⁴ Please see footnote 3 above with respect to proceeds that consist of U.S. Dollars and are held by the Secured Party in the manner described in *Annex B*.

⁵ The UCC provides that, subject to several qualifications, a person has "notice of an adverse claim" if "(1) the person knows of the adverse claim; (2) the person is aware of facts sufficient to indicate that there is a significant probability that the adverse claim exists and deliberately avoids information that would establish the existence of the adverse claim; or (3) the person has a duty, imposed by statute or regulation, to investigate whether an adverse claim exists, and the investigation so required would establish the existence of the adverse claim". UCC § 8-105(a). The filing of a financing statement under Article 9 of the UCC would not be notice of an adverse claim to U.S. Treasury Securities Collateral. *Id.* § 8-105(b).

6. *Security Interests in "Cash" Collateral*

Pursuant to Section 2.2(a) of the Collateral Annex, the Pledgor has agreed to deliver any U.S. Dollar Collateral to the Secured Party by causing such funds to be credited to one or more accounts specified by the Secured Party or its agent. As noted above, we have assumed that such accounts will be bank accounts (each, a "Cash Collateral Account") held by the Secured Party in a bank located within the State of New York, and that the Secured Party will have exclusive dominion and control over such Cash Collateral Accounts. The Pledgor will have no right to make any withdrawal from the Cash Collateral Account. The Secured Party is required to return U.S. Dollar Collateral from the Cash Collateral Account only in the circumstances specified in Sections 3.3 and 5.1 of the Collateral Annex.

Security interests in U.S. Dollar Collateral held in the State of New York are not governed by the UCC, and instead are governed by the common law of the State of New York. There have been no recent judicial decisions regarding such security interests, and we are not aware of any judicial decision by New York courts, or federal courts applying New York law, that has considered contractual provisions such as those contained in the Collateral Annex in respect of the administration of the Cash Collateral Account. However, we have set forth in *Annex B* our analysis of the reasoning of the cases that we have examined and the statutory and judicial purposes of the perfection of a security interest. Based on and subject to the foregoing and to the analysis set forth in such *Annex B* and subject also to the comments and qualifications set forth below, it is our opinion that the provisions of the Collateral Annex should be effective to create in favor of the Secured Party a valid security interest in any U.S. Dollar Collateral deposited into the Cash Collateral Account, and such security interest should be senior to the rights of a person who obtains a lien granted by the pledgor on, or a person who obtains (or who is deemed to obtain) a judicial lien on, or an execution against, the property of the pledgor after the Transfer of such U.S. Dollar Collateral into the Cash Collateral Account.

7. *Ability to Retain, Liquidate and Apply Collateral*

(a) *Bankruptcy Code Entities*

If the Pledgor is a Bankruptcy Code entity, it will be necessary to consider the provisions of the Bankruptcy Code that permit a trustee in bankruptcy to avoid transfers of property by the Pledgor prior to the commencement of a bankruptcy case or that limit the right of a secured party to exercise rights against the Pledgor after the commencement of a bankruptcy case.

(1) *Avoidance of Transfers of Collateral.*

A trustee in bankruptcy may avoid transfers of collateral made by a debtor prior to the commencement of a bankruptcy case under several circumstances.

Fraudulent Transfers. Under Section 548(a) of the Bankruptcy Code, a trustee in bankruptcy may avoid a "fraudulent transfer", *i.e.*, any transfer of an interest of a debtor in property or obligation incurred by the debtor that is made or incurred within one year before the filing of a petition under the Bankruptcy Code if (i) the debtor made such transfer or incurred such obligation with actual intent to hinder, delay or defraud present or future creditors or (ii) the debtor received less than a "reasonably equivalent value" (*i.e.*, "fair consideration") in exchange for the transfer and the debtor (a) was insolvent on the date the transfer was made or became insolvent as a result thereof, (b) was engaged in business or in a transaction, or was about to do so, for which any property remaining with the debtor was an unreasonably small capital, or (c) intended to incur or believed that it would incur debts beyond its ability to pay as they matured.

In addition, under Section 544(b) of the Bankruptcy Code, a trustee in bankruptcy may avoid a transfer made prior to the filing of a bankruptcy petition if the transfer could be avoided by an unsecured creditor under applicable state law. As noted above, we express no opinion with respect to the law of any state other than the State of New York. The fraudulent transfer law of New York is generally similar to Section 548 of the Bankruptcy Code except that (i) a transfer or obligation for which the debtor does not receive fair consideration may also be avoided if the debtor is a defendant in an action that results or has resulted in an unsatisfied judgment against the debtor and (ii) in general, the period during which transfers may be avoided is six years prior to the commencement of the bankruptcy case, rather than the one-year period specified in the Bankruptcy Code.

Section 548(d)(2)(A) provides that "'value' means property, or satisfaction or securing of a present or antecedent debt of the debtor". The fraudulent transfer law of New York contains a similar provision. Accordingly, to the extent that transfers of Collateral pursuant to the Collateral Annex are made to secure present or antecedent debt of the Pledgor, such transfers will be transfers for value.

Furthermore, Section 548(d)(2)(D) provides that a "swap participant" that receives a transfer in connection with a swap agreement takes for value to the extent of such transfer. For purposes of this provision, both the Pledgor and the Secured Party will be "swap participants" with respect to the Master Agreement that includes the Collateral Annex, the Secured Party will receive such transfers

of collateral in connection with a swap agreement between the Secured Party and the Pledgor, and, accordingly, the Secured Party will receive such transfers of collateral "for value" to the extent of such transfers. The New York fraudulent transfer law does not contain a comparable provision.

Finally, the effect of both Sections 544 and 548(a) is limited by Section 546(g) of the Bankruptcy Code, which provides that, notwithstanding Sections 544 and 548, a trustee may not avoid a transfer that is made before the commencement of the case under a swap agreement, by or to a swap participant, in connection with a swap agreement except for a transaction that is voidable under Section 548(a)(1) because it was made with actual intent to hinder, delay or defraud creditors of the debtor. Section 546(g) "is intended to protect normal transfers of collateral made in connection with a swap agreement". See 136 Cong. Rec. S7535 (daily ed. June 6, 1990).

Accordingly, based on and subject to the foregoing and the assumptions set forth in Paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that an attempt by a trustee in bankruptcy, or a party asserting the rights of a trustee in bankruptcy, to set aside any transfer of Collateral made by the Pledgor to the Secured Party under the Collateral Annex as a fraudulent transfer under Sections 544 or 548 of the Bankruptcy Code should not be successful.

Preferences. Under Section 547 of the Bankruptcy Code, a trustee in bankruptcy may avoid a "preference", *i.e.*, any transfer of an interest of a debtor in property (1) to or for the benefit of a creditor, (2) for or on account of a debt owed by the debtor before such transfer was made, (3) made while the debtor was insolvent, (4) made within 90 days before the filing of a petition under the Bankruptcy Code (or one year if the creditor was an "insider" of the debtor), and (5) that enables such creditor to receive more than such creditor would receive if the bankruptcy case were a case under Chapter 7 of the Bankruptcy Code, the transfer had not been made, and such creditor received payment of such debt to the extent provided by the provisions of the Bankruptcy Code.

Section 546(g) of the Bankruptcy Code provides that, notwithstanding Section 547 of the Bankruptcy Code, a trustee may not avoid a transfer made before the commencement of the case under a swap agreement, by or to a swap participant, in connection with a swap agreement, except under Section 548(a)(1) of the Bankruptcy Code. Accordingly, Section 546(g) would prohibit the trustee from avoiding as preferences any transfers of Collateral pursuant to the Collateral Annex, which transfers will be made in connection with swap agreements between the Pledgor and the Secured Party, pursuant to Section 547. As mentioned above, the legislative history confirms that Section 546(g) would apply to a transfer of Collateral under the Collateral Annex.

Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that Section 546(g) of the Bankruptcy Code should prevent a trustee in bankruptcy, or a creditor asserting the rights of a trustee in bankruptcy, from setting aside any transfer of Collateral made by the Pledgor to the Secured Party under the Collateral Annex as a preference under Section 547 of the Bankruptcy Code.

(2) *Limitations on Exercise of Rights Against Collateral.*

Under Section 362 of the Bankruptcy Code, the filing of a petition for relief under the Bankruptcy Code generally operates as a stay of any act to create, perfect or enforce any lien against property of the debtor or the setoff of any debt owing to the debtor that arose before the petition against any claim against the debtor. However, Section 362(b)(17) of the Bankruptcy Code provides that Section 362(a) shall not stay the setoff by a swap participant of any mutual debt and claim under or in connection with any swap agreement that constitutes the setoff of a claim against the debtor for any payment due from the debtor under or in connection with any swap agreement against cash, securities or other property of the debtor held by or due from such swap participant to guarantee, secure or settle any swap agreement.⁶

In addition, Section 560 of the Bankruptcy Code expressly permits a swap participant to exercise a contractual right to terminate a swap agreement and to offset or net out any termination values or payment amounts owed under it despite the counterparty's insolvency. The Collateral Annex provides that, in the case of the Pledgor's default, the Secured Party may set off the obligations of the Pledgor pursuant to or in connection with the Master Agreement against the cash or other property of the Pledgor pledged to the Secured Party pursuant to the Collateral Annex.

Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that the liquidation of Collateral under and in accordance with the Collateral Annex, and the setoff of the

⁶ Because collateral posted by or to the debtor must be "held by or due from" a swap participant, and "swap participant" is defined to include only those entities that have swap agreements "with the debtor", 11 U.S.C. § 101(53C) (emphasis added), these provisions protect a secured party only with respect to collateral posted by the debtor itself to secure its own obligations. If the collateral is posted by a debtor to secure another party's obligations under a Master Agreement, these protective provisions of the Bankruptcy Code would not be applicable.

obligations of the Pledgor to the Secured Party under or in connection with the Master Agreement against Collateral pledged to the Secured Party pursuant to the Collateral Annex, should not be subject to the automatic stay imposed by Section 362(a) of the Bankruptcy Code.

(b) *Insured Depository Institutions*

If the Pledgor is an insured depository institution, it will be necessary to consider the provisions of the FDIA that permit a conservator or receiver to avoid transfers of property by the Pledgor prior to the appointment of the conservator or receiver or that limit the right of a secured party to exercise rights against the Pledgor after the appointment of the conservator or receiver.

(1) *Avoidance of Transfers of Collateral.*

Avoidance Powers of the FDIC Generally. The FDIA does not contain independent "preference" provisions that apply to transfers of assets by the insolvent institution. However, if the FDIC is acting as conservator or receiver for an insolvent national bank (or, it appears, if it has been appointed by a Federal banking agency or itself as conservator or receiver for an insured New York bank), it can avoid preferential transfers to the extent provided in the National Bank Act as described below. If the FDIC has been appointed as conservator or receiver for an insolvent New York bank by the Superintendent, it can avoid preferential transfers to the extent provided in the NYBL as described below.

The FDIA, National Bank Act and NYBL also do not contain independent fraudulent transfer provisions that apply to transfers of assets by an insolvent institution. However, although we have not identified cases in which such a claim has been raised, there is a possibility that a receiver or conservator appointed under the National Bank Act or the NYBL — and hence the FDIC — also may be able to assert the rights of a creditor under the New York fraudulent conveyance law described above.⁷ If that is the case, it is unlikely that other creditors of a bank could exercise such rights.⁸ If not, then it is likely that such other creditors would be permitted to do so.

⁷ "[W]hen the assignee, trustee or whatever he may be called, derives his authority . . . from the mandate of the law . . . in the interest of creditors, he represents the latter and is vested with their powers.' We may take it as true, then, that the statutory liquidator has the right to set aside a fraudulent conveyance." Garrard Glenn, *Fraudulent Conveyances and Preferences* § 101b (1940). *But see Federation Bank & Trust Co. v. Hammons*, 26 N.Y.S.2d 56 (1941) (Superintendent is limited to powers specified in statute).

⁸ *Cf. 5 Collier on Bankruptcy* ¶ 544.09[2] at 544-17, -18 (Lawrence P. King ed., 15th ed. 1996).

However, Section 11(e)(11) of the FDIA, 12 U.S.C. § 1821(e)(11), provides that the FDIC generally may not avoid any “legally enforceable or perfected security interest” in the assets of a failed institution, unless that interest was “taken in contemplation of the institution’s insolvency or with the intent to hinder, delay or defraud the institution or the creditors of such institution”. *Id.* § 1821(e)(11). Furthermore, with respect to QFCs, the FDIA specifically provides that the FDIC, as conservator or receiver, “may not avoid any transfer of money or other property in connection with any qualified financial contract with an insured depository institution” unless the transferee had “actual intent to hinder, delay or defraud such institution, the creditors of such institution, or any conservator or receiver appointed for such institution”, *id.* § 1821(e)(8)(C)(i). Thus, the FDIC would not have the right to avoid the grant by the Pledgor of a security interest in, or a transfer by the Pledgor of, Collateral to the Secured Party unless the FDIC determines that the Secured Party had actual intent to hinder, delay or defraud the institution, its creditors or any conservator or receiver appointed for the institution. *Id.* § 1821(c)(ii).

The FDIC has concluded that Section 11(e)(11) does not prevent it from exercising its right to repudiate a secured obligation under Section the FDIA, but has acknowledged that a “legally enforceable or perfected” security interest in favor of a party to a contract with an insured depository institution would remain in place securing the counterparty’s claim for damages arising out of such repudiation. Any amount by which the value of the collateral exceeds the amount of the counterparty’s claim would revert to the FDIC, in its capacity as conservator or receiver. Accordingly, if the FDIC were to repudiate a Master Agreement that was secured by Collateral posted under a Collateral Annex, the Secured Party would retain a security interest in the Collateral to the extent of the Secured Party’s claim in respect of the repudiated Master Agreement.

Requirements of D’Oench Duhme and Section 1823(e). The rights of counterparties to a QFC to obtain the benefits of collateral are subject to the requirement that the security interest be “legally enforceable” to obtain the benefits of collateral. The FDIC has stated that this requirement requires both that the agreement be enforceable as a matter of applicable non-insolvency law and that the agreement satisfy the applicable requirements of the *D’Oench Duhme* doctrine and Section 13(e) of the FDIA. *See Statement of Policy Regarding Treatment of Security Interests After Appointment of the FDIC as Conservator or Receiver*, 58 Fed. Reg. 16833, 16844 (Mar. 31, 1993) (the “*Security Interests Policy Statement*”).

The Supreme Court adopted the *D’Oench Duhme* doctrine in 1942 as a means of preventing the enforcement of “secret agreements” against the interests of an insolvent insured depository institution. *See D’Oench, Duhme & Co. v. Federal Deposit Insurance Corporation*, 315 U.S. 442 (1942). In that decision, the Supreme Court stated that a contract, even if otherwise legally enforceable, could

not be enforced against the FDIC if the agreement was against the interests of an insolvent institution and was not reflected in the books and records of the institution. *Id.* at 461. This doctrine has been progressively broadened over the years, and Section 13(e) of the FDIA, 12 U.S.C. § 1823(e), further substantially broadened the power of the FDIC, as conservator or receiver for an insured depository institution, to avoid a contract against the interests of the institution. Under Section 13(e) of the FDIA, no contract may be enforced against the FDIC, as conservator or receiver, unless it (i) is in writing, (ii) was executed by the institution and the other party "contemporaneously" with the acquisition of the related asset by the depository institution, (iii) was approved by the board of directors of the depository institution or its loan committee (and such approval is reflected in the minutes of such body), and (iv) has been, since its execution, an official record of the depository institution. *Id.* § 1823(e).

The FDIC has, however, adopted a policy statement that provides protection to QFCs and security arrangements relating to QFCs. See *Policy Statement Regarding Qualified Financial Contracts* (Dec. 12, 1989) (the "QFC Policy Statement"). In the QFC Policy Statement, the FDIC stated that "[a]ny QFC (including any ancillary agreements, such as a master agreement or security agreements) that complies with the [criteria set forth in the QFC Policy Statement] will be deemed to satisfy the requirements set forth in Sections 11(d)(9), 11(n)(4)(I) and 13(e) of the" FDIA. As noted above, we have been advised and are assuming that such requirements will be satisfied with respect to each Master Agreement, Transaction and Collateral Annex.

The Collateral Annex will also have the benefits of the Security Interests Policy Statement, which applies to all security arrangements, not only those relating to QFCs. In the Security Interests Policy Statement, the FDIC confirmed that it would not seek to "avoid an otherwise legally enforceable and perfected security interest solely because the secured obligation or the collateral subject to such security interest (a) was not acquired by the Institution contemporaneously with the approval and execution of the security agreement granting the security interest and/or (b) may change, increase, or be subject to substitution from time to time during the period that the security interest is enforceable and perfected", provided that (a) the agreement was undertaken in the ordinary course of business, not in contemplation of insolvency, and with no intent to hinder, delay or defraud the institution or its creditors; (b) the secured obligation represents a bona fide and arm's length transaction; (c) the secured party or parties are not insiders or affiliates of the institution; (d) the grant or creation of the security interest was for adequate consideration; and (e) the security agreement evidencing the security interest satisfies the other requirements of Section 13(e)(1). See *Security Interests Policy Statement*, 58 Fed. Reg. at 16834. The FDIC noted in this policy statement that this position is consistent with its prior

advisory opinions, FDIC Advisory Opinion 4423 (Dec. 25, 1989) and FDIC Advisory Opinion 4537 (Apr. 2, 1991). The FDIC also noted that this policy statement should not be "interpreted as contradicting or impairing the policies expressed" in the QFC Policy Statement, 58 Fed. Reg. at 16833, and accordingly, if a QFC satisfies the provisions of the QFC Policy Statement, it should also satisfy the requirements specified in clause (e) above. Thus, the Collateral Annex would have the benefit of both the QFC Policy Statement and whatever additional protection the Security Interests Policy Statement may provide.

Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that the FDIC, as conservator or receiver, should not have the authority under the FDIA to avoid the creation of the security interests granted by the Pledgor under the Collateral Annex or any transfer of Collateral made pursuant to the Collateral Annex before the appointment of the FDIC as conservator or receiver.

(2) *Limitations on Exercise of Rights Against Collateral.*

Section 11(e)(8)(A) and (E) of the FDIA provide that, subject only to the right of the FDIC to transfer or repudiate a QFC, a party to a QFC is not stayed from exercising "any right under any security arrangement" relating to a QFC or "any right to offset or net out any . . . transfer obligation" arising under one or more QFCs. Section 11(e)(8)(B), however, provides that the party's ability to exercise such rights after appointment of a receiver is subject to the limited "stay" imposed by Section 11(d)(12) of the FDIA.

Under Section 11(d)(12) of the FDIA, the FDIC may, after its appointment as conservator or receiver for an insured depository institution, request a stay in any judicial action to which the insured depository institution is or becomes a party. This stay extends for 45 days in the case of a conservatorship and for 90 days in the case of a receivership. 12 U.S.C. § 1821(d)(12). As a matter of practice, the FDIC routinely obtains such stays at the time of its appointment as either conservator or receiver. However, unlike the broader stay provisions of the Bankruptcy Code, the FDIC's stay applies only to judicial actions to which the depository institution is or becomes a party.

The FDIC's general counsel opined in 1989 that, given the absence of a generalized "stay" under the FDIA, a party (other than an affiliate of the depository institution) to a *bona fide*, arm's length contract would be permitted to liquidate collateral held by it as security for obligations of an insured depository institution even after the FDIC is appointed as receiver or conservator for that institution, provided that, in the case of a conservatorship, the right to so liquidate arose as a result of a default other than an "ipso facto" provision in the

contract. See *Self-Help Liquidation of Collateral by Secured Claimants in Insured Depository Institution Receiverships*, 1989 FDIC Interp. Ltr. LEXIS 69 (Dec. 15, 1989). The FDIC has affirmed this view more recently in its policy statements relating to collateralized letters of credit and collateralized put obligations. See *Statement of Policy Regarding Treatment of Collateralized Letters of Credit After Appointment of the FDIC as Conservator or Receiver* (May 19, 1995); *Statement of Policy Regarding Treatment of Collateralized Put Obligations After Appointment of the FDIC as Conservator or Receiver*, 56 Fed. Reg. 36152 (July 31, 1991).

Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that if the Secured Party is permitted to terminate the Master Agreement or the Master Agreement is repudiated by the FDIC, the Secured Party would be permitted to liquidate any Collateral then held by it pursuant to the Collateral Annex and apply such Collateral to the obligations of the Pledgor under the Master Agreement. Any remainder would be required to be turned over to the FDIC.

(c) *Uninsured National Banks*

If the Pledgor is an uninsured national bank, or a national bank for which the FDIC is not appointed and does not appoint itself as conservator or receiver, the liquidation of the Pledgor would be governed by the National Bank Act (as defined above).

(1) *Avoidance of Transfers of Collateral.*

Preferences. Under Section 91 of the National Bank Act, any transfer of the assets of a national bank and all payments of money to its shareholders or creditors "made after the commission of an act of insolvency, or in contemplation thereof, made with a view to prevent the application of its assets in the manner prescribed by this chapter, or with a view to the preference of one creditor to another . . . shall be utterly null and void." 12 U.S.C. § 91. Section 194 of the National Bank Act requires that the OCC (or the receiver appointed by the OCC) distribute the proceeds of the liquidation of a national bank "ratabl[y]" to creditors. *Id.* § 194; see *Texas American Bancshares, Inc. v. Clarke*, 954 F.2d 329 (5th Cir. 1992). The courts have found that a pledge of collateral made prior to a bank's insolvency, and not in contemplation of insolvency, is not rendered invalid by the "ratable distribution" requirements of Sections 91 and 194. See *Scott v. Armstrong*, 146 U.S. 499, 510 (1892); OCC Interpretive Letter #768 (Oct. 4, 1995). However, these provisions generally invalidate transfers of collateral made after an act of insolvency or in contemplation of insolvency – whether or not a conservator or receiver has yet been appointed and, in most cases, whether

or not the recipient of the transfer had any knowledge of the act or contemplation of insolvency or had any intention to be preferred.

A national bank is "not in contemplation of insolvency until the fact becomes reasonably apparent to its officers that it will presently be unable to meet its obligations, and will be obliged to suspend its ordinary operations." "Acts of insolvency" include the adoption by the directors of a bank of a resolution to suspend its operations, a failure by the bank to pay a deposit on demand or to meet its obligations at maturity, an admission by the bank or its officers that it is unable to satisfy its obligations when due or the appointment of a receiver or conservator for the bank. 10 Am. Jur. 2d § 762 at 725. Any transfer occurring after such an act, or when the officers know that insolvency cannot be avoided, is void.

Neither the National Bank Act nor the case law interpreting it provides an explicit or definitive exemption from this rule for "ordinary course" or "contemporaneous" transactions, nor are there explicit provisions of the National Bank Act protecting QFCs. However, an "ordinary course" transaction carried out by a national bank, even after the national bank is insolvent, may not be preferential under the National Bank Act, "if [it is] not made in contemplation of insolvency, with a view to prefer one creditor over another, or after an act of insolvency." 10 Am. Jur. 2d § 762 at 724. For example, in examining a series of payments made by a national bank that was in fact, insolvent, the Supreme Court noted that "a finding that the payments and remittances . . . were made in contemplation of insolvency and with an intent to prefer that bank" could not be

based on the mere allegation that the [national bank] was actually insolvent, and that its insolvency must have been known to its officers. It is a matter of common knowledge that banks and other corporations continue, in many instances, to do their regular and ordinary business for long periods, though in a condition of actual insolvency, as disclosed by subsequent events. It cannot surely be said that all payments made in the due course of business in such cases are to be deemed to be made in contemplation of insolvency, or with a view to prefer one creditor to another. Accordingly, a transfer made by a national bank, even after insolvency, should not be voidable under Section 91 if the "ordinary course" nature of the transfer and other facts and circumstances indicate that the transfer was not made with a view to prefer one creditor over another.

McDonald v. Chemical National Bank, 174 U.S. 610, 618 (189a).

The same reasoning has allowed courts to conclude that a pledge of securities to secure new indebtedness of the national bank may not be avoided as

a preference simply because the transfer occurred after the national bank was actually insolvent. The National Bank Act "does not . . . invalidate a pledge of its securities to a reasonable amount to raise money to meet an unexpected run, although the bank is then in fact insolvent, if it has not become reasonably apparent to its officers that it will presently be unable to meet its obligations and will be obliged to suspend its ordinary operations." 10 Am. Jur. 2d § 762 at 725. Thus, for example, such a pledge was valid, although the bank was then insolvent, because the insolvent bank "did not intend to pledge the securities as collateral to its antecedent indebtedness when it sent them . . . to the defendant, or for any purpose other than the advances which it then desired." *Armstrong v. Chemical National Bank*, 41 F. 234 (C.C.S.D.N.Y. 1890); cf. OCC Interpretive Letter #768, *supra* (finding that collateral arrangements made by federal branches and agencies in connection with multilateral foreign exchange-clearing house should not be voidable under Section 91 because they were not created "in contemplation of insolvency"). The OCC has suggested, in recent letters, that even collateral posted after an act of insolvency, or in contemplation thereof, should not be invalidated as a result of such act, so long as the security interest in such collateral is valid and perfected under applicable U.S. law and, "[a]t the time of its execution, the security agreement was not entered into in contemplation of the foreign bank's insolvency, or that of the branch or agency". See OCC Interpretive Letter #733 (June 19, 1996).

Accordingly, while the matter is not free from doubt (particularly in light of the absence of recent cases under Section 91), a transfer of Collateral by a national bank to secure indebtedness contemporaneously incurred should not constitute a "preference" for purposes of Section 91, so long as the transfer does not occur after an act of insolvency, or in contemplation thereof, or with a view to create a preference.

Fraudulent Transfers. The National Bank Act does not contain independent fraudulent transfer provisions that apply to transfers of assets by an insolvent national bank. However, as discussed above, although we have not identified cases in which such a claim has been raised, there is a possibility that a receiver or conservator appointed under the National Bank Act also may be able to assert the rights of a creditor under the New York fraudulent conveyance law described above (or comparable laws of other jurisdictions, if applicable). If that is the case, it is unlikely that other creditors of a bank could exercise such rights. If not, then it is likely that such other creditors would be permitted to do so. Accordingly, whether the rights under state fraudulent conveyance laws may be exercised by a conservator or receiver, or by another creditor, of a bank, it appears likely that a transferee of property from a national bank would be subject to the risk that such transfer could be avoided under the New York fraudulent transfer laws (or such comparable laws of other jurisdictions, if

applicable). Accordingly, to the extent that transfers of Collateral under the Collateral Annex are not made for a fair consideration, it would appear likely that such transfers could be avoided by the conservator or receiver, or by a creditor of the pledgor. To the extent that collateral is transferred for fair consideration, however, the conservator or receiver, or creditor, should not have the power to avoid such transfers as fraudulent transfers.

(2) *Limitations on Exercise of Rights Against Collateral.*

The National Bank Act does not grant a conservator or receiver a generalized stay against actions involving the insolvent institution. However, under the Bank Conservation Act, a conservator appointed by the OCC may request that any judicial action or proceeding to which the bank or the conservator is a party be stayed for up to 45 days after the appointment of the conservator, and the court is required to grant this request.⁹

The OCC has acknowledged that the National Bank Act does not permit a receiver appointed by the OCC to prevent a counterparty with a valid and perfected security interest from exercising its remedies under the collateral arrangement. *See* OCC Interpretive Letter #733, *supra*. While the OCC's letter expressly addressed only receiverships, we believe the OCC's reasoning in that letter applies equally to conservatorships.¹⁰ Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that, to the extent a Secured Party is permitted to retain Collateral as described in paragraph 7(c)(1) above, the Secured Party should be permitted to exercise its remedies with respect to such Collateral pursuant to the terms of the Collateral Annex and applicable law.

(d) *Non-U.S. Banks with Uninsured Federal Branches and Federal Agencies*

If the Pledgor is a non-U.S. bank that maintains an uninsured federal branch or a federal agency, the liquidation of the branch or agency (and any limitations under U.S. law on the Secured Party's ability to exercise its rights against the non-U.S. bank) will be governed by the IBA and the National Bank Act. Thus, in these cases, it will be necessary to consider the provisions of the

⁹ 12 U.S.C. § 203(b)(2).

¹⁰ The letter addressed only receiverships because it related to federal branches of non-U.S. banks, for which conservatorships are not available. However, the Bank Conservation Act, like the receivership provisions of the National Bank Act, does not contain provisions granting a conservator the authority to interfere with the rights of a secured party.

National Bank Act and the IBA, as applicable, that permit a conservator or receiver to avoid transfers of property by the Pledgor prior to the appointment of the conservator or receiver or that limit the right of a secured party to exercise rights against the Pledgor after the appointment of the conservator or receiver.

Under Section 4(j)(2) of the IBA, the provisions described in paragraph 7(c) above also apply in a receivership of a federal branch or federal agency of a non-U.S. bank. *See* OCC Interpretive Letter #733, *supra*. Thus, when a federal branch or agency of a non-U.S. bank pledges Collateral to secure its obligations under a Master Agreement, the same conclusions outlined in paragraph 7(c) above will apply.

However, Section 4(j)(1) of the IBA gives the OCC (or a receiver appointed by the OCC) the authority to seize all assets located in the United States of a non-U.S. bank with a federal branch or agency, as well as all assets worldwide that are "booked" in the federal branch or agency. Accordingly, if a non-U.S. bank has a federal branch or agency, the OCC, or its receiver, would have the authority to seize collateral posted by the non-U.S. bank if the collateral is located in the United States, even if the collateral does not secure obligations of the U.S. offices of the non-U.S. bank. Furthermore, Section 4(j)(2) of the IBA provides that, once the assets seized by the OCC, or its receiver, have been applied to satisfy "claims arising out of transactions had by [creditors of the non-U.S. bank] with any branch or agency of such foreign bank located in any State of the United States", all remaining assets must be turned over to the head office of the non-U.S. bank or the home country receiver of the non-U.S. bank. Read literally, this provision would invalidate all collateral arrangements entered into by non-U.S. banks with federal branches and agencies, to the extent those arrangements secure obligations of non-U.S. offices of the non-U.S. bank.

The OCC has opined, however, that "the IBA does not provide authority for the receiver of a Federal branch to defeat the rights of a secured creditor". *See* OCC Interpretive Letter #733, *supra*. While the OCC's conclusion has not been confirmed by judicial opinion, we believe that, based on the reasoning in the OCC's letter, Section 4(j)(2) should not allow a receiver appointed by the OCC in respect of a federal branch or agency of a non-U.S. bank to invalidate a collateral agreement entered into by a non-U.S. bank with respect to obligations of its non-U.S. branches or agencies.

(e) *Uninsured New York Banks*

If the Pledgor is an uninsured New York chartered bank, or a New York chartered bank for which the FDIC is not appointed and does not appoint itself as conservator or receiver, the liquidation of the Pledgor would be governed by the NYBL.

(1) *Avoidance of Transfers of Collateral.*

After taking possession of a bank under the NYBL, the Superintendent is required to give notice of such action to all entities holding assets of the bank and to demand such entities to turn over all such assets to the Superintendent for disposition in accordance with the NYBL. See NYBL § 615(1) & (2). However, Section 615(2) provides that this right does not affect any rights of a secured creditor with "a perfected security interest, or other valid lien or security interest enforceable against third parties, to retain collateral". NYBL § 615(2). Accordingly, the NYBL would not give a receiver for a New York chartered bank the power to avoid or rescind a transfer of Collateral pursuant to the Collateral Annex. Furthermore, although there have been no cases decided under the provisions of the NYBL that permit the Superintendent to repudiate contracts, nothing in the NYBL indicates that a creditor's right to retain collateral will not remain effective even if the conservator or receiver repudiates the contract.

However, as discussed in paragraph 7(b)(1) above, it appears likely that a transferee of property from a New York bank would be subject to the risk that such transfer could be avoided under the New York fraudulent transfer laws (or comparable laws of other jurisdictions, if applicable).

The NYBL also permits a conservator or receiver for a New York bank to avoid contracts that do not satisfy certain requirements. However, these requirements do not include board approval or "contemporaneousness" requirements of the type included in the FDIA, and therefore do not raise particular issues for secured transactions.

Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that Section 615(2) of the NYBL should prevent the Superintendent from setting aside a transfer of Collateral made by the Pledgor to the Secured Party under the Collateral Annex, unless such transfer constitutes a fraudulent conveyance under applicable law.¹¹

(2) *Limitations on Exercise of Rights Against Collateral.*

Under Section 619(1)(d)(1) of the NYBL, the Superintendent's taking of possession of any bank and the liquidation of such a bank operates as a stay of

¹¹ As discussed in paragraph 7(a)(1) above, to the extent that such transfers are made to secure present or antecedent debt of the pledgor, such transfers should not constitute fraudulent transfers unless they are made with actual intent to hinder, delay or defraud the present or future creditors of the debtor.

any judicial action against such bank, the enforcement of any judgment, any act to take possession of, exercise control over or create or perfect a lien against the bank's property, and any act to collect a claim against the bank that arose before the taking of possession.

We understand that the Superintendent has taken the position that this stay would prevent a counterparty to a QFC with a New York-chartered bank from liquidating and applying collateral held by such party as security for the QFC. The stay does not, however, prevent the commencement by any secured creditor with a perfected security interest, or other lien enforceable against third parties, from commencing a judicial action to enforce such security interest or lien. Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that upon the repudiation of a Master Agreement by the Superintendent or the termination of the Master Agreement by the Secured Party, the Secured Party would be permitted to apply to the supreme court overseeing the liquidation of the Pledgor for an order granting relief from the stay to permit the Secured Party to liquidate any Collateral then held by the Secured Party (to the extent that the transfer of such Collateral may not be avoided as a fraudulent transfer) and apply that Collateral to the obligations of the Pledgor under the Master Agreement. Any remainder would be required to be turned over to the receiver.

(f) *Non-U.S. Banks with Uninsured New York Branches and New York Agencies*

If the Pledgor is a non-U.S. bank that maintains an uninsured New York branch or a New York agency, the liquidation of the branch or agency (and any limitations under U.S. law on the Secured Party's ability to exercise its rights against the non-U.S. bank) will be governed by the NYBL, unless another type of insolvency proceeding is commenced with respect to the non-U.S. bank.¹² Assuming that a New York branch or agency is liquidated under the provisions of the NYBL, it will be necessary to consider the provisions of the NYBL that

¹² As noted above, if the non-U.S. bank maintains federal branches or agencies, a proceeding commenced by the OCC under the IBA will supersede the provisions of the NYBL. In that case, the assets and liabilities of the New York branches and agencies would be included in the proceeding under the IBA, and would be treated as described in paragraph 7(d) above.

It is also possible that an ancillary proceeding under Section 304 of the Bankruptcy Code would be commenced with respect to the non-U.S. branch, and that that proceeding would supersede the provisions of the NYBL. We do not address in this opinion the treatment of a Collateral Annex in the context of an ancillary proceeding.

permit a conservator or receiver to avoid transfers of property by the Pledgor prior to the appointment of the conservator or receiver or that limit the right of a secured party to exercise rights against the Pledgor after the appointment of the conservator or receiver.

Section 606(4)(A) gives the Superintendent the authority to seize all assets located in the State of New York of a non-U.S. bank with a New York branch or agency, as well as all assets worldwide that are "booked" in the New York branch or agency. Accordingly, if a non-U.S. bank has a New York branch or agency, the Superintendent would have the authority to seize collateral posted by the non-U.S. bank if the collateral is located in the State of New York, even if the collateral does not secure obligations of the New York offices of the non-U.S. bank. Furthermore, Section 606(4)(a) of the NYBL also provides that the assets seized by the Superintendent may be applied only to "claims of creditors of [the non-U.S. bank] arising out of transactions had by them with its New York agency or agencies, or with its New York branch or branches". Furthermore, the turnover and stay provisions of the NYBL described in paragraph 7(e) above apply to receiverships in respect of New York branches and agencies of non-U.S. banks.

However, Section 615 of the NYBL permits a secured creditor to retain collateral under a security arrangement related to a QFC, and Section 618-a(2)(d) permits the creditor to apply such collateral to the obligations of the non-U.S. bank under the QFCs, so long as the total amount of collateral applied to the secured creditor's claims does not exceed the "global net payment obligation" (as defined in the NYBL) of the non-U.S. bank under the QFCs. Until the enactment of an amendment to the NYBL on June 25, 1999, this provision applied only to security arrangements to which the New York branch or agency was itself a party. However, as a result of this amendment, this provision was extended to all QFC security arrangements with a non-U.S. bank with a New York branch or agency.

Accordingly, based on and subject to the foregoing and the assumptions set forth in paragraph 2 above and subject also to the comments and qualifications set forth below, it is our opinion that upon the repudiation of a Master Agreement by the Superintendent or the termination of the Master Agreement by the Secured Party, the Secured Party would be permitted to liquidate any Collateral then held by the Secured Party (to the extent that the transfer of such Collateral may not be avoided as a fraudulent transfer) and apply that Collateral to the obligations of the Pledgor under the Master Agreement, to the extent that such collateral does not exceed the global net payment obligation of the non-U.S. bank under the Master Agreement. Any remainder would be turned over to the Pledgor's home country receiver to be applied to the Pledgor's other obligations.

8. *Additional Qualifications*

The foregoing opinions are subject to the following:

(1) The enforceability of Section 5.3 of the Collateral Annex may be limited by laws limiting the enforceability of provisions exculpating or exempting a party from, or requiring indemnification of a party for, its own action or inaction, to the extent such action or inaction involves gross negligence, recklessness or willful or unlawful conduct.

(2) The enforceability of Section 8.6 of the Collateral Annex to the effect that the Collateral Annex may not be terminated except in writing may be limited if the Parties make a legally enforceable verbal agreement to terminate the Collateral Annex or take other actions that indicate that they have agreed to terminate the Collateral Annex.

(3) We express no opinion as to:

(a) the existence of, or the right, title or interest of the Pledgor in, to or under, any of the Collateral;

(b) except as expressly provided in paragraphs 5 and 6 above, the priority of the security interest referred to in paragraph 4 above;

(c) the validity, binding effect or enforceability of any provision in the Master Agreement or the Collateral Annex that purports to (A) impose on the Secured Party or any other person limitations on standards for the care of Collateral in its possession other than as provided for in Section 9-207 of the UCC, (B) permit the Secured Party or any other person to vote or otherwise exercise any rights with respect to any investment property absent compliance with the requirements of applicable laws and regulations as to the voting of, or other exercise of rights with respect to, such investment property, or (C) waive, or consent to the absence of compliance with, any rights of the Pledgor, or duties owing to it as a matter of law, except to the extent that the Pledgor may so waive or consent under applicable law; or

(d) except as expressly provided in paragraphs 5 through 7 above, the creation or perfection of any security interest in, or other lien on, the Collateral.

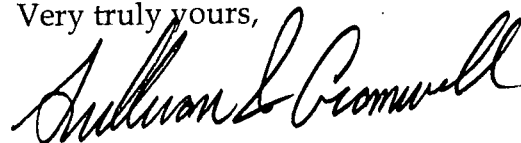
In connection with the opinions set forth above, we note that, as of the date of this opinion, a judgment for money in an action based on an Agreement or Transaction in a Federal or state court in the United States ordinarily would be enforced in the United States only in United States dollars. The date used to

determine the rate of conversion of the Base Currency into United States dollars will depend upon various factors, including which court renders the judgment. Under Section 27 of the New York Judiciary Law, a state court in the State of New York rendering a judgment on an Agreement or an Transaction would be required to render such judgment in the Base Currency, and such judgment would be converted into United States dollars at the exchange rate prevailing on the date of entry of the judgment.

* * *

This letter is furnished to you by us as counsel to The Foreign Exchange Committee and is solely for your benefit.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Sullivan & Cromwell".

Annex A

*Modifications to Collateral Annex to Accommodate the Forms of
1993 IFEMA and 1992 ICOM*

1993 IFEMA

To accommodate an Agreement using the form of 1993 IFEMA, the Collateral Annex should be amended as follows:

- The definition of "Close-Out Netting Provision" should be amended to refer to Section 5.1 of the 1993 IFEMA, with Part VI thereof (if applicable).
- The definition of "Credit Support Priority Provision" should be amended to state "Not applicable".
- The definition of "Force Majeure, Act of State, Illegality and Impossibility Provision" should be amended to refer to Section 6 of the 1993 IFEMA.
- The definition of "Set-off Provision" should be amended to refer to Section 5.8 of the 1993 IFEMA.
- The definition of "Suspension of Obligations Provision" should be amended to refer to Section 5.5 of the 1993 IFEMA.
- The definition of "Termination Provision" should be amended to refer to Section 8.6 of the 1993 IFEMA.

1992 ICOM

To accommodate an Agreement using the form of 1992 ICOM, the Collateral Annex should be amended as follows:

- The definition of "Close-Out Netting Provision" should be amended to refer to Section 8.1 of the 1992 ICOM.
- The definition of "Credit Support Priority Provision" should be amended to refer to Section 11.7 of the 1992 ICOM.
- The following definition of the term "Currency" should be added to the Collateral Annex:

"Currency" means money denominated in the lawful currency of any country or the Euro.

- The definition of "Force Majeure, Act of State, Illegality and Impossibility Provision" should be amended to refer to Section 10 of the 1992 ICOM.
- The definition of "Set-off Provision" should be amended to refer to Section 8.6 of the 1992 ICOM.
- The definition of "Suspension of Obligations Provision" should be amended to refer to Section 8.3 of the 1992 ICOM.
- The definition of "Termination Provision" should be amended to state "Not applicable".
- Section 1.2(a) of the Collateral Annex should be amended to replace the word "In" at the beginning of such section with the words "Notwithstanding Section 11.7 of the Master Agreement, in".
- Section 8.6 of the Collateral Annex should be amended to read as follows:

Each of the Parties may terminate this Collateral Annex at any time by seven days' prior written notice to the other Party delivered as prescribed in Section 11.2 of the Master Agreement, and termination shall be effective at the end of such seventh day; provided, however, that the provisions of this Collateral Annex shall continue to apply until all the obligations of each Party to the other under the Agreement have been fully performed.

Annex B

Assumptions, Qualifications and Analysis Relating to Paragraph 6 of the Opinion

The granting and perfection of a security interest in a deposit account is excluded from the scope of Article 9 of the UCC under Section 9-104(l) thereof, except as provided in the UCC with respect to proceeds and priorities in proceeds. Accordingly, the granting and perfection of consensual security interests in such deposit accounts in New York are governed by New York common law. *Gillman v. Chase Manhattan Bank, N.A.*, 534 N.E.2d 824, 831 (N.Y. 1988). Under New York common law, a security interest in a bank deposit may be created by appropriate terms in an agreement between the depositor and the secured party making specific reference to such a security interest. *See id.*

There are few recent cases applying New York law that have addressed the status of a pledge or assignment of a deposit account in the event of the debtor's default, insolvency or bankruptcy. Money deposited in a general deposit account does not remain the property of the depositor, but becomes the property of the depository bank. *See, e.g., Miller v. Wells Fargo Bank International Corp.*, 540 F.2d 548, 560 (2d Cir. 1976). Upon the crediting of funds to the depositor's account, the depository bank becomes indebted to the depositor in an amount equal to the money deposited plus accrued interest, if any, and the depositor receives a contractual claim against the bank. Thus, it is the depositor's contractual claim, a "chose in action", that is the subject of a creditor's security interest. *Id.*; *In re C JL Co.*, 71 B.R. 261, 265 (Bankr. D. Or. 1987). Accordingly, the cases that have applied New York law to a security interest in a deposit account have often held that a grant of such a security interest is governed by the common law applicable to assignments of intangibles. *See, e.g., Wells Fargo*, 540 F.2d at 562-63. More recent cases, however, have adopted the law of "pledge", even in cases where there is no physical instrument evidencing the account, as had been required by the common law of pledge. *See, e.g., Duncan Box & Lumber Co. v. Applied Energies, Inc.*, 270 S.E.2d 140, 144 (W. Va. 1980); *In re C JL Co.*, 71 B.R. at 265-66. In either case, however, the courts have found that to make an effective grant of such a security interest, it is necessary that the deposit account be in the sole dominion and control of the secured party and, where the depository bank is not the secured party, that notice be given to the depository bank as the obligor in respect of the account, *Wells Fargo*, 540 F.2d at 560.

Dominion Over the Pledged Account. With respect to the issue of dominion over the account, the court in *Wells Fargo* applied New York law to a claimed assignment, as security for a debt, of a time deposit account, stating that such an assignment requires "an intention of transferring the chose in action to the assignee, when the assignor is divested of all control and right to cause of action

and the assignee is entitled to control it and receive its fruits". *Id.* at 557 (quoting *Advance Trading Corp. v. Nydegger & Co.*, 127 N.Y.S.2d 800, 801 (Sup. Ct. 1953)); accord *Duncan Box*, 270 S.E.2d, at 145; *In re CJL Co.*, 71 B.R. at 266; *Cissell v. First National Bank of Cincinnati*, 476 F. Supp. 474, 491 (S.D. Ohio 1979).

Courts have suggested or held that the requisite control by the secured party over the deposit account does not exist when the pledgor may freely make withdrawals from the account. *See, e.g., Duncan Box*, 270 S.E.2d at 146 n:11; *Cissell*, 476 F. Supp. at 491. In *Wells Fargo*, the court held that an assignment, even an "assignment in collateral . . . for security purposes only", "cannot exist where an assignor retains control over the fund or any authority to collect or any power to revoke", *Wells Fargo*, 540 F.2d at 558-59. Similarly, in *Benedict v. Ratner*, 268 U.S. 353 (1925), the Supreme Court considered whether, under New York law, an assignment as collateral of accounts receivable was valid under New York law so that it could not be invalidated under the Bankruptcy Act of 1898. The *Benedict* court held that "[u]nder the law of New York a transfer of property as security which reserves to the transferor the right to dispose of the same, or to apply the proceeds thereof, for his own uses is, as to creditors, fraudulent in law and void", *id.* at 360 (footnote omitted), and that "[t]he results which flow from reserving dominion inconsistent with the effective disposition of title must be the same whatever the nature of the property transferred", *id.* at 364.

New York cases subsequent to *Benedict* have held, in considering the nature of the dominion and control that must be conveyed to an assignee of a chose in action, that "an effective assignment necessitates such a present transfer of title or dominion that the debtor [in this context the depository bank] can safely pay the fund to the assignee notwithstanding any protests or orders to the contrary by the assignor". *Maloney v. John Hancock Mutual Life Insurance Co.*, 271 F.2d 609, 614 (2d Cir. 1959) (citations omitted); accord *Wells Fargo*, 540 F.2d at 559 (quoting *Maloney*).

It should be noted that the requirement that dominion be relinquished does not require that there be no conditions to the assignee's or pledgee's right to seize the contents of the account. For example, New York courts have held that "an effective present assignment" may be conditioned upon "the assignor's default in repayment of the [secured obligation] . . . or even upon his default in performance of an independent contract", and that "[m]ere power in the assignor to control the amount of eventual payment under a transfer does not prevent an effective assignment". *Maloney*, 271 F.2d at 614; accord *Wells Fargo*, 540 F.2d at 559 (citations omitted). What is required is a present transfer in which nothing remains to be done by the assignor in order to vest the assignee with its rights, as distinguished from a mere promise by a borrower to pay a debt out of a designated fund, whether existing or to come into existence in the future. *See,*

e.g., *Malone v. Bolstein*, 151 F. Supp. 544 (S.D.N.Y. 1956), *aff'd per curiam*, 244 F.2d 954 (2d Cir. 1957); *Wells Fargo*, 540 F.2d at 558.

With respect to the Cash Collateral Account, as noted above, we have assumed that the Secured Party has complete dominion and control over the Cash Collateral Account, that the pledged deposits have been transferred to an account in the name of the Secured Party and that the Pledgor has no right to withdraw funds from the account or to gain access to the account or those funds in any other manner. Although the Secured Party has an independent contractual obligation to release U.S. Dollar Collateral from the Cash Collateral Account in the circumstances described in the Collateral Annex, this independent obligation would not itself permit the Pledgor to transfer funds in the Cash Collateral Account without action by the Secured Party. The Pledgor would also be unable to prevent the Secured Party from transferring funds in the account for the benefit of the Secured Party at any time upon the occurrence of the specified conditions. Accordingly, the Secured Party would be entitled to absolute control of the Cash Collateral Account, and no rights to dispose of funds in such account would have been retained by the Pledgor. See *Benedict*, 268 U.S. at 360; *Wells Fargo*, 540 F.2d at 559; *Maloney*, 271 F.2d at 614. If the Secured Party breaches its obligations under the Collateral Annex to make returns or payments of funds on deposit in the Cash Collateral Account in accordance with Section 3.3 of the Collateral Annex, the Pledgor's remedy would be a cause of action against the Secured Party under the Collateral Annex, and not a direct right to funds in the Cash Collateral Account. See *Wells Fargo*, 540 F.2d at 460. Accordingly, the terms of the Collateral Annex should not be inconsistent with the Secured Party's dominion and control over the Cash Collateral Account.

Notice to the Depositary. The cases that have addressed security interests in deposit accounts under New York law have not expressly addressed the question of "perfection". Neither the UCC nor New York common law expressly defines the concept of "perfection" of a security interest in such property. As stated in New York Annotation (1)(d) to UCC Section 9-301: "The general rule under existing New York law [prior to adoption of the UCC] is that no steps need be taken for the perfection of a security interest in [accounts and general] intangibles". Similarly, at least one federal court applying New York law found that no public filing is required. *Wells Fargo*, 540 F.2d at 557; *accord Duncan Box*, 270 S.E.2d at 146 (West Virginia law). When an account is assigned or pledged to a party other than the depositary bank, however, at least one court has held that notice to the depositary bank may be necessary to preserve the assignee's or pledgee's interest in the account against claims of third parties. See, e.g., *Wells Fargo*, 540 F.2d at 560 (citing notice required in assignments of intangible rights under insurance policies, accounts payable and mortgages).

In the case of the Cash Collateral Account, the fact that the account is established in the Secured Party's name should give clear and unambiguous notice to the Secured Party's custodian, as depository, of the Secured Party's rights in the Cash Collateral. This fact also should make clear to third parties that funds in the Cash Collateral Account are not subject to unrestricted use (or, indeed, any use) by the Pledgor. Accordingly, the provisions of the Collateral Annex are consistent with the purposes of perfection of a security interest, notice to third parties and the policy expressed in New York statutory and case law that a party's rights should be subject to the rights of prior secured parties of which it has notice.