To Mr. Klaus Löber  
EFMLG Secretary,  
Postfach 16 03 19  
Frankfurt am Main.  
Germany  

From Francisco Garcimartín  
Catedrático de Derecho internacional privado  
C/Ulises, 92, 1º A  
28043 Madrid  
Spain  

Dear Mr. Löber,  

I have read with much interest the report produced by the EFMLG on set-off and netting agreements under EC law. I congratulate you on the analysis. I agree with you that there are certain doubts about the scope of the protection granted by EC law, in particular in relation to close-out netting agreements.

Professor Miguel Virgós (who wrote the report of the 1995 Insolvency Convention) and I have dealt with that very issue –and other closely related aspects- in our commentary to the Insolvency Regulation published by Kluwer in 2004. I think that the part of the book in which we analyze the problem may be of interest to you. I am attaching a copy of these pages. In particular, in paragraph 193 we advocate for a broad understanding of article 6. The uncertainty remains, but I guess that our comments may be of some help to support your position.

Best regards,  

Francisco Garcimartín
The European Insolvency Regulation: Law and Practice

by

MIGUEL VIRGÓS
Professor, School of Law, Universidad Autónoma de Madrid, Spain

and

FRANCISCO GARCIMARTÍN
Professor, School of Law, Universidad de Castilla-La Mancha, Spain

KLUWER LAW INTERNATIONAL
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About the Authors

*Miguel Virgós* is professor at the School of Law of the Universidad Autónoma de Madrid, member of the Spanish Law Commission and Of-Counsel at Uria & Menéndez, Madrid. He is coauthor of the Virgós/Schmit Report on the 1995 Convention on insolvency proceedings from which the Insolvency Regulation stems and has participated in the drafting of the new Spanish Insolvency Law. *Francisco Garcimartín* is professor at the School of Law of the Universidad de Castilla-La Mancha and Spanish delegate for the negotiation and drafting of the Convention on the Law Applicable to Certain Rights in respect of Securities held with an Intermediary, drawn up by the Hague Conference on private international law. Both authors have ample experience providing legal advice in regard to international business transactions and litigation.

Any comment on this book will be welcome at either <miguel.virgos@uam.es> or <francisco.garcimartin@ucm.es>
the asset be located in a Member State other than the State of opening, and also that it has been delivered to the purchaser or the person by this designated.

172. The majority of commentators deduce from the tenor of Article 7 that it only applies to simple reservations of title, not to more complex figures such as "prolonged" or "extended" reservation of title; this clearly without prejudice to the fact that when these figures are protected as rights in rem they can be covered by Article 5.\footnote{Herschen, pp. 120–121; Lieble/Staudinger (2000), p. 553 (based on Article 4.1 of Directive 30/95, dated June 29).}

Explanation. Prolonged reservations of title are really a combination of two distinct operations: a reservation of title with authorisation to sell and an anticipated assignment by way of guarantee of the claim resulting from this sale. Article 7 would apply to the reservation of title and Article 5 to the anticipated assignment by way of guarantee, where appropriate.

173. Article 7 presupposes the existence of this right, i.e. that title to the asset has been validly retained under the applicable law. This is a preliminary question that has to be determined according to the ordinary conflict of laws rules (e.g. in the case of movables, according to the lex rei sitae). If a valid retention of title has been constituted, what Article 7 excludes is the possible interference of the insolvency rules of the lex fori concursus, the lex rei sitae and lex contractus (= rule of non-alteration, see, mutatis mutandis, No. 162 ff). In this respect, as is also the case with Article 5, we are dealing with a rule of substantive rather than of confictual scope.\footnote{Vries, p. 19.}

NB. The agreement on retention of title has dual significance, both contractual and real: the guarantee for the seller/supplier consists of the possibility of cancelling the sale and recovering the object which has been sold. Article 7 ensures the protection of both the real aspects and the contractual aspects of the agreement on retention of title,\footnote{See Tausitz, p. 342; Huber, p. 160.} i.e. it ensures that the declaration of the opening of the insolvency proceedings does not interfere with the effectiveness of the agreement in either of its two spheres.

2.3. Detrimental acts

174. Both Article 5 and Article 7 are based on the non-fraudulent location of the assets;\footnote{Vries, Schmitt Report, Margin No. 105; Tausitz, p. 341,} the Regulation does not cover fraud in the location of the asset so, in such uses, we must look to the general rule: the application of the lex fori concursus.

175. Actions to set-aside (i.e. actions of voidness, voidability or unenforceability acts which are detrimental to the body of creditors) rights in rem covered by Article 5 and reservations of title protected by Article 7 are subject to the lex fori insursus. This is expressly stated both in Articles 5.4 and 7.3. However, Article 13 also may come into play. This provision allows the application of the lex fori concursus to be excluded if the beneficiary of the act in question proves that the said act is, according to the law which governs it (lex causae), legally unquestionable. We shall examine this regime in more detail when commenting on Article 13.

2.4. Credit institutions and insurance undertakings

176. The Directives on the reorganisation and winding-up of credit institutions and insurance companies contain rules which are similar to those of Articles 5 and 7 of the Insolvency Regulation (Articles 21 and 22; and 20 and 21, respectively). In this case, the importance of this exception to the play of the law of the State of origin is greater insofar as these Directives do not provide for the possibility of opening territorial proceedings. The Directive on credit institutions also establishes a special rule for repurchase agreements (Article 26).

3. SET-OFF (ARTICLES 4 AND 6)

177. Set-off may be described as the discharge of reciprocal obligations to the extent of the smaller obligation.\footnote{Wood, p. 71.} Set-off presupposes the existence of two distinct claims, the primary claim, which is the claim owed to the insolvent debtor, and the cross claim, which is the claim owed to the creditor, that are set against each other to produce a single balance.

The Insolvency Regulation alludes to set-off in two provisions. Article 4.2.d subjects "the conditions under which set-offs may be invoked" to the lex fori concursus. And Article 6 states that "the opening of insolvency proceedings shall not affect the right of creditors to demand the set-off of their claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor’s claim".

178. Traditionally, there has been some debate as to how law governs the set-off of claims in the event of commencement of insolvency proceedings. In comparative law, several solutions have been proposed: (a) the lex fori concursus; (b) the proper law of the claim to be discharged, total or partially, by set-off (the insolvent debtor’s claim); or (c) either of the two laws, alternatively. In this matter, the Insolvency Regulation leans towards the third solution, that is to say, towards an alternative solution. The combination of Articles 4 and 6 ends up permitting set-off in accordance with either of these two laws: the law of the State of opening (lex fori concursus) or the law governing the insolvent debtor’s claim (the primary claim).

179. The relationship between Articles 4 and 6 of the Insolvency Regulation is explained as follows. Article 4 establishes the application of the lex fori concursus as the basic rule of the system. Insolvency law can be seen as a part of the general system of discharge of obligations; this explains why set-off, as a special mechanism to effect...
such a discharge, is, in situations of insolvency, subject to the *lex fori concentus* on equal terms for all of the creditors. However logical this solution may be, it means that any party who wishes to calculate the consequences of the insolvency of the counterpart must first anticipate (by means of Article 3) which State is "destined" to become the forum of the insolvency proceedings (i.e. where the debtor's centre of main interests, or a debtor's establishment, will presumably be situated at the time of requesting the opening of insolvency proceedings).\(^{199}\) This result is not coherent with the function performed by set-off in a number of Member states, where it operates, in substance, as a form of security. For this reason, Article 6 establishes an exception to Article 4 in order to "protect legitimate expectations and the certainty of transactions" (Recital 24). Article 6 permits set-off if this is possible, in *cases of insolvency*, in accordance with the law governing the claim where the insolvent debtor is the creditor in relation to the other party (i.e. the insolvent debtor's claim). This provision crystallizes the right to set-off in a national law which is predictable from the very moment of contracting, even though the debtor may become insolvent at a later date under a different national law. In conclusion, in Article 4, set-off is regarded primarily as a means of discharging or settling claims, whereas in Article 6 it is seen more as a means of guarantee.

### 3.1. Article 4: set-off under the *lex fori concentus*

180. The starting point is the general rule contained in Article 4: the *lex fori concentus* applies to set-off in the insolvency. This rule derives not so much from Article 4.2.d of the Insolvency Regulation, which has a specific function which we shall examine later, as from the character of Article 4 as a general rule: unless another rule of the Regulation establishes an exception, the *lex fori concentus* governs the insolvency proceedings and all of its effects, both procedural and substantive, in respect of the rights and positions of the parties. The admission, extension or reduction of set-off is one of these effects and, consequently, unless another rule of the Regulation establishes an exception, it is determined by the *lex fori concentus*. This

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\(^{199}\) Fletcher (1999), p. 274.
right. The right to set-off constitutes a "preliminary question" to be decided by the national law which governs the claim to be set off. Consequently, if, in accordance with the non-insolvency rules of the national law which governs this claim, the creditor can discharge his obligation by way of a set-off, the conditions under which this right may be invoked in the insolvency of the debtor are determined by the lex fori concursus. Only if we obtain a "yes" under the law governing the preliminary question, will the second question (efficacy in the insolvency proceedings) arise. Essentially, the pre-insolvency right to set-off is subject to its applicable law, but whether this right can be invoked or not in the insolvency of the counterpart (and whether or not specific conditions are required for this to be possible) is subject to the lex fori concursus. The problem is that according to this construction the Regulation would be imposing a given normative model of insolvency set-off, when what the Regulation seeks to do, as we shall see, is not to interfere with the national models of set-off.

182. In order to interpret Article 4.2.d correctly, we have to bear in mind two points: first, its relationship with Article 4.1 (systemic argument); second, its relationship with the different national systems of set-off (comparative law argument).

From the perspective of the first, it is clear that the purpose of the list of issues contained in Article 4.2 is not to limit the role of the law of the State of opening (lex fori concursus), but rather simply to give examples of its application. It serves to eliminate doubts concerning the scope of Article 4.1, but does not replace it. From the perspective of second argument, it is also clear that solutions to the problem of set-off in the Member States vary significantly. Seen in this context, the function of Article 4.2.d is not to "reproduce" a given national model on a European Community scale (and thereby reduce the scope of Article 4.1 with regard to set-off) but, on the contrary, to preserve the "neutrality" of Article 4 in the face of the different models of set-off which exist in the Member States.

In order to understand this last statement it is essential to distinguish between the different approaches to set-off that exist in Europe. Under English law, for example, set-off is treated as a mandatory process which must be applied to all insolvency proceedings opened in England.202 "Insolvency set-off" functions as an autonomous institution. It requires the mutual debts between the parties to be taken into account. Then, even if the claims are completely unrelated to each other, set-off takes place by operation of the law. This results in the extinction of the two claims and only the aggregate result is payable. "Insolvency set-off" tends to be justified on the grounds that it facilitates a proper and orderly administration of the insolvent's estate. There is no doubt that Article 4.1 applies to this "procedural model" of set-off and that the lex fori concursus determines, in this case, both the possibility ("existence") of set-off and the conditions under which it may be enforced ("efficacy").

In other systems, insolvency set-off is not an institution related to the administration of the insolvent's estate, but simply a "prolongation" or extension of the pre-insolvency right to set-off. The question in these systems is whether or not that pre-existing right to set-off can be invoked and enforced once insolvency proceedings have commenced in the same way as it exists outside the insolvency of the debtor, and whether or not to impose certain restrictions upon the exercise thereof. Article 4.2.d was drafted with this model in view. Let us take the example of German law. Paragraph 94 of its Insolvenzordnung states that "if an insolvency creditor has, at the time the insolvency proceedings are opened, a right to set-off derived from the law or from a set-off agreement, this right shall not be affected by the proceedings". This provision means that set-off is also governed in the insolvency of the debtor by the general rules of the Civil Code and that the insolvency rules are limited to establishing certain restrictions upon the exercise thereof. In other words, the insolvency rules recognise and respect the right to set-off just as it exists according to the general non-insolvency regime;203 and this ordinary non-insolvency regime, is determined by the ordinary conflict of laws rules. Technically, the existence of the right to set-off constitutes a preliminary question, governed by the ordinary conflict rules. Thus, Article 4.2.d ensures that, in the States which follow this model, the lex fori concursus is not applied beyond what it demands. There is no reason for the Insolvency Regulation to interfere with this "substantive model", causing the lex fori concursus to have other effects distinct from those sought by the national legislator (e.g. by applying the non-insolvency set-off rules of the German Civil Code even if the insolvent's debtor claim is governed by a different national law, merely because the insolvency proceedings are opened in Germany).

183. In conclusion, Article 4.2.d. does not monopolise the way set-off is dealt with, either within the framework of the Insolvency Regulation (see Articles 9 and 6, for example) or within the framework of Article 4 itself. Thus, Article 4 must be considered as a whole which contains, in reality, two rules regarding set-off.204 The first rule is the general rule whereby the insolvency proceedings and their effects are governed by the lex fori concursus (Article 4.1). Insofar as this law so requires, it will govern both the possibility and the conditions of set-off in the event of insolvency. This is the case, for example, with the insolvency set-off of English law. The second rule (Article 4.2.d) operates when the lex fori concursus does not contain a specific model of insolvency set-off, but simply allows the ordinary regime of non-insolvency set-off to apply and establishes (or not) limits or exceptions to its application. The pattern of application provided for in Article 4.2.d permits, therefore, the substantive model of the national law to be respected. In other words, the Regulation does not impose a model, but recognises the model established by the lex concursus; it is the latter which decides, not the former.

### 3.2. Article 6: set-off under the law governing the insolvent debtor's claim ("primary claim")

184. Alongside this possibility, Article 6.1 of the Insolvency Regulation establishes an alternative rule: even when set-off is not possible through the application

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203 Albeit after establishing some restrictions on the exercise thereof in paragraph 96 InsO.
204 In this respect, GARCÍA GUTIERREZ, passim.
f the lex fori concursus, it would still be possible when the law which governs the insolvent debtor’s claim (or “primary claim”) permits set-off in spite of the insolvency of the debtor (or precisely because of it). For this reason, Article 6.1 establishes that “the opening of insolvency proceedings shall not affect the right of creditors to demand the set-off of their claims against the claim of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor’s claim”.  

185. As we have already stated, in Article 6 set-off is perceived as a security-like device. The possibility of a set-off in insolvency, as allowed by the laws of some Member States, gives the parties a degree of confidence equivalent to that of a security interest. It reflects the idea that the parties were transacting in reliance upon their ability to secure payment and that it would be unfair to deprive the solvent party of its security to the extent of the set-off. The purpose of Article 6 is to protect this guarantee function. For this reason, it permits the acquisition of a right to set-off in accordance with a law that can be determined at the very moment of contracting or occurring the obligation (the law governing the primary claim), and ensures that this right will be recognized in the insolvency of the debtor. This provision is very important for commercial predictability and availability of credit within the European market.

186. Article 6.1 not only protects the rights of set-off from the insolvency effects established by the lex fori concursus, but also contains a uniform conflict rule on the law applicable to the right of set-off itself (see Recital 26). The existence of this right of set-off is determined by the law which governs the insolvent debtor’s claim (i.e., the primary claim). This uniform rule displaces the national rules of Private International Law.

187. The referral made by Article 6.1 to the law of the insolvent debtor’s claim includes the insolvency rules of that legal system. The question which must be asked whether, according to the law which governs this claim, the creditor has the right to demand set-off in the event that insolvency proceedings are opened against the debtor. The Report is very clear on this point: “... Article 6 constitutes an exception to the general application of that law in this respect, by permitting the set-off according to the conditions established for insolvency set-off by the law applicable to the insolvent debtor’s claim” (our italics).

Difference between Articles 5 (right in rem) and 6 (set-off). This difference is easy to appreciate. Basically, what Article 5 says is that the creditor has the same position he would have under non-insolvency according to the national law which governs his right in rem; and Article 6 says that the creditor has the same position he would have under insolvency according to the national law governing the set-off.

188. Article 6 applies in respect of mutual claims incurred prior to the opening of the insolvency proceedings (i.e., claims existing before that moment). If the claims are incurred afterwards, Article 6 does not operate and the lex fori concursus (ex Article 4) governs both the possibility and the conditions of set-off.

NB. This requirement must be interpreted in the light of the sense and purpose of the provision: to protect the expectations of set-off on the part of the solvent creditor when these expectations arose before the declaration of opening. For this reason, Article 6 applies when the claims arose out of contracts or other dealings entered into prior to the opening of the insolvency proceedings, even if they were, at that moment, mature or immature, contingent or not.

189. The wording of the provision does not require that the law in question be the law of a Member State, but this requirement is implied as a result of the intra-Community limitation of the Insolvency Regulation itself.

190. The regime of actions to set-aside (i.e., the actions of voidness, voidability or unenforceability of those acts which are detrimental to the creditors as a whole) which might affect a set-off protected by Article 6 is subject to the lex fori concursus by virtue of the referral made by Articles 6.2 to 4.2.m. It must be remembered, however, that Article 13 permits the application thereof to be excluded if the beneficiary of the act in question proves that the said act is legally unquestionable according to the national law which governs it (i.e., the lex causae). We shall examine this regime in more detail when commenting upon Article 13.

NB. In payment systems and financial markets, actions to set-aside are governed by the provisions of the law applicable to the system itself or to the market in question (Article 9.2).

3.3. Contractual set-off

191. Contractual set-off enables parties dealing with each other to combine an account in credit with an account in debt and to restrict liabilities to the payment of the resulting balance. Contractual set-off is governed by the law applicable to the contract establishing the set-off arrangement. As a general rule, this law is determined in accordance with the Rome Convention of 19 June 1980 on the law applicable to contractual obligations. This solution is implicit in Article 6 (the drafting of which is better adjusted to set-off in law) as the Explanatory Report confirms without any doubt: “contractual set-off implies an agreement subject to its own applicable law according to the 1980 Rome Convention”.

Accordingly, under Article 6, the opening of insolvency proceedings will not affect the right of a creditor to set-off.

his claims against the claims of the debtor, where such set-off is permitted by the law applicable (including its insolvency rules) to the set-off agreement that governs the transactions between them.

NB. Article 6.2 IR establishes an exception to this rule: actions to set-aside detrimental acts would remain the competence of the lex fori concursus, although subject, in turn, to the restriction provided for by Article 13 IR.

192. Article 6 is applicable to agreements which, according to the law of the State that governs them,211 enable their participants to manage their credit exposures arising from all kinds of transactions on a net basis, by setting off reciprocal claims to produce a single amount due or owed.

The set-off agreement may be a provision contained in the same contract out of which the insolvent debtor’s claim arises or may constitute an autonomous agreement. In a typical arrangement, a number of transactions are subject to a master agreement that functions as an umbrella governing the relationships between the parties and imposes common terms on the underlying transactions, including set-off or netting arrangements. This master agreement will have its own applicable law, which may be different from that of the underlying transactions. In the latter case, the law applicable to the set-off arrangement might be different from the law which governs each of the underlying claims. If the law applicable to the master agreement allows the set-off to operate successfully in the event of the insolvency of the counterpart, then Article 6 protects this result and the set-off operates successfully in respect of all the underlying transactions. For this reason the Report stated that “the same rationale on which Article 5 (security rights) is based explains that in the event of a contractual set-off covering different claims between two parties, the law of the Contracting State applicable to that agreement will continue to govern the set-off of claims covered by the agreement and incurred prior to the opening of the insolvent proceedings”.212

Development. Under Article 3 of the 1980 Rome Convention, the parties to a contract may freely choose the national law which better suits their interests. This means that the law applicable to the primary claim referred to in Article 6 may be the law expressly chosen by the parties. This is the situation where Article 6 is contemplating: the set-off agreement as an accessory pact within the main contract, the law of which governs both the claim and the set-off agreement. However, under Article 3 of the 1980 Rome Convention, the parties may select different national laws to govern separable parts of the contract. This means that the parties can choose the same law to govern the contract and the set-off agreement, but can also choose different laws to govern each of them, as distinct and separable parts of the contract (content v. discharge). It may be the case that the set-off agreement is concluded as a separate or autonomous agreement, subject to its own lex contractus, and that this law does not coincide with the one which governs the insolvent debtor’s claim – in the example given above, because the parties have entered into a master set-off agreement encompassing several transactions, each one of them with its own lex contractus. This result is both consistent with the teleology of Article 6 and with the possibilities allowed for by the 1980 Rome Convention. Article 6 focuses on the function of the set-off as a form of guarantee and, in these cases, this function does not derive from the law which governs the primary claim, but from the master agreement in which it is inserted. For this reason, and taking into account the freedom to choose the applicable law in contractual matters, Article 6 should be understood as deferring, in the case of an autonomous set-off agreement, to the proper law of this agreement. The accuracy of this interpretation is confirmed by the fact that this is the solution which is expressly included in the Directive on the reorganisation and winding-up of credit institutions (see Article 25). To reject this interpretation and claim that Article 25 of the Directive and Article 6 of the Insolvency Regulation provide different solutions would give rise to a paradoxical situation: that in the case of an agreement between a credit institution and an ordinary debtor, whether or not the set-off arrangement would be valid would depend on which of the parties of the set-off agreement was declared insolvent, the bank or the ordinary debtor, because the national law applicable to the set-off agreement would be different in each case.

193. The conditions for applying the set-off will be those agreed by the parties within the framework of the autonomy which the national applicable law allows them. In contractual set-off it falls to the parties themselves to establish the circumstances and the conditions in which set-off applies. Article 6 does not establish any specific condition or limit to set-off agreements different from those established by the national applicable law. For this reason, Article 6 may protect not only “simple” contractual set-off clauses (those that cover reciprocal monetary claims), but also more “complex” set-off agreements which contain special contractual provisions to convert non-monetary obligations (i.e., an obligation to deliver commodities) into monetary obligations or to close-out open contracts and net all obligations arising out of those contracts. In other words, Article 6 also covers “netting agreements”.213 This broad interpretation of the scope of Article 6 is also necessary given the absence of a specific exception for financial contracts in the Insolvency Regulation. Contractual set-off and netting play a central role in effective credit and systemic risk management, which, in turn, is essential for liquidity and market efficiency. For this reason, all Member States recognise contractual set-off and netting clauses in financial contracts, either by application of general insolvency rules or by special carve-outs provisions. Legal certainty and consistency require that this state of things be also recognised at the conflict of laws level. Article 6, in combination with the national applicable law, make it possible for these agreements to operate also in cross border situations. However, Article 6 does not limit its protection to financial contracts since it does not establish any subject-matter limitation in its sphere of application.

Rationale. In international practice, it is normal for set-off agreements to include contractual provisions which ensure that the set-off is completed before a specified date through

211 In our view, the law of a Member State, see No. 189.
212 Parenthesis added, VIEGOS/SMIT Report, Margin No. 110.
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acceleration or cancellation clauses; or to establish that the claims resulting from all of the transactions included are consolidated and replaced by a single debtor or creditor claim, so that the parties can only demand the resulting net balance; or for non-monetary obligations to be converted into monetary obligations so that the set-off can be applied.\(^{214}\)

The problem lies in determining whether these contractual devices designed to produce or facilitate set-off are also protected by Article 6 as components of the set-off arrangement or whether they fall under the general competence of Article 4 IR, since, as general rule, the effects of the insolvency proceedings on current contracts are determined by the lex fori concursus.

Take the example of "close-out netting" agreements. This form of netting embraces two steps: "termination" of contracts and the set-off of all obligations arising out of those contracts on an aggregate basis. However, the clauses on termination and set-off are pieces of a single risk management mechanism that cannot be separated and used for the purposes for which they are intended. In financial transactions, counterparties typically hedge their risks by entering into contracts with third parties. Without the ability to close out, net and set-off defaulted contracts, failure of a party could lead the counterparties to be unable to perform their related financial contracts, resulting in a series of defaults in back-to-back transactions ("interdependence risk"); this would hinder hedging against market fluctuations and risk management, reducing credit availability. For this reason, the close-out contractual provisions constitute a vital part of the "security structures" based on set-off which have gained great practical significance in financial transactions, and this security function is precisely, what the Insolvency Regulation seeks to protect (see Recital 28). Article 6 was conceived to promote commercial and financial predictability by respecting these structures, not to change them; it would therefore be applicable to determine the set-off or netting arrangements that are enforceable in the insolvency of the debtor and their scope. The result is that the provisions of the set-off or netting agreement will be enforceable in accordance with their own terms against the insolvent party if and insofar as the national law applicable to the agreement so allows. Not only the teleological argument speaks in favour of this interpretation. The parallelism that exists between the Insolvency Regulation and the Directive on reorganisation and winding up of credit institutions as parts of a Community law provide a further reason (a systemic argument). In effect, Article 25 of the Directive expressly admits set-off and netting, including close-out netting, regardless of whether the counterpart is the administrative authority of the credit or insurance institution or an ordinary creditor. If the Insolvency Regulation and the Directive were not in accordance, netting would or would not be possible depending on which of the parties becomes insolvent; a result that cannot be admitted. This is also consistent with the view taken by Directive 2002/47 on Financial Collateral Arrangements on analogous close-out provisions forming part of security interest structures. According to its Article 7, Member States shall ensure that close-out netting provisions can take place in accordance with their terms regardless of the commencement of insolvency proceedings. The conflict of laws reflection of this rule is the application of the law governing the agreement itself, to determine its validity and enforceability in the event of the insolvency of the counterpart.

194. The Directives on reorganisation and winding up of credit institutions and insurance companies contain similar rules. Set-off is allowed: (a) if it is permitted by the lex fori concursus (see Articles 10.2.c and 9.2.e respectively); or (b) if it is contemplated by the law that governs the primary claim (Articles 23 and 22, respectively). In addition to this, Article 25 of the Directive on credit institutions\(^{215}\) contains a special rule regarding contractual set-off. According to this provision, the effects of the opening of insolvency proceedings on netting agreements (and a fortiori, simple set-off agreements) "shall be governed solely by the law applicable to the contract which governs such agreements". Unlike the Regulation, Article 25 does not expressly reserve the application of the lex fori concursus for actions to set-aside (as do Articles 6.2 IR or 23.2 of the Directive).

**Difficulty: actions to set-aside.** The parallels between the solutions provided by the Regulation and those provided by the Directive are justified on the grounds of general validity except on one point, where the solution provided by the Directive responds to the specific needs of financial entities, i.e. actions to set-aside. The Regulation subjects this regime (Article 6.2) to the general rules (Article 4.2.m in relation with Article 13, see No. 190), and the explanatory report, which is careful to adapt the solution of Article 6 to contractual set-off agreements, is silent on this point. This indicates that the general regime continues to apply. However, Article 25 of the Directive subjects these agreements exclusively to the law of the contract, without making any provision for the application of the lex fori concursus, as Article 23 does with regard to the set-off in law.\(^{216}\) The aim of this is to show that actions to set-aside do not follow the general regime of the lex fori concursus, but are rather governed by the same law as the netting arrangement. The foundation for this special regime lies in the vital role played by set-off and netting in facilitating control of the solvency ratio of the credit institutions, which is a matter of public interest. This is why Article 25 of the Directive simplifies the conflict of laws solution and provides immediate legal certainty as compared to the Insolvency Regulation, where the interplay of Articles 4.2.m and 13 provides a less immediate answer. This foundation applies specifically to credit institutions, and cannot be extrapolated and applied to the Regulation in order to create a general exception to Article 6.2. However, when the set-off agreement is between an ordinary debtor and a credit entity, it seems justifiable to apply the solution provided for in Article 25 of the Directive, as the lex specialis. Firstly, because the law applicable to the set-off agreement should not vary according to the procedural position of the parties (i.e. according to which of them is declared insolvent); such a solution would be incompatible with the function which these agreements fulfill in commercial transactions and inconsistent with the teleology of Article 25 of the Directive. Secondly, because it would be paradoxical for rules which protect a public interest (facilitate control on insolvency and reduce systemic risks) to insulate credit institutions against the risk of the insolvency of the counterpart to a lesser extent in the case of those debtors where the risk of insolvency is greater (ordinary debtors) than in the case of those other debtors where the risk of insolvency is, at least in theory, lower (other credit entities).

195. With regard to the set-off regime of payment and settlement systems, see infra Nos 211 et seq.

4. Effects on Contracts

4.1. General rule: Lex fori concursus (Article 4.2.e)

196. In principle, the rights and duties of the parties and the dynamics of a contract (i.e. performance, termination and discharge) are subject to the law governing

\(^{214}\) For an explanation of these mechanisms, see GOOS (1997), p. 178.

\(^{215}\) On this Directive, DEUG, No. 41 ff. and 66.

\(^{216}\) DEUG, No. 66.