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The single agreement concept in international Framework Contracts for Cross-Border Derivatives and other financial Transactions

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Abstract. Master agreements produced by trade associations – standardized framework contracts used in international markets – have largely replaced tailor-made documentation in the contemporary financial world. These agreements provide a reliable foundation for structuring obligations across a broad range of financial instruments, including forwards, options, swaps, repurchase agreements (repos), and securities lending transactions. Despite being developed in diverse regions, standard contracts for cross-border financial products exhibit several common features. A key feature is the “single agreement” concept, and its corresponding contractual clause. The article provides an overview of “single agreement” clauses found in international master agreements and examines two critical implications of this fundamental aspect of standard documentation. First, it explores the enforceability of close-out netting, a mechanism vital for managing counterparty risk in the event of default. Second, it discusses the application of a unified governing law to all elements of the standard documentation, which might otherwise be subject to various laws determined by conflict-of-laws rules. Beyond these legal applications, the single agreement also serves a technical function by uniting numerous schedules, annexes, confirmations, protocols, and other components of standard documentation withing a single legal framework.

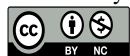
Key words: close-out netting, master agreement, financial transactions, bankruptcy, derivatives, repurchase agreements, securities lending, single agreement

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Концепция единого договора в международных рамочных соглашениях для трансграничных деривативов и других финансовых сделках

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Аннотация. Генеральные договоры, подготовленные торговыми ассоциациями, т.е. стандартные рамочные соглашения, применяемые игроками на международных рынках вместо ситуативно подготовленной документации, в настоящее время доминируют в финансовом мире. Стороны таких договоров структурируют свои обязательства, основываясь на пользующихся доверием стандартных документах, покрывающих большое количество финансовых инструментов. К их числу относятся опционы, форварды, свопы, договоры репо и сделки займа ценных бумаг. Несмотря на подготовку типовых соглашений в разных странах мира, стандартные контракты для трансграничных финансовых продуктов имеют много общего. Концепция единого договора и соответствующее договорное положение выступает примером такого общего элемента. Помимо описания положений о едином договоре в статье рассматриваются два важных последствия использования этого краеугольного камня стандартной документации. К таким последствиям относится возможность принудительного исполнения положений о ликвидационном неттинге и распространение применимого права на все элементы стандартной документации, которые подчинялись бы праву разных стран, если бы применимое право определялось на основе коллизионных норм. Помимо этих важных последствий принцип единого договора выполняет чисто техническую роль, выступая единым связующим звеном для различных приложений, дополнений, подтверждений, протоколов и других элементов стандартной документации на международных финансовых рынках.

Ключевые слова: ликвидационный неттинг, генеральное соглашение, финансовые сделки, банкротство, деривативы, сделки репо, займы ценных бумаг, единый договор

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Introduction

Exchange-traded financial instruments exhibit a high level of standardization, with minimal variations allowed at the discretion of the parties (Muscat, 2009:36). In contrast, a significant volume of financial instruments is traded privately, without the involvement

of an exchange or clearinghouse (Benzler, 1999:34). These privately negotiated transactions are referred to by finance professionals as “over the counter” (OTC) financial contracts¹. In French-speaking countries the OTC market is known as *marché de gré à gré*², while in Germany, it is referred to as *außerbörsliche Handel*³.

In the absence of contractual specifications imposed by an exchange⁴, the parties to OTC contracts would, in theory, need to draft numerous bespoke agreements internally to conduct transactions with their peers and clients. This would result in higher legal and organizational costs due to the time and resources required for lengthy negotiations. Such a framework, however, does not meet the practical needs of this dynamic market. In practice, dealers in international financial markets are typically aligned in their approach to documenting contractual relationships in OTC markets. To minimize costs and streamline operations, they almost always rely on pre-drafted standard contracts published by industry associations, rather than negotiating bespoke agreements for each transaction.

These standard agreements, often available in the form of master agreements, may govern all financial contracts between two parties or apply to specific classes of transactions (Franzen, 2009:24). Their widespread use has become a defining feature of financial industry (Benzler, 1999:37), bringing a high degree of standardization to privately negotiated transactions (Muscat, 2009:36). To further reduce costs and manage risks, financial contracts often include provisions for the early discharge of payment obligations through netting. Netting clauses may apply to payments owed in opposite directions (Bamford, 2015:45) or to the termination of obligations following an event of default, in both cases resulting in the calculation of a single net amount.

Due to the widespread use of netting clauses, standard contracts for financial transactions are often referred to as “master netting agreements”. The UNCITRAL Insolvency Guide defines a netting agreement as a type of financial contract between two or more parties that provides for one or more of the following options: (i) the net settlement of payments due in the same currency on the same date, whether by novation or otherwise; (ii) the termination of transactions and the netting amounts due under such transactions into a single net amount upon insolvency or other default by a party; or (iii) the set-off of amounts calculated in accordance with item (ii) under two or more netting agreements⁵.

The Bank for International Settlements (BIS)⁶ defines a master netting agreement as ‘an agreement that permits the netting of amounts owed under transactions governed by

¹ Over-the-Counter (OTC) Markets: Trading and Securities Available at: <https://www.investopedia.com/terms/o/otc.asp> [Accessed 24th November 2024].

² *Marché de gré à gré : principe, avantages et inconvénients* Available at: <https://www.capital.fr/entreprises-marches/marche-gre-a-gre-1374828> [Accessed 24th November 2024].

³ Was ist der OTC-Handel? Available at: <https://www.next-kraftwerke.de/wissen/otc-handel> [Accessed 24th November 2024].

⁴ Specification is the name of a standard contract issued by an exchange or a clearing house. Specifications index, equity, money and commodity derivatives traded at Moscow Exchange are available at <https://www.moex.com/a1904> [Accessed 24th November 2024]; CME Group proposes contract specifications for futures trading in a manner similar to Moscow Exchange. Available at: <https://www.cmegroup.com/education/courses/introduction-to-futures/learn-about-contract-specifications.html> [Accessed 24th November 2024].

⁵ UNCITRAL Insolvency Guide – Legislative Guide on Insolvency Law, 2004, UNCITRAL, Available at: https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/05-80722_ebook.pdf [Accessed 24th November 2024].

⁶ Glossary of definitions of technical terms commonly used in the BIS Quarterly review. Available at: <https://www.bis.org/statistics/glossary.htm?&selection=214&scope=Statistics&c=a&base=term> [Accessed 24th November 2024].

different agreements, often including one or more ISDA Master Agreements”. The ISDA Master Agreement is a framework contract published by the International Swaps and Derivatives Association (ISDA)⁷, a trade association initially established to unite swap dealers (Benjamin, 2007:65). The origins of ISDA can be traced back to the early development of the swaps market. The first reported swap transaction was executed between IBM and the World Bank several years before ISDA was formally established (D’Hollander, 1996:74). As the swaps market grew, the need for standardized documentation and practices became evident, prompting leading swap traders to collaborate and form an industry organization to address these challenges.

Over time, ISDA expanded its activities to encompass all types of derivatives, in addition to swaps. The value of these highly innovative financial instruments is derived from an underlying asset or variable⁸. Such underlying assets may include foreign currency, securities, commodities, interest rates, indexes, or even specific events. Another key characteristic of derivatives is that their performance date typically occurs significantly later than the date of the contract (Benjamin, 2007:65). As a result, parties to derivative trades are often exposed to long-term risks associated with the solvency of their counterparties. The development, drafting, and promotion of standardized documentation for the OTC derivatives industry became a primary goal and one of ISDA’s most significant accomplishments (Flanagan, 2001:228).

ISDA documentation is widely regarded as governing the majority of OTC derivative transactions in the world (Bamford, 2015:45). The remaining portion of cross-border derivative trades is documented using standard contractual instruments developed by other industry associations, such as the Foreign Exchange Committee (FXC) and the European Banking Federation (EBF). Additionally, organizations like the International Capital Market Association (ICMA) and the International Securities Lending Association (ISLA) publish their own master agreements to address the specific needs of parties involved in securities lending and securities repurchase transactions. The rise of China as an emerging superpower has also influenced the domain of contract drafting. In 2022, National Association of Financial Market Institutional Investors (NAFMII), an industry group established by the People’s Bank of China, introduced its first cross-border framework template agreement for derivatives. Known as the 2022 NAFMII Master Agreement (2022 NAFMII MA)⁹, this document was made available to both Chinese and international counterparties, reflecting China’s growing role in the global financial markets.

The terms of the aforementioned international master agreements often overlap and are frequently “taken for granted” (Nasseti, 1995:145). Nearly every contract establishing a framework for the subsequent execution of financial transactions typically includes provisions on trade negotiation and delivery of confirmations¹⁰, undertakings of the parties, representations and warranties, payment netting provisions, and a list of events of default and termination events. Additionally, boilerplate clauses common in international

⁷ ISDA official website. Available at: <https://www.isda.org/> [Accessed 24th November 2024].

⁸ These financial contracts, whose value is derived “from something else” include swaps, options, forwards, and structured products. Their source of value is referred to as the “underlying asset” or simply the “underlying” (Muscat, 2009: 33).

⁹ Refer to: NAFMII Master Agreement (Cross-Border – 2022 Version) (English Translation) Available at: <https://www.nafmii.org.cn/ggtz/gg/202208/P020220831632138066172.pdf> [Accessed 24th November 2024].

¹⁰ A confirmation is not a document different from the framework contract as it is governed by and forms part of the ISDA Master Agreement (Murray, 2012).

commercial transactions – such as severability clauses, governing law and dispute resolution provisions, and delivery of notices – are also included.

The paper argues that one of these clauses warrants separate consideration due to its particular importance for the smooth functioning of OTC derivatives markets.

2. Material and Methodology

This study primarily relies on the texts of international master agreements that include a single agreement clause, which are publicly available on the websites of ISDA, ICMA, ISLA, NAFMII, FXC and EBF. The research also draws on publications of German, English, and American scholars and practitioners. The methodology employed in this article is based on traditional tools commonly used in the humanities and social sciences, including induction, deduction, synthesis, and comparative analysis. Additionally, the author applies the formal legal method, which is typically used in legal disciplines to interpret the contractual provisions of standard master agreements. Given that the standard contractual instruments analyzed in this study have financial implications, the research also incorporates economic data to illustrate the risk mitigation potential of single agreement clauses in these contracts.

3. Discussion

3.1. Overview of Master Netting Agreements

The global financial crisis of 2006–2008 was a significant test for the financial industry, leading to the insolvency of Lehman Brothers, a major transnational investment bank active in OTC markets. While framework contracts largely withstood the crisis (Paech, 2016:36), their provisions were subsequently modified to better accommodate public interests. Unlike the International Capital Market Association (ICMA)¹¹ which focuses on the development of primary¹² and secondary capital markets¹³, ISDA's activities are exclusively centered on market for privately negotiated derivatives, including swaps, options, and forwards. At the forefront of the broad implementation of standard market documentation (Muscat, 2009:36), ISDA introduced its first framework contract in 1987¹⁴, two years following its inception.

Although ISDA is headquartered in New York, its framework agreement quickly gained widespread use in Europe in the years that followed (Yeowart & Parsons, 2016:71). Encouraged by this success, ISDA updated its standard master agreement in 1992. The 1992 ISDA Master Agreement was made available in two versions: Local Currency – Single Jurisdiction¹⁵ and Multicurrency – Cross Border¹⁶. Both versions encompassed a

¹¹ ICMA official website. Available at: <https://www.icmagroup.org/> [Accessed 24th November 2024].

¹² Available at: <https://www.icmagroup.org/market-practice-and-regulatory-policy/primary-markets/> [Accessed 24th November 2024].

¹³ Available at: <https://www.icmagroup.org/market-practice-and-regulatory-policy/secondary-markets/> [Accessed 24th November 2024].

¹⁴ Available at: <https://www.isda.org/book/1987-interest-rate-and-currency-exchange-agreement/> [Accessed 24th November 2024].

¹⁵ 1992 ISDA Master Agreement (Local Currency – Single Jurisdiction) of the International Swaps and Derivatives Association, Available at: <https://www.isda.org/book/1992-isda-master-agreement-local-currency/> [Accessed 24th November 2024].

¹⁶ 1992 ISDA Master Agreement (Multicurrency – Cross Border) of the International Swaps and Derivatives Association, Available at: <https://www.isda.org/book/1992-isda-master-agreement-multi-currency/> [Accessed 24th November 2024].

broader range of OTC derivatives transactions than their predecessor. The most recent framework contract introduced by ISDA, the 2002 ISDA Master Agreement, is designed to document all types of financial derivatives, both domestically and internationally. The structure of ISDA Master Agreements is twofold: the framework contract itself establishes the core terms of the relationship between the parties, while the accompanying schedule allows the parties to make necessary elections and opt out of certain provisions, they find undesirable (Benzler, 1999:38). Unlike the schedule, the ISDA Master Agreement is signed “as is”, without amendments or additional input from the parties (Bobkov, 2020:55).

The 2002 ISDA Master Agreement is widely regarded as the most commonly used framework contract¹⁷ and a “quasi standard for derivatives from global perspective”¹⁸. Other examples of framework contracts for over-the-counter (OTC) derivatives sponsored by international professional associations include the European Master Agreement (EMA)¹⁹, developed by the European Banking Federation (EBF), and a range of master agreements drafted by the Financial Market Lawyers Group (FMLG) under the auspices of the Foreign Exchange Committee (FXC)²⁰.

A notable feature of the EMA is its cross-product nature – the agreement includes a variety of product annexes that address repurchase transactions, securities loans, deposits, derivatives, and interest rate transactions. According to the EBF’s explanatory memorandum, the EMA not only reduces costs but also provides a standardized framework for financial transactions in jurisdictions that lack their own standard documentation. This standardization simplifies and accelerates the documentation process²¹. In addition to its multi-product scope, the EBF highlights the EMA’s innovative and multi-jurisdictional nature, which has made it a popular choice in Europe, particularly for repurchase (repo) transactions (Johansson, 2009:71).

However, the global prospects of the EMA remain uncertain. On the one hand, there is evidence of its use in specific contractual relationships involving European financial institutions, both public and private. For instance, the European Central Bank (ECB) relies on the EMA template for securities repurchase transactions with its counterparties²². Similarly, Belfius Bank reports that nearly 30% of its OTC derivatives transactions are governed by EMA²³. Encouraging evidence also comes from Russia, where the National

¹⁷ Available at: <https://www.kramerlevin.com/images/content/4/3/v2/43362/180726-Lexis-PSL-Kolifraith-Gilles-European-derivatives-master-a7g.pdf> [Accessed 24th November 2024].

¹⁸ Preliminary draft report on: The need for an international instrument on the enforceability of close-out netting in general and in the context of bank resolution. UNIDROIT study group on principles and rules on the netting of financial instruments (Study 78C – Doc. 2). UNIDROIT, Rome, Italy. Report on close-out netting, UNIDROIT 2011 Study 78C – Doc. 2. Available at: <https://www.unidroit.org/english/documents/2011/study78c/s-78c-02-e.pdf> [Accessed 1st November 2024].

¹⁹ Available at: <https://www.ebf.eu/home/european-master-agreement-ema/> [Accessed 24th November 2024].

²⁰ Available at: <https://www.newyorkfed.org/fmlg/documentation/master.html> [Accessed 24th November 2024].

²¹ Master Agreement for Financial Transactions. Explanatory Memorandum for Version 2004 and 2020. Available at: https://www.ebf.eu/wp-content/uploads/2020/06/Explanatory_memorandum_version-2020.pdf [Accessed 24th November 2024].

²² Master agreement for financial transactions between the European Central Bank and Narodowy Bank Polski: Special provisions. Available at: https://www.ecb.europa.eu/ecb/access_to_documents/document/pa_document/shared/data/ecb.dr.par2020_0062ECBagrementeuroNarodowyBankPolski.en.pdf [Accessed 24th November 2024].

²³ European Master Agreement: Experience at Belfius Bank. Available at: https://www.ecb.europa.eu/paym/groups/pdf/omg/2019/201906/2019-06-03_OMG_Item2_European_Master_Agreement_views_of_Belfius.pdf?cc51ea798d701e060edc99e2c48c3fe6 [Accessed 24th November 2024].

Settlement Depository – the local central securities depository and trading repository for financial transactions – has included the EMA in its list of recognized master agreements²⁴.

Unlike ISDA, the European Banking Federation (EBF) has made all of its contractual instruments freely available on its website. This accessibility could serve as a competitive advantage for EBF documentation over ISDA's, particularly for users of standard financial documentation who do not have access to ISDA materials. Another notable advantage of EBF framework is the inclusion of cross-product netting, which enhances risk mitigation possibilities²⁵.

However, it is unlikely that EMA contractual templates will replace ISDA documentation in the foreseeable future. ISDA's framework is deeply integrated into settlement systems on a global scale²⁶, making it the dominant standard. The majority of OTC financial transactions are conducted by G-16 financial institutions from a handful of countries (Braithwaite, 2021:22). These institutions are ISDA members and are likely reluctant to transition to EMA templates due to their strong ties to ISDA and their extensive use of its contractual documentation.

Additionally, promoting the laws of EU countries as the governing framework for financial markets would require challenging the Anglo-Saxon dominance in derivatives and other financial products. This shift would take considerable time and effort, likely longer than EBF and its proponents anticipate.

FXC master agreements are designed to document obligations and provide common legal terms for transactions within the foreign currency sector, including spot transactions, forwards, and options. The first contractual template published under the auspices of the FXC was the International Bullion Master Agreement in 1994. In 1997, FXC significantly expanded its contractual offerings with the publication of the International Currency Options Market Master Agreement (ICOM)²⁷ for currency options and the International Foreign Exchange Mast Agreement (IFEMA)²⁸ for foreign currency transactions. IFEMA provided a standardized framework for documenting the trading of simple foreign currency instruments and options. The most recent FXC standard instrument, the International Foreign Exchange and Currency Option Master Agreement (IFXCO)²⁹, was introduced in 2005.

The ICMA Global Master Repurchase Agreement (GMRA)³⁰, dated 2011, is the latest version of a master agreement for securities repurchase transactions. It replaced earlier versions of ICMA's standard framework contract published in 2000 and 1995. Similarly, the Global Master Securities Lending Agreement (GMSLA), a framework contract for

²⁴ Available at: [https://repository.nsd.ru/en/versioned/current/taxonomy/master-agreement-type\(nsd\)](https://repository.nsd.ru/en/versioned/current/taxonomy/master-agreement-type(nsd)) [Accessed 24th November 2024].

²⁵ Das European Master Agreement – die europäische Lösung für Cross-Product Netting. Available at: <https://www.zbb-online.com/heft-6-2009/zbb-2009-451-das-european-master-agreement-die-europaeische-loesung-fuer-cross-product-netting/> [Accessed 24th November 2024].

²⁶ Welches Master Agreement ist das Beste? Available at: <https://bahlconsult.com/welches-master-agreement-ist-das-beste/> [Accessed 24th November 2024].

²⁷ NSD's trade repository messages specifications. Available at: <https://www.newyorkfed.org/medialibrary/microsites/fmlg/files/icom.pdf> [Accessed 24th November 2024].

²⁸ Available at: <https://www.investopedia.com/terms/i/ifema.asp> [Accessed 24th November 2024].

²⁹ 2005 International Foreign Exchange and Currency Option Master Agreement by the Foreign Exchange Committee, Available at: https://www.newyorkfed.org/medialibrary/microsites/fxc/files/ifxco_booklet.pdf [Accessed 24th November 2024].

³⁰ Available at: https://www.asifma.org/wp-content/uploads/2018/05/nafmii_master_agreement_2009.pdf [Accessed 24th November 2024].

securities lending transactions promoted and maintained by ISLA, was issued in 2010, following earlier versions of 2009 and 2000.

In China, the Inter-Bank Market Financial Derivatives Master Agreement, developed by the National Association of Financial Market Institutional Investors (NAFMII)³¹, allows parties to conclude financial derivative transactions under the laws of the People's Republic of China. Recently, NAFMII introduced a competitor to ISDA templates by publishing the first Chinese law-based master agreement. The NAFMII Master Agreement (Cross-border – 2022 Version) (the 2022 NAFMII MA)³² includes all standard provisions found in other international framework contracts. Additionally, it is supplemented with annexes that provide credit support under both title transfer arrangements and pledge structures³³.

Separate transactions under ISDA, GMRA, GMSLA, EMA, NAFMII and FXC agreements are documented using a “confirmation”, a document that outlines the terms of relevant derivative trade, repurchase contract, or securities lending transaction. While the parties may agree on the terms of a single transaction electronically or even by phone, the absence of a confirmation does not typically render the transaction invalid. However, confirmations serve as valuable evidence of the agreed terms of OTC trades. Standard terms for agreements and template confirmations are often included in the “definitions”. For instance, ISDA 2006 Definitions³⁴ provide provisions for interest rate transactions, while the 1998 FX and Currency Option Definitions³⁵ outline the terms for forwards, options, and FX spot transactions. Other examples include ISDA Equity Derivatives Definitions³⁶, ISDA Credit Derivatives Definitions³⁷, and ISDA Commodity Derivatives Definitions³⁸.

International framework agreements are often supplemented by annexes and additional protocols designed to mitigate risks or address legal and regulatory requirements. One such example is the ISDA Credit Support Annex (CSA)³⁹, which serves both purposes. On the one hand, collateral arrangements under CSA are widely recognized as an effective risk mitigation technique in wholesale financial markets (Johansson, 2009:72). On the other hand, the CSA facilitates compliance with mandatory rules governing the use of collateral for non-centrally cleared derivatives⁴⁰. Bilateral collateral transfers between the parties to ISDA agreements can also be structured using documents such as 1995 ISDA Credit Support Deed (Security Interest – English Law)⁴¹, the 1994

³¹ Available at: https://www.asifma.org/wp-content/uploads/2018/05/nafmii_master_agreement_2009.pdf [Accessed 24th November 2024].

³² Available at: <https://www.nafmii.org.cn/ggtz/gg/202208/P020220831632138066172.pdf> [Accessed 24th November 2024].

³³ Available at: <https://www.kwm.com/cn/en/insights/latest-thinking/mastering-cross-border-derivatives-in-china-the-new-2022-nafmii-master-agreement-cross-border-version0.html> [Accessed 24th November 2024].

³⁴ Available at: <https://www.isda.org/book/2006-isda-definitions/> [Accessed 24th November 2024].

³⁵ Available at: <https://www.isda.org/book/1998-fx-and-currency-option-definitions/> [Accessed 24th November 2024].

³⁶ Available at: <https://www.isda.org/book/2002-isda-equity-derivatives-definitions/> [Accessed 24th November 2024].

³⁷ Available at: <https://www.isda.org/book/2014-isda-credit-derivative-definitions/> [Accessed 24th November 2024].

³⁸ Available at: <https://www.isda.org/book/1993-isda-commodity-derivatives-definitions/> [Accessed 24th November 2024].

³⁹ Available at: <https://www.isda.org/books/#jump-1> [Accessed 24th November 2024].

⁴⁰ Refer, for instance, to Regulation (EU) No 648/2012 of the European Parliament and the Council of 4th July 2012 on OTC derivatives, central counterparties and trade repositories. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32012R0648> [Accessed 24th November 2024].

⁴¹ Available at: <https://www.isda.org/book/1995-isda-credit-support-deed-pdf/> [Accessed 24th November 2024].

ISDA Credit Support Annex (Security Interest – New York Law)⁴² and other similar agreements⁴³.

Nevertheless, parties to ISDA Agreements may choose more traditional methods of securing obligations and mitigating credit risks arising from their derivatives transactions. ISDA documentation introduces the concepts of “credit support document” and a “credit support provider” (Harding 1999:179). For instance, a third party may provide a guarantee or suretyship to secure the obligations of a counterparty under the master agreement, even though ISDA has developed its own risk mitigation mechanism in the form of “financial collateral”, described above.

In many respects, financial collateral is comparable to the initial and variation margin posted by participants in organized trading on securities, commodities, and foreign currency exchanges. However, collateral addendums to international master agreements extend these risk mitigation tools to participants of over-the-counter (OTC) financial markets.

Other annexes, protocols, and addendums are often designed to align the standard documentation of international associations with local legal and regulatory requirements. For example:

- The ISDA 2018 U.S. Resolution Stay Protocol⁴⁴ was introduced to facilitate compliance with regulations issued by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency.
- The EMIR Annex to the Master Agreement for Financial Transactions (2002 Edition)⁴⁵ enables parties to comply with certain regulatory requirements under the EMIR Regulation, excluding those related to the collateralization of derivatives.
- The GMRA 2011 Russian Annex⁴⁶ was developed to align Russian insolvency law requirements regarding close-out netting for securities repurchase transactions, thereby ensuring the enforceability of this framework contract in Russian courts.

3.2. The Single Agreement Concept: Clauses, Governing Law, and OTC Transactions

According to the definition provided by the Bank for International Settlements, a master agreement “*sets forth the standard terms and conditions between two parties that apply to all or a defined subset of transactions that the parties to the agreement may enter*

⁴² Available at: <https://www.isda.org/book/1994-isda-credit-support-annex-security-int-ny-law/> [Accessed 24th November 2024].

⁴³ FXC Collateral Annex <https://www.newyorkfed.org/fmlg/documentation/collateral.html> EBF Margin Maintenance Annex Available at: https://www.ebf.eu/wp-content/uploads/2020/06/EMA-Margin-Maintenance-Annex_-2020.pdf [Accessed 24th November 2024]; Collateral Addendum of the German Banking Association https://bankenverband.de/media/uploads/2019/07/04/bsa-2018-eng-44520_0918a_muster.pdf [Accessed 24th November 2024].

⁴⁴ Available at: <https://www.isda.org/protocol/isda-2018-us-resolution-stay-protocol/> [Accessed 24th November 2024].

⁴⁵ Available at: [ebf.eu/wp-content/uploads/2020/06/EMA-EMIR-Annex_2020.pdf](https://www.ebf.eu/wp-content/uploads/2020/06/EMA-EMIR-Annex_2020.pdf) [Accessed 24th November 2024].

⁴⁶ Available at: <https://www.icmagroup.org/assets/documents/Legal/2018/Annexes/2018-RUSSIAN-ANNEX-TO-GMRA-2011.pdf> [Accessed 24th November 2024].

into from time to time”⁴⁷. The application of these standard terms to the relevant transactions is based on the concept of the “single agreement”⁴⁸. This concept is embodied in the “single agreement clause” found in framework contracts. The idea behind the concept and the corresponding clause is straightforward: the master agreement and the transactions concluded under it form a single, unified contract between the parties, even if the transactions are not physically bundled into one document physically or are concluded through different means.

The concept of the single agreement was originally developed by American jurists (Benzler, 1999: 130). However, German scholars are also familiar with this principle, which is known in Germany as “*Einheitsvertragsonzeption*” (Benzler, 1999: 130). The *Deutscher Rahmenvertrag für Finanztermingeschäfte* (DRV), governed by German law, incorporates the single agreement principle to the same extent as its English and New York law-governed counterparts. Clause 1 (2) of the DRV states: “*All transactions shall – in relation to each other and together with this Master Agreement – constitute a single agreement...; they shall be entered into in view of an integrated risk assessment and on the basis of and in reliance on this understanding*” (Böhm, 2001: 112).

The same principle is reflected in other master agreements developed by the German Banking Union, such as the *Deutscher Rahmenvertrag für Wertpapierpensionsgeschäfte* (Repos)⁴⁹ for repurchase transactions and the *Deutscher Rahmenvertrag für Wertpapierdarlehen*⁵⁰ for securities lending.

The single agreement clause first appeared in 1987 ISDA Interest Rate Swap and Currency Exchange Master Agreement⁵¹. The relevant wording, included in the preamble to the framework contract stated:

“Each Confirmation constitutes a supplement to and forms part of this document and will be read and construed as one with this document, so this document and all the Confirmations constitute a single agreement between the parties (collectively referred to as this “[Agreement]”). The parties acknowledge that all Swap Transactions are entered into in reliance on the fact that the parties would not otherwise enter into any Swap Transactions.”

This concept was further refined in the 2002 ISDA Master Agreement, where section 1(c) states:

“All Transactions are entered into in reliance on the fact that this Master Agreement and all Confirmations form a single agreement between the parties (collectively referred to as this “Agreement”), and the parties would not otherwise enter into any Transactions.”

Thus, ISDA’s interpretation of the single agreement concept is twofold:

⁴⁷ Available at: <https://www.bis.org/cpmi/publ/d00b.htm?&selection=169&scope=CPMI&c=a&base=term> [Accessed 24th November 2024].

⁴⁸ In this article the principle of a single agreement will also be referred to as a “single agreement principle”, “single agreement concept” or the “concept of a single agreement”.

⁴⁹ Available at: https://bankenverband.de/media/contracts/44515_0918__muster_dr.pdf [Accessed 24th November 2024].

⁵⁰ Available at: <https://bankenverband.de/service/rahmenvertraege-fuer-finanzgeschaefte/deutscher-rahmenvertrag-fur-wertpapierpensionsgeschaeft-repos/> [Accessed 24th November 2024].

⁵¹ Available at: <https://bankenverband.de/service/rahmenvertraege-fuer-finanzgeschaefte/deutscher-rahmenvertrag-fur-wertpapierdarlehen/> [Accessed 24th November 2024].

- The framework contract and all confirmations related to individual transactions together constitute a single agreement.

- The parties rely on this principle, acknowledging that they would not have entered into the framework contract or individual transactions in the absence of the single agreement clause.

In comparison, Paragraph 13 of the GMRA, which contains the single agreement clause for repo transactions, is even more detailed than the clauses developed by the German Banking Union and ISDA. Under the GMRA single agreement clause, each party acknowledges that it has entered into the framework agreement in consideration and reliance upon the fact that all transactions under the agreement constitute a “single business and contractual relationship between the parties”. Furthermore:

- A default in the performance of obligations under one transaction constitutes a default under all transactions.

- Payments, deliveries, and transfers made by either party under one transaction are made in consideration of payments, deliveries, and transfers under any other transaction.

This comprehensive approach ensures that all transactions under the GMRA are interconnected, reinforcing the single agreement principle and its role in mitigating risk and ensuring enforceability.

The single agreement clause present in the European Master Agreement (EMA) reads as follows:

“The Agreement constitutes a single contractual relationship. Accordingly, (i) each obligation of a party under any Transaction is incurred and performed in consideration of the obligations incurred and to be performed by the other party under all Transactions, and (ii) unless otherwise agreed, a failure by a party to perform an obligation under any Transaction shall constitute a failure to perform under the Agreement as a whole. The parties enter into the Master Agreement between them and each Transaction thereunder in reliance on these principles, which they consider fundamental to their risk assessment”.

A similar single agreement principle, comparable to the one used in the Global Master Repurchase Agreement (GMRA), is found in Article 17 of the Global Master Securities Lending Agreement (GMSLA):

“Each Party acknowledges that, and has entered into this Agreement and will enter into each Loan in consideration of and in reliance upon the fact that, all loans constitute a single business and contractual relationship and are made in consideration of each other.”

The FXC-sponsored IFXCO also incorporate the single agreement principle in Section 1.2, which states:

“Adherence Agreement (the Terms and the Adherence Agreement being the “Master Agreement”), the terms agreed to between the Parties with respect to each FX Transaction and Currency Option Transaction (and, to the extent recorded in a Confirmation, each such Confirmation), and all amendments to any of such items shall together form the agreement between the Parties (the “Agreement”) and shall together constitute a single agreement between the Parties. The Parties acknowledge that all FX Transactions and Currency Option Transactions are entered into in reliance upon such fact, it being understood that the Parties would not otherwise enter into any FX Transaction or Currency Option Transaction.”

Thus, the principle of a “single agreement”, which addresses the critical goal of consolidating various elements of standard documentation for OTC financial transactions into one unified contract, is a fundamental feature of every standard master agreement governing cross-border financial transactions.

The National Association of Financial Market Institutional Investors (NAFMII) also adopted this approach, following the practices of its Western counterparts. Section 1(I) of the 2022 NAFMII Master Agreement (MA) states that the master agreement, its supplements, and effective transactions agreements together constitute a single and complete agreement between the parties. Notably, NAFMII has introduced the same clause in its domestic standard contracts for derivatives⁵². However, the domestic master contract for securities lending transactions only refers to the “completeness” of agreements between the parties, without explicitly referencing the single agreement principle.

Single agreement clauses can also be found in Spanish⁵³, French⁵⁴ and Russian⁵⁵ contracts for OTC derivatives transactions. These contracts primarily target domestic financial markets, although occasional cross-border use may occur. Therefore, it is not an exaggeration to state that the single agreement concept is embedded in nearly every industry-wide master agreement used in international financial markets. Without this principle and the corresponding clause in the master agreement, transactions under a framework agreement would have an independent character (Böhm, 2001: 137), even if the confirmations reference the relevant master agreement. The technical role of the single agreement clause should not be underestimated, especially given the vast variety of standard documentation instruments available.

For instance, the European Banking Federation (EBF) sponsors the issuance of several product-specific annexes, including the Product Annex for Repurchase Transactions, Product Annex for Securities Loans Transactions, Margin Maintenance Annex for Repurchase Transactions and Securities Loans, Deposit Annex, Derivatives Annex, Index of Defined Terms, and the Interest Rate Transactions and Clearing Annex. Similarly, the German Banking Union and Russian financial associations such as NAUFOR, ARB and NFA publish product annexes for their local standard documentation. These annexes typically include confirmation templates for specific types of transactions. Together with the master agreement, its schedule (if applicable), and each confirmation, these documents form a single agreement between the parties, effectively consolidating otherwise scattered elements of standard documentation.

Uniting various parts of standard documentation into a single contract is also significant from the perspective of governing law. The inclusion of choice-of-law provisions is a common feature of international master agreements for financial transactions (Böger, 2013: 237). For instance,

- The 1992 ISDA Master Agreement and the 2002 ISDA Master Agreement may be governed by either English law or the laws of New York, depending on the parties' choice⁵⁶.

⁵² Available at: <https://www.isda.org/book/1987-interest-rate-and-currency-exchange-agreement/> [Accessed 24th November 2024].

⁵³ Available at: https://www.asifma.org/wp-content/uploads/2018/05/nafmii_master_agreement_2009.pdf [Accessed 24th November 2024].

⁵⁴ Available at: <https://www.fbf.fr/en/about-us/master-agreements/> [Accessed 24th November 2024].

⁵⁵ Available at: <http://spfi.info> [Accessed 24th November 2024].

⁵⁶ Users of an ISDA Master Agreement specify the applicable law in the schedule (annex) to the agreement. The selected law – either England law or the laws of New York – will govern the agreement and all related

- In anticipation of Brexit, ISDA published framework contracts governed by Irish and French law in 2018⁵⁷, although prior to this, the association had consistently preferred common law jurisdiction to govern its documents.

- The European Master Agreement (EMA) allows parties to specify the applicable law in the special provisions section, which serves as a schedule to its master agreements. If the parties fail to make a choice regarding the applicable law, the laws of the country where the parties have their offices will apply.

- According to the Global Master Repurchase Agreement (GMRA), the agreement and non-contractual obligations arising out of or in connection with it are governed by and interpreted in accordance with English law.

- The NAFMII 2002 Master Agreement is governed by the laws of the People's Republic of China.

The single agreement principle resolves the governing law issue for individual financial transactions, as the law selected in the master agreement automatically applies to all trades conducted under the framework contract. But what would happen if the governing law issue for transactions was not resolved through a combination of the single agreement principle and the governing law clauses in the master agreement? In such a scenario, the parties would need to determine the applicable law for each individual transaction, as the relationship between the governing law of the master agreement and the transactions themselves is not always straightforward.

While including a governing law clause in a written confirmation may seem simple, the process becomes more complex when transactions are executed electronically or when trades are conducted orally, such as over the telephone.

In the absence of a chosen applicable law, the rules of private international law come into effect. In such cases, the parties would need to rely on fallback conflict-of-laws principles applied in their respective jurisdictions. When determining the applicable law for a contract, courts typically look for the country to which a contract is most closely connected. Another widely recognized connecting factor is the law of the country where the party performing the characteristic obligation of the contract is domiciled⁵⁸.

This rule is broadly accepted in many jurisdictions and is embedded in instruments such as Rome I Regulation⁵⁹, the Civil Code of the Russian Federation⁶⁰, and other national laws and international frameworks.

Relying solely on fallback rules presents significant challenges for many cross-border derivatives transactions. For instance, S. James highlights the difficulty in identifying the party providing characteristic performance in swap and foreign exchange transactions (James, 1999: 208). Similarly, Yeowart and Parsons emphasize the complexities of determining characteristic performance in interest rate swap contract where both parties

elements of the ISDA documentation. It is important to note that the ISDA Master Agreement cannot be governed by both laws simultaneously.

⁵⁷ Available at: <https://www.lexology.com/library/detail.aspx?g=001c8339-4791-460a-9d50-4b029620d947> [Accessed 24th November 2024].

⁵⁸ The term was coined in Swiss doctrine and developed in Swiss courts (Lipstein, 1981).

⁵⁹ Regulation (EC) No 593/2008 of the European Parliament and of the Council of June 17, 2008 on the law applicable to contractual obligation. Available at: <https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A32008R0593> [Accessed 24th November 2024].

⁶⁰ Article 1211 of the Civil Code of the Russian Federation. Available at: <https://www.consultant.ru/cons/cgi/online.cgi?req=doc&rnd=FtvNuA&base=LAW&n=452892&cacheid=B7A43533781564275372222E3A3E5257&mode=rubr#KzBJWtToXo27VS1q> [Accessed 24th November 2024].

make payments (Yeowart & Parsons, 2016: 299). These difficulties in ascertaining the governing law for contracts within international financial markets underscore the utility agreement concept for parties involved, as well as for judges and arbitrators resolving related disputes.

3.3. Single Agreement Concept, Close-out Netting and Mitigating Cherry-Picking Risk

According to the ISDA 2002 Guide⁶¹, the single agreement provision establishes that each confirmation does not represent a separate agreement between the parties. Instead, all confirmations form part of a single, overarching agreement. This principle is fundamental to the operation of close-out netting, a crucial mechanism for risk mitigation in international financial markets. This is particularly significant given that the ISDA itself was established to manage risks in derivatives market (Muscat, 2009: 36).

Beyond its technical and conflict-of-laws implications, the single agreement concept also facilitates the smooth functioning of close-out netting provisions within industry framework agreements. This third implication, which will be explored in this article, is arguably the most significant. Contract drafting techniques allow parties to address challenges related to the lack of connection between elements of contractual documentation and private international law issues, further reinforcing the importance of the single agreement concept.

Under clause 21 of the UNIDROIT Principles on the Operation of Close-out Netting Provisions⁶², a close-out netting clause may be included into a standard master documentation, a non-standard framework agreement, or even as a self-standing document. The mechanism of close-out netting, as well as netting in general, warrants closer examination. In the realm of international banking settlements, netting first gained international

prominence with the publication of Angell Report by the Bank for International Settlements in 1989⁶³. This report, prepared by a group of G-10 experts who convened in Basel, examined internationally related netting arrangements. Section 5 of the Angell Report, which focused on the legal types of netting, identified several forms: position netting, binding payments netting, netting by novation, novation and substitution, and netting by close-out.

Although several decades have passed since the publication of the first comprehensive study on netting, its importance endures due to its potential for risk reduction (Nassetti, 1995:145). According to more recent research, participants in international financial markets primarily rely on four major forms of netting: payment netting, close-out netting, netting by novation and multilateral netting (Loizou, 2012:429). Multilateral netting, which requires the involvement of a clearinghouse (Derham, 1991:536), is more likely to occur on a securities exchange rather than within a standard industry master agreement.

In contrast to other types of netting, such as netting by novation or settlement netting, close-out netting provisions become effective upon the occurrence of a default event. Such

⁶¹ Available at: <https://www.isda.org/book/ug-to-2002-isda-master-agreement/> [Accessed 24th November 2024].

⁶² Available at: <https://www.unidroit.org/instruments/capital-markets/netting/> [Accessed 24th November 2024].

⁶³ Angell Report – Report on Netting Schemes, Bank for International Settlements, 1989. Available at: <https://www.bis.org/publ/cps02.pdf> [Accessed 24th November 2024].

events may include the initiations of insolvency proceedings, material license revocation, credit rating deterioration, or the failure to settle a financial transaction.

The use of close-out netting has become widespread in financial markets over the past few decades (Böger, 2013:234). Today it serves as a “core” component⁶⁴ and a “principal block” of master agreements in the financial markets (Paech, 2016:862). This contractual mechanism provides an effective means of mitigating financial risks associated with international financial markets (Benzler, 1999:37). However, close-out netting differs from set-off, as it incorporates unique elements not typically found in set-off, such as the termination or acceleration of obligations (Böger, 2013:235). As a result, it is often regarded in scholarly literature as a *sui generis* instrument (Benzler, 1999:56).

Close-out netting typically exists as a contractual clause present in an agreement within an agreement or as part of the rules governing organized trading and settlement. It has gained global recognition as a crucial risk mitigation tool, alongside collateral arrangements for the transfer of financial collateral in the form of cash and securities (Fuchs, 2013: 5). Yeowart and Parsons identify two models of close-out netting provided for in master documentation for over-the-counter financial transactions: “set-off” and “conditional novation” (Yeowart, Parsons, 2006: 54). The first model is embedded into ISDA master documentation, while the second is commonly used for closing out claims under repurchase and securities lending transactions governed by GMRA and GMSLA master agreements.

Let us examine the specific features of close-out netting procedures under ISDA standard documentation. Both 1992 and 2002 ISDA Master Agreements outline several events that may trigger the termination of dealings between the parties. These events are divided into two categories: events of default and termination events.

- Events of default are generally within the control of a party to the framework contract. These include failure to pay or deliver, insolvency, cross-default, breach of representation, repudiation of the agreement, default under a specified transaction, and merger without assumption.

- Termination events, on the other hand, are external in nature and cannot typically be prevented by the end-user of an over-the-counter financial instrument. These include illegality, tax events upon merger, and, in the case of the 2002 ISDA Master Agreement, force majeure.

Illegality arises when the performance of obligations under the framework contract or individual transactions becomes unlawful, either due to statutory law or case law. Force majeure events include acts of God, strikes, wars, and other circumstances that impede the performance of relevant transactions. Additionally, the parties may specify additional termination events in the schedule to the master agreement. Common examples include a change of control with respect to a party, material adverse change, and rating events.

In contrast, the GMRA and GMSLA frameworks have a simpler structure. These agreements do not include termination events; instead, the close-out netting procedure is triggered solely by events of default. These events include failure to pay, deliver, or make margin transfers, insolvency acts, violation of representations, and other specified grounds. Similarly, the General Provisions (Edition 2020) of the EMA distinguish between the termination due to an event of default (e.g., failure to pay, deliver, or post required margin

⁶⁴ Systemic risk, regulatory powers and insolvency law – The need for an international instrument on the private law framework for netting. Available at: https://www.ilf-frankfurt.de/fileadmin/_migrated/content_uploads/ILF_WP_116.pdf [Accessed 24th November 2024].

payment or securities, cross-default, repudiation of the agreement) and termination due to a change of circumstances, such as changes in taxation, illegality, or impossibility.

Close-out netting under ISDA Master Agreements differs depending on whether it is triggered by an event of default or a termination event. Firstly, in the case of an event of default, all transactions between the parties are terminated. In contrast, for termination events, only the transactions affected by the relevant event are subject to close-out. Secondly, termination events often allow for grace periods or the assignment of obligations to another party, providing flexibility to the affected party. Lastly, in the case of the most critical event of default – insolvency – close-out netting may occur automatically if the parties have included such a provision in the schedule to the master agreement.

The automatic nature of close-out netting in insolvency cases underscores its importance, particularly during periods of financial instability. The surge in litigation involving derivatives during times of financial turmoil (Braithwaite, 2012: 792) highlights the significance of insolvency as a default event. In such cases, all transactions between the parties are terminated, and the resulting net amount is calculated retrospectively as part of the bankruptcy proceedings.

Furthermore, the likelihood of a net amount claim arising as a result of close-out netting being presented during insolvency proceedings is high, given the presence of other events of default that indicate the deteriorating financial condition of a counterparty. This is equally true for close-out netting under various other master agreements, both cross-border and domestic. In cases of insolvency, the enforceability of close-out netting provisions ceases to be a matter of *lex contractus* (the law governing the contract) and instead becomes an issue of insolvency law (Böger, 2013: 250).

In many jurisdictions, insolvency laws grant administrators so-called “cherry picking rights” – the ability to reject the unprofitable or burdensome transactions while demanding performance of contracts deemed advantageous to the creditors of the insolvent entity. This poses a significant risk to the enforceability of close-out netting provisions, as cherry-picking can undermine the integrity of the netting process.

There is strong evidence that single agreement principle plays a critical role in the operation of close-out netting. Under this principle, the resulting net amount is treated as a single contractual claim, rather than as the outcome of set-off across multiple unrelated contractual arrangements. As a result, the insolvency administrator is entitled to either accept or reject the net amount payment as a whole, rather than cherry picking profitable financial contracts from among the transactions concluded under the same master agreement. Thus, single agreement clauses, which are common elements of cross-border and domestic framework netting agreements, are of vital importance (Harding, 2004: 35). These clauses significantly reduce the so-called “cherry picking risk” – the possibility of an insolvency administrator rejecting unprofitable financial contracts while assuming obligations under trades that increase the estate of the defaulting party to the master agreement (Benzler, 1999: 55).

Russian insolvency statute also incorporates the single agreement (referred to as *edinyj dogovor* in Russian). To facilitate the smooth application of close-out netting under master agreements for financial contracts, relevant domestic laws provide safe harbor protections⁶⁵. Specific provisions within the Russian insolvency statute support the single

⁶⁵ Refer to Articles 4.1, 142 (13), 189.96 (35) of the Federal Law No. 127-FZ On Insolvency (Bankruptcy) dated October 26, 2002 (as amended). Available at: <https://base.garant.ru/558050518/> [Accessed 24th November 2024].

agreement principle, address the cherry-picking risk, and create exceptions to the general prohibition on insolvency set-off.

In recent years, Russian courts have shifted their traditionally restrictive approach to the ban on insolvency set-off, allowing a specific type of offsetting known as *sal'dirovanie*⁶⁶. However, due to the explicit safe harbor rules, close-out netting remains unaffected by this new approach. The termination of obligations through close-out netting is already enforceable under Russian law, ensuring the continued protection of netting arrangements in insolvency scenarios.

4. Conclusion

The role of the single agreement rule is threefold, ranging from a purely technical to the prevention of ‘cherry picking’ by an insolvency administrator with respect to transactions profitable for the insolvency estate.

The first, and most obvious technical role is to consolidate the agreement and its accompanying elements, such as annexes, confirmations, protocols, addenda, and other related documents, into a single, unified agreement. While this role may initially seem less significant, the sheer number of additional elements that typically accompany an ISDA Master Agreement highlights the necessity of such a unifying principle. These inter-related documents require a link, and the single agreement rule provides that essential connection.

Secondly, the single agreement concept addresses the governing law issue, which can pose challenges for derivatives and other financial transactions. By treating all related documents as part of a single agreement, the concept allows the parties to handle governing law issues in an efficient and unambiguous manner, reducing the potential for legal disputes.

Finally, and most critically, the absence of a single agreement clause would create opportunities for insolvency officials to exploit the changing value of over-the-counter transactions. Without the single agreement principle, insolvency administrators could exclude certain transactions from the close-out netting calculation, cherry-picking those that are unfavorable to the insolvency estate while retaining those that are profitable. The single agreement rule prevents this by ensuring that all transactions under the master agreement are treated as part of a single, indivisible framework.

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⁶⁶ As German commentators have put it, “*Saldierung keine Aufrechnung sind*”. Available at: https://www.advant-beiten.com/fileadmin/beiten/Flyer_2024/Regulierung_des_Insolvenzverfahrens_in_Russland_Flyer_ADVANT_Beiten.pdf [Accessed 24th November 2024].

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