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THE FRENCH LAW ISDA MASTER AGREEMENT, A CIVIL LAW ALTERNATIVE POST BREXIT

On 31 January 2020 the United Kingdom ("**UK**") left the European Union ("**EU**") and entered into a transition period (currently planned to end on 31 December 2020) during which EU law will continue to apply to and in the UK, even though the UK is no longer an EU member state.

Although the UK and the EU have set out their positions on their future relationship, the negotiations have been protracted and are ongoing. As the end of the transition period approaches fast, great uncertainty remains regarding the precise shape of the future relationship between the UK and the EU.

Since the Brexit referendum took place in June 2016, France has implemented an ambitious strategy to develop Paris as a prime European financial centre and to incentivise international banking and financial institutions (in particular parties to derivatives agreements) to select Paris as their place of business and destination of choice for international dispute resolution.

Amongst the most significant measures taken in pursuit of this objective were: the signature of two protocols relating to the procedural rules applicable to the international chamber of the Paris Commercial Court (the "**ICCC**") and the international chamber of the Court of Appeal of Paris (the "**ICCA**") in February 2018 (respectively the "**ICCC Protocol**" and the "**ICCA Protocol**", and together the "**Protocols**"); the publication of a French law version of the 2002 ISDA Master Agreement in June 2018 (the "**French law ISDA**"); and the publication by the French government of an ordinance relating to the withdrawal of the UK from the EU in February 2019 (the "**Brexit Ordinance**")[1].

So far, these steps have not had the desired results; in particular use of the French law ISDA has been slow to get off the ground. But now that Brexit has happened and given that the terms of the future relationship between the UK and the EU remain uncertain, the advantages of the French law ISDA may finally become more apparent to market participants and result in increased use.

The French law ISDA deviates little from the English law ISDA

The French law ISDA was developed by the International Swaps and Derivatives Association ("**ISDA**") to provide institutions with an option, on the UK leaving the EU, to continue trading derivatives under an ISDA Master Agreement governed by an EU member state law and containing EU court jurisdiction clauses.

The French law ISDA is the first version of an ISDA Master Agreement governed by a civil law system[2]. In order to facilitate its adoption by market participants, the approach taken was to deviate as little as possible from the 2002 Master Agreement governed by English law (the "**English law ISDA**") which is predominantly used in the market (and well known by market participants) and to limit changes only to clarifications / technical adaptations which were strictly necessarily in order to comply with French law.

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[1] Ordinance n° 2019-75 dated 6 February 2019 relating to the contingency measures for the withdrawal of the United Kingdom from the European Union in respect of financial services.
[2] The ISDA Master Agreements are governed by English law or the law of the State of New York (and since June 2018, by Irish law) which are all common law systems.

The main deviations of the French law ISDA from the English law ISDA are as follows:

- **Section 2(a)(iii) - Flawed Assets**. The provision was adapted to maintain the proper functioning and effect of the flawed asset mechanism (which has no equivalent under civil law) but using the principles of the French Civil Code as the legal basis. The flawed asset provisions have been highly debated in the context of the Lehman Brothers bankruptcy, leading to conflicting case law in the UK and in the US[3] and to the publication by ISDA of amendments to Section 2(a)(iii) to insert a time limit. That standard wording developed by ISDA was reproduced with no modification in the French law ISDA.

- **Section 2(c) - Netting of Payments.** Payment netting under French law does not operate by way of novation (as under English law) but as a means of payment. The provision was adapted to reflect that conceptual difference but the change does not have any consequence in practice for the negotiation of the French law ISDA.

- **Section 3 - Representations.** The reference to 'equity as a source of law' was deleted as equity is a concept specific to common law. The word '*équité*' was retained as it is important in relation to the French law principle of interpretation of the intention of the parties. A reference to *'bonne foi*' (good faith), a very important French law principle, was also added[4].

- **Sections 9(f) - No Waiver of Rights.** A party which has not exercised a right under the ISDA Master Agreement is not deemed to have waived it. The provision was adapted to take into account French law on time limitations (*délais de prescription*) applicable to contractual obligations: these may be shortened but not extended.

- **Section 13 - Governing Law / Jurisdiction / Process Agent.** French law was specified as the governing law and jurisdiction was granted to the Commercial Court and Court of Appeal in Paris (either on an exclusive or non-exclusive basis at the election of the parties to be made in the Schedule to the French law ISDA)[5]. The service of process provisions were adapted to refer to the equivalent French concept of 'Election of Domicile'. Election of domicile is not mandatory under French law and it is therefore up to the parties to elect domicile or not for the purpose of the French law ISDA.

It is worth noting that since the Brexit Ordinance[6], there is no more need to modify the standard ISDA provisions regarding compounding of interest. Under French law, interest can only be compounded if due for over one year[7]. The Brexit Ordinance modified that point for derivatives contracts and, derogating from French law principles, permitted compounding of interest (*anatocisme*) due for less than a year under a master agreement governing derivatives

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[3] In *re Lehman Brothers Holdings, Inc, et al* (Case No 08-13555 (JMP) Bankr SDNY, 15 September 2009) and *Lomas v JFB Firth Rixson Inc*. [2012] EWCA Civ 419.

[4] Pursuant to Article 1104 of the French Civil Code, *"contracts must be negotiated, concluded and performed in good faith. This provision is of public order".*

[5] The form of Schedule attached to the French law ISDA also provides an option for arbitration. The provisions reflect the ISDA arbitration guide. Note that the *Haut Comité Juridique de Place* in Paris published a report in respect of arbitration for banking and financial disputes, that could also facilitate the use of the French law ISDA.

[6] The Brexit Ordinance is part of the wider strategy to develop Paris as a prime European financial centre. It provides in particular for two changes aimed at adapting certain aspects of French law to derivatives contracts and therefore supporting the adoption of the French law ISDA. In addition to the change to compounding of interest, the Brexit Ordinance extends the scope of the close-out netting to Spot FX transactions and sale, purchase and delivery of precious metals and transactions relating to CO2 allowances, removing uncertainty as to the enforceability of the close-out netting in respect of ISDA Master Agreements covering such type of transactions.

[7] Article 1343-2 of the French Civil Code.

transactions (which is in line with the English law ISDA, where compounding of interest applies from the first day of non-payment).

These changes between the French law ISDA and the English law ISDA have very little impact in practice on the negotiation of the French law ISDA (which is a significant advantage for institutions: there is no need to specifically train ISDA negotiation teams on a new type of Master Agreement or put in place new negotiation policies).

The adoption of the French law ISDA by market participants will ultimately depend on the willingness of institutions and their legal departments to have their derivatives business governed by French law and their being comfortable using the French courts as a venue to resolve disputes, particularly where a significant monetary or reputational stake is involved. This prospect might not be initially appealing to institutions familiar with the English courts. However in the post-Brexit context, with English judgments expected to lose mutual automatic recognition within the EU under the Recast Brussels Regulation[8], the uncertainty as to the effect of English jurisdiction clauses in cross-border disputes[9] and the questions surrounding the accession by the UK (in its own right) to the Hague Convention[10] or the Lugano Convention[11] (which would in any case not be as comprehensive as the current regime[12]), the French law ISDA may begin to look more attractive, especially now that France has undertaken a modernisation of its judicial system, creating specialised international chambers with procedural rules inspired by English law proceedings.

The French law ISDA grants jurisdiction to the Commercial Court of Paris and the Paris Court of Appeal (the ICCC and ICCA), which both feature chambers specially designed to handle complex international disputes

The ambition to attract institutions looking to relocate from the UK to Paris and promote Paris as a destination of choice for international dispute resolution made the modernisation of the French judicial system a prerequisite. This modernisation was also particularly necessary to encourage the launch of the French law ISDA and its adoption by market participants.

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[8] Mutual recognition of judgments is set out in the Brussels I Regulation Recast dated 12 December 2012 (the "**Recast Brussels Regulation**") and provides that a judgment obtained in an EU member state is automatically recognised in every EU member state and can be directly enforceable by any EU enforcement authority. At the end of the transition period, and unless a deal is reached on that point, an English court decision would no longer benefit from the automatic and immediate recognition of judgments and simplified enforcement in the EU under the Recast Brussels Regulation.

[9] There is the potential for an increase in the risk of parallel 'torpedo style' proceedings. Under the Recast Brussels Regulation, a court seised pursuant to an exclusive jurisdiction clause - even if not the court first seised - determines its own jurisdiction while all other proceedings are stayed. The position would be different under the Lugano Convention where the court first seised is to take such initial step while all other proceedings are stayed, including those of any court seised pursuant to an exclusive jurisdiction clause.

[10] There is currently uncertainty as to the application of the 2005 Hague Convention on Choice of Court Agreements (the "**Hague Convention**") to exclusive jurisdiction clauses in favour of the UK courts in agreements entered into before the UK accedes to the Hague Convention in its own right. The UK deposited its instrument of accession to the Hague Convention on 28 September 2020 (following the earlier withdrawal of the UK's previous accession notice in 2019 pursuant to then moving timelines of the Brexit effective date at the time). According to the official press release, the Hague Convention will enter into force for the UK on 1 January 2021 (as for now it continues to apply to the UK as part of the transitional arrangements).

[11] On 8 April 2020, the UK deposited an application to accede to the 2007 Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters (the "**Lugano Convention**"). However, for the UK to accede to the Lugano Convention, all the contracting parties (EU, Denmark as an independent state, Iceland, Norway and Switzerland) need unanimously to approve the UK's application. The position of the European Commission is reported to be unwelcoming so far.

[12] For instance, the Hague Convention does not provide for automatic recognition of EU judgments and simplified enforcement, in the same way as the Recast Brussels Regulation. Moreover, the scope of the Hague Convention is limited: it only applies to UK judgments rendered on the basis of an exclusive jurisdiction clause. As for the Lugano Convention, although it provides for automatic recognition of all judgments issued by the courts of parties to the convention, obtaining *exequatur* is still necessary prior to enforcement.

The Protocols which created the ICCA, a new international chamber within the Paris Court of Appeal, and modernised the rules applicable to the ICCC (created over 25 years ago) have this objective.

The Protocols aim to promote a more flexible conduct of commercial litigation with procedural rules inspired by the rules governing English law proceedings (notably the examination of experts and witnesses and a form of 'specific' disclosure) and to facilitate the use of foreign languages, in particular English. At the same time important characteristics of the French commercial judicial system, such as the reduced cost of proceedings and the absence of 'systematic' disclosure, are preserved. The aim is to present the ICCC and the ICCA as a real alternative to the English courts to which participants in the financial markets are accustomed, especially the prestigious London Commercial Court, which is the leading forum for commercial litigation in the world.

Broadly speaking the ICCC and the ICCA have jurisdiction over economic and commercial cases with an international element, notably where foreign or EU law may apply. The ICCA is the appropriate forum to hear appeals against judgments rendered by the ICCC. The Protocols provide a non-exhaustive list of disputes over which the ICCC and ICCA have jurisdiction, and expressly include disputes relating to transactions on financial instruments, market standard master agreement, as well as financial contracts, instruments and products. Jurisdiction may also be based on a contractual stipulation granting jurisdiction to the courts within the district of the Paris Court of Appeal[13].

The ICCC Protocol and the ICCA Protocol are drafted in very similar terms. The main characteristics of the procedural rules in the ICCC and the ICCA as set out in the Protocols are:[14][15]

- **Use of foreign languages.** The Protocols facilitate the use of foreign languages, in particular English: documentary evidence can be submitted in English without translation[16], parties, experts, witnesses and counsels, when they are non-native French speakers, are authorised to express themselves in English (however simultaneous translation in French must be organised with the cost borne by the requesting party [17]) and arguments conducted in French can be subject to simultaneous translation[18] (at the expense of the requesting party). The Protocols

[13] This contractual possibility raised several questions as to how parties could effectively designate the international chambers as the appropriate forum in specific cases. Indeed, the international chambers are not jurisdictions but divisions of the Commercial Court of Paris and the Paris Court of Appeal and could therefore not be elected per se by the parties (the allocation to such chambers is subject to an administrative decision by the judge). As a compromise, Chantal Arens, the First President of the Paris Court of Appeal between 2014 and 2019, suggested that parties should incorporate traditional jurisdiction clauses, but with reference in brackets to the international chambers. The French law ISDA however follows a conservative approach and refers only to the jurisdiction of the Commercial Court of Paris and the Paris Court of Appeal (without any reference to the international chambers).

[14] For a further detailed presentation of the Protocols, please refer to the article *"A critical view of the Protocols relating to proceedings before the international chambers of the Commercial Court of Paris and the Paris Court of Appeal"* by Rupert Reece and Gabriel Hannotin.

[15] The ICCC and the ICCA are currently developing a practical bilingual (French-English) procedural guide intended to present in detail the course of proceedings in the international chambers in Paris.

[16] Article 2.3 of the ICCC Protocol and Article 2.2 of the ICCA Protocol. This is an important point as this will prevent judges from rejecting evidence that is exhibited in English, which is currently permitted on the basis of case law of the French Supreme Court (*Cour de Cassation*).

[17] Article 6.3 of the ICCC Protocol provides that simultaneous translation is at the cost of the party requesting to speak in a language other than French. This wording is unclear as to the allocation of costs when a party expresses itself in French, but its counsel, expert or witness expresses itself in another language, or where a party, expert or witness who expresses itself in another language is called to give evidence by the opposing side. Article 3.3 of the ICCA Protocol puts the burden of these costs on the applicant requesting the hearing, which seems an appropriate solution.

[18] Simultaneous translation is a right in the ICCC (Article 6.2 of the ICCC Protocol); however the consent of the judge must be obtained in the ICCA (Article 3.2 of the ICCA Protocol).

however continue to require legal submissions to be drafted in the French language and the judgment of the Court to be delivered in French (but the judgment will be accompanied by a sworn English translation).

- **Procedural timetable.** The Protocols introduce the possibility for the judge to order a procedural timetable (*calendrier de procédure*)[19] specifying the keys dates of the procedure, such as the dates on which the parties have to appear before the Court or exchange their submissions, when the witnesses and the experts will be heard or when legal counsels must deliver their oral arguments or even the date on which the decision of the Court will be rendered[20]. A procedural timetable is mandatory in the ICCA[21].

- **Production of evidence and documents.** The Protocols allow a party to require that a document held by the opposing party or a third party is produced[22]. The Protocols go further than the French Civil Procedure Code by allowing requests for the production of 'specifically identified categories of documents' (while case law in France traditionally tends to confine these requests to documents specifically identified). This practice of document production is reminiscent of the English law practice of specific disclosure, even though it remains more limited and controlled by the judge.

- **Hearings and examinations.** The Protocols put considerable emphasis on oral evidence, with hearings of the parties, experts and witnesses. This a novelty in the French judicial system where hearing the parties, witnesses or experts is extremely rare outside criminal cases. The Protocols provide that the judge may invite a party to answer the questions asked by another party or invite witnesses to answer the questions asked by the parties. Witness examination will be conducted on the basis of the filed written statements, but the judge may then invite witnesses to answer the questions asked by the parties[23], which is again reminiscent of English law proceedings where testimonial evidence is provided in written form but is then tested through examination of the witness, allowing important issues to be clarified and the witness being asked to explain apparent contradictions of its statement. Hearing of technicians - and in particular experts[24] - will be subject to the same rules as for the hearing of witnesses.

The initial reaction of market participants to the ICCC and ICCA is encouraging but it remains to be seen how attractive they will be for the settlement of disputes relating to derivatives.

It will likely depend largely on the willingness of parties to agree to apply the Protocols. The Protocols do not apply automatically to proceedings in the ICCC and the ICCA[25] and should a party object to their application, the normal procedural rules of the French Civil Procedure

[19] Article 3 of the ICCC Protocol.
[20] Jean-Michel Hayat, the First President of the Paris Court of Appeal, declared at the hearing marking the beginning of the Court's judicial year on 13 January 2020, that the ICCA has the ability to decide on its jurisdiction within four months and to render a judgment on the merits within eleven months.
[21] Article 4.3 of the ICCA Protocol.
[22] Article 4.1 of the ICCC Protocol and Article 5.1 of the ICCA Protocol.
[23] This departs from the general position set out in Article 214 of the French Civil Procedure Code which currently prohibits a party from directly addressing a witness, and instead requires them to ask their questions through the judge, who can refuse to transmit them.
[24] Experts are judicially appointed upon the parties' request or at the judge's own initiative. When the experts are appointed by the parties, the judge assesses the relevance of such request and has the power—but is not obliged—to order their attendance. In such a case, the parties will also file the report of the expert's testimony.
[25] The ICCA Protocol expressly provides that its application must be agreed by the parties during the first pre-trial hearing (Article 4.1.1 of the ICCA Protocol). The ICCC Protocol is however silent on this point.

Code will apply[26]. In fact, the use of the Protocols has not been properly tested yet, as most of the cases allocated to these international chambers to date were there by reason of the existence of a genuinely international element in the dispute, rather than as a result of the parties' choice.

It will be interesting to see how the ICCC and the ICCA practice will develop further in the future when they start to handle cases involving parties who have specifically chosen to submit their dispute to the Protocols in order to take advantage of their provisions.

Although the uptake of the French law ISDA was initially rather slow, in recent months, more French market participants (in particular corporates) have been considering its adoption and requesting their banking counterparties to trade derivatives under the French law ISDA and implement the necessary arrangements to convert their stock of English law governed ISDA Master Agreements into French law. The ISDA Brexit Working Group published a form of amendment agreement aiming at facilitating such conversion to the French law ISDA. Will the French law ISDA finally appear as a real alternative to the English law ISDA and be embraced by the market in a post-Brexit world? Only time will tell.

[26] Provisions allowing parties contractually to agree the application of the Protocols in the ICCC and the ICCA are currently developed. However, their enforceability is questionable.

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