Connecter Protéger Coopérer Depuis 1893
Connecting Protecting Cooperating Since 1893
Conectando Protegiendo Cooperando Desde el 1893

Convention of 5 July 2006 on the Law Applicable to Certain Rights in Respect of Securities held with an Intermediary

The need for uniform conflict of laws rules that comport with the reality of how securities are held and transferred today is increasingly critical. Legal uncertainty as to the law governing the perfection, priority and other effects of transfers imposes significant friction costs on routine transactions and operates as an important constraint on desirable reductions in credit and liquidity exposures. Increased exposure to unsecured credit risk amplifies systemic risk and the potential proliferation of the number of bankruptcies.

The Securities Convention aims to bring legal certainty and predictability as to the law governing issues that are of practical importance for holding and transfer of securities held with an intermediary. Taking a pragmatic approach, the Securities Convention provides certainty as to the law applicable to clearance, settlement and secured credit transactions that cross national borders. The Convention improves transactional efficiencies in global securities markets, reduces systemic risk in cross-border transactions and intermediary holdings, and facilitates cross-border capital flows.

Principal features of the Convention

Applicable law

The Convention deals only with applicable law (Art. 4). It has no effect on the substantive law that will be applied once the conflict of laws determination has been made. Instead, the Convention sets forth the primary conflict of laws rule to determine the law applicable to all the issues falling within the scope of the Convention. This primary rule is based on the relationship between an account holder and its intermediary, and gives effect to the express agreement by the parties in their account agreement on the law governing all the issues falling within the scope of the Convention.

The parties may choose between two alternative agreements. The first envisages the parties expressly agreeing on a law governing their account agreement (also called the general governing law clause). In that case, that law also governs all the issues falling within the scope of the Convention. The second envisages the account holder and its relevant intermediary expressly agreeing that the law of a particular State will govern all the issues falling within the scope of the Convention. In this latter case, that law governs all these issues, regardless of whether there is a separate choice of law to govern the account agreement generally. The law chosen by the parties to the account agreement applies only if, at the time of the agreement on governing law, the relevant intermediary has a Qualifying Office in the State whose law is selected which,

- alone or with another office or third party, serves certain functions relating to the maintenance of securities accounts, or
- is identified, by any specific means, as maintaining securities accounts in that State.

The securities accounts being maintained need not be the specific account in question.

If the applicable law is not determined under Article 4, there are certain fall-back provisions (Art. 5) in the Convention that would result, ultimately, in application of the law of the jurisdiction in which the intermediary is incorporated or otherwise organised.

Scope

The Convention applies to all the issues enumerated in the broad but exhaustive list in Article 2(1). Most significant among the issues listed in Article 2(1) are: the legal nature and effects against the intermediary and third parties of rights resulting from a credit of securities to a securities account (Art. 2(1)(a)); the legal nature and effects against the intermediary and third parties of a disposition of securities held with an intermediary (Art. 2(1)(b)); the perfection requirements of a disposition (Art. 2(1)(c)); and whether an interest extinguishes or has priority over another person's interest (Art. 2(1)(d)).

The Convention also includes in its scope the protection of rights upon a change of the applicable law (Art. 7), insolvency proceedings (Art. 8), the determination of applicable law for Multi-unit States (Art. 12), and certain transitional provisions for determining priorities between pre-Convention and post-Convention interests, and for dealing with pre-Convention account agreements and securities accounts (Arts 15 and 16).

The Convention has no impact on regulatory schemes relating to the issue or trading of securities, regulatory requirements placed on intermediaries, or enforcement actions taken by regulators. Therefore, supervisory authorities are, in the exercise of their authority, free to prohibit intermediaries from choosing any governing law, choosing a particular governing law, or choosing a governing law other than the law specified by the authority.

Harmonisation

In its 2003 Global Clearing and Settlement Plan of Action, the Group of Thirty (G30) recommended that "the Hague Convention be ratified as quickly as possible by as many nations as possible". The *ex-ante* legal certainty that the Convention is designed to achieve is also important under the revised capital adequacy framework commonly known as Basel II.

The Committee on Payment and Settlement Systems and the Technical Committee of the International Organization of Securities Commissions have also noted that the Securities Convention is significant in order to harmonise the laws governing securities settlement systems (SSSs), the contracts between SSSs and direct system participants, and the contracts between direct system participants, other intervening intermediaries and their respective customers.

Additional resources

The Securities Section of the HCCH website contains the latest information about the Securities Convention. This includes:

- Text of the Convention
- Status table of Contracting Parties
- Explanatory Report on the Securities Convention