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INDIRECTLY HELD SECURITIES

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# TABLEAU RÉSUMANT LES COMMENTAIRES REÇUS SUR LE « PROJET ANNOTÉ DE JUILLET 2001 »

***Préparé par le Bureau Permanent***

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# CHART SUMMARISING COMMENTS RECEIVED ON THE "ANNOTATED JULY 2001 DRAFT"

***Prepared by the Permanent Bureau***

*Document préliminaire No 5 de novembre 2001*
*à l'intention de la Commission spéciale de janvier 2002*

*Preliminary Document No 5 of November 2001*
*for the attention of the Special Commission of January 2002*

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# COMMENTS RECEIVED ON THE "ANNOTATED JULY 2001 DRAFT"

*In order to avoid any misrepresentation of the comments submitted, the Permanent Bureau has reproduced (as far as possible) these comments in their original form.*

| ARTICLE: | COMMENT: | AUTHOR: |
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| **In general** | The EC has passed the *Insolvency Regulation*, the *Settlement Finality Directive* and the directives on *reorganization* and *winding up* of credit institutions and insurance undertakings. Further, the *Collateral Directive* is likely to be passed this year or next year. Some of the rules in this EC legislation may conflict - or at least potentially be interpreted differently - than the rules in the Hague Convention. Perhaps, it is about time to discuss how this problem should be overcome. | Ulrik Rammeskow Bang-Pedersen / Denmark (p.4) Spain (p.6) |
| | The Swiss consultation proceedings have shown unflagging support for the proposed Convention as a means to achieve consistency and predictability in an area of law that is currently plagued by considerable uncertainty. We also continue to stress the importance of keeping this project on the fast track so that we can benefit as soon as possible from the clarification that it is likely to bring about. Following are some of the suggestions that we consider particularly important from a Swiss perspective. | Switzerland (p.1) |
| | We fully support the Hague Conference on Private International Law's proposal to draw up a PIL convention on proprietary rights in indirectly held securities. The present situation, which focuses on where the securities are physically situated, often makes it very difficult to ascertain with certainty the law governing the disposition of a particular security. This applies especially to the issue of using securities held abroad as collateral. An international convention could make it easier to determine the law governing the disposition of securities located abroad and thus also increase the acceptance of such securities as collateral.<br>In the revised draft of July 2001, several points are formulated more clearly than in the previous version. | The Association of German Banks (*Bundesverband deutscher Banken,* p.1) |
| | The current draft of the Convention and the commentary leave a number of issues to be considered further. Where it has not expressly commented on a point, ISDA also reserves its position for further study, consultation and discussion among its members. | ISDA (p.6) |

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| **Title of the Convention (E+F)** | The terms securities held with an intermediary and indirectly held securities are used interchangeably throughout the text. The Canadian delegation prefers securities held with an intermediary.<br>Nous remarquons que les termes titres détenus auprès d'un intermédiaire et titres intermédiés sont utilisés de façon interchangeable dans le texte. Nous préférons l'utilisation de «titres détenus auprès d'un intermédiaire » . | Canada (p.2) |
| | We support the new short wording of the title. Additionally, we support the way that both the title and Art. 1 make clear that the Convention deals only with proprietary aspects of dealings in securities held with an intermediary. However, as we have stressed before in our March 2001 comments, we **prefer using the same terms throughout the text**.<br>We **prefer the wording "indirectly used securities" (used in the title) to be used also in Art.** 1, para. 1.<br>We prefer the wording **"aspects"** (used in Art. 1, para. 2) to wording "rights" (used in the title and Art. 1, para. 1).<br>The suggested new Art. 2, para. 4 makes it clear that the Convention is not intended to cover direct holding patterns used, e.g. in Finland. We have urged that it should be made clear also in the title and Art. 1 that the Convention really deals **only with indirect holding systems**. So, we prefer the wording presented by the Working Group in March 2001 for Art. 1: "…**securities held indirectly through a securities account."** | Finland (p.1) |
| | In the title, the expression "indirectly held securities" is used, whilst in Art. 1 (1) and in the definitions of Art. 2, the expression used is "securities held with an intermediary". **Would it not be better to use the latter ("securities held with an intermediary") also in the title of the Convention?** | Spain (p.1) |
| | Il est proposé de modifier le titre de la Convention comme suit: "Convention sur la loi applicable aux droits réels portant sur des **titres détenus auprès d'un intermédiaire**".<br>D'une part le terme de "titres intermédiés" n'est ni un terme juridique consacré ni un terme utilisé dans la pratique. D'autre part le terme n'est plus repris dans la Convention qui dans les définitions parle de "titres détenus auprès d'un intermédiaire". | Luxembourg (p.1) |

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| | The title of the draft convention refers to "indirectly held securities". Article 1, paragraph 1 of the January draft referred to "securities held indirectly through a securities account". A restrictive interpretation might take this to mean that the future convention is to cover only securities held in collective custody. We suggest, however, that for the sake of completeness and in order to avoid unnecessary distinctions, securities held in **individual safe custody (jacket custody) should also be covered.** See also Art. 1(1) - "securities held with an intermediary" – German comments | The Association of German Banks (p.2) |
| **1(1):**<br><br>**"proprietary rights" – terminology** | Proprietary rights, proprietary aspects and proprietary effect seem to be used interchangeably throughout the text. There is a need for consistent terminology throughout the text.<br><br>Les termes droit réel, aspects de droit réel, et effets réels sont utilisés de façon interchangeable d'un bout à l'autre du texte. Il serait important d'utiliser la même expression pour éviter de semer la confusion.<br><br>The Canadian delegation suggests using the term property rights throughout the text.<br><br>La délégation canadienne suggère d'utiliser le terme droit de propriété (property rights) dans le texte. | Canada (p.1) |
| | We strongly support the limitation of the proposed Convention to the property aspects of indirectly held securities. However, the term "proprietary rights" in Article 1 has caused some confusion, particularly because the French term "droits réels" is relatively clear. One may question whether **"property rights"** might not be a more adequate term here. | Switzerland (p.1) |
| | The current draft uses different versions of this phrase in different places:<br><br>"proprietary rights": Art 1(1), 6(1)<br><br>"proprietary aspects": Art 1(2)<br><br>"proprietary effects": Art 2 (definition thereof), Art 4(b)<br><br>We suggest that the Convention consistently use a single simple phrase: **"property rights."**<br><br>We note that concerns have been raised about clarifying the point that the Convention applies to pledge or other dealings in securities held with an intermediary whether that package is a property right or contractual right. We think that concern can best be addressed by adding language covering the point to the definition of "securities held with an intermediary." See below | USA (p.1) |

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| | We suggest a slight change to clarify the function of the Convention. We also remain of the view that a cross-reference to the operative article is important in the introductory scope clause, as follows:<br><br>Art. 1(1): "This Convention determines ~~the~~ which State's law governs ~~governing~~ property rights in respect of securities held with an intermediary, as specified in Article 4. | USA (p.1) |
| **1(1):**<br><br>**"proprietary rights" – definition** | According to the comments on the draft Convention, proprietary rights arising from the transfer of purely contractual rights are covered by the Convention, if an interest in the securities is provided as collateral or transferred to a purchaser. In this context it should be made clear that the term **"proprietary rights" also includes forms of holding that substitute the actual acquisition of ownership**.<br><br>The reason for clarifying the term "proprietary rights" is that securities located abroad are often held under a system whereby a German depository bank acquires the ownership of the securities or an equivalent legal position, which it holds for the customer in a fiduciary capacity (*Wertpapierrechnung*). In this case the customer acquires no right of property with respect to the securities, but he has an economic position comparable to that of beneficial owner by virtue of the fiduciary agreement. By the fact that the economic position of the customer is comparable to that position where the customer acquires the right of property with respect to the securities holding in the form of Wertpapierrechnung should also fall within the scope of the Convention. | Germany (p.2)<br>The Association of German Banks (p.2) |
| | The Convention covers "proprietary rights arising from the transfer of purely contractual rights" (explanatory comment to Art. 1 (1)). We consider that it is worth discussing the **possible overlap with the Rome Convention**.<br><br>If according to the law of the relevant intermediary, the account holder does not have a right *in rem*, but only a contractual claim against his intermediary, the pledge of this claim (including money as proceeds of a securities account) is covered by the Convention. This means that the pledge is governed by the law of the State of the relevant intermediary. The problem that we find in this solution is that according to a principle of private international law –established in many European countries, and probably in the Rome Convention- the constitution of proprietary rights over contractual rights are subject to the law applicable to that contractual right (which may or may not be the place where the relevant intermediary is located). We consider that this point should be discussed. | Spain (p.1) |

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| **1(1):**<br><br>**"securities held with an intermediary"** | We agree with the proposed omission of the reference to "account rights" and the use of the phrase "securities held with an intermediary" throughout the whole text instead. The harmonisation of the text will contribute to the better understanding of the proposed provisions and leave no room for false interpretation or misunderstandings. | Greece (p.1) |
| | In the interest of legal certainty and for the sake of completeness the draft Convention should also cover securities held in individual safe custody **(jacket custody**). | Germany (p.2) |
| **1(2):**<br><br>**exclusions from the substantive scope of the Convention** | We think it is **advisable to keep** this paragraph, which explicitly sets out the cases where the Convention does not apply, in order to avoid misunderstandings at this stage. Maybe we should delete it at a later stage in the drafting of the text. | Greece (p.1) |
| | We **support** the new Art. 1, para. 2 that makes clear that the Convention does not determine the contractual and other non-proprietary aspects in respect of indirectly held securities. Especially important is, that the Convention does not apply to the law concerning the creation, ownership or transfer of securities. This rule has been expressed, e.g. in the EU Settlement Finality Directive.<br>We prefer the wording "**aspects**" (used in Art. 1, para. 2) to the wording "rights" used in the title and Art. 1, para. 1. | Finland (p.1) |
| | For **consistency** in usage of **"proprietary …"** and in use of "law governing/law applicable," change as follows:<br>"This Convention does not determine ~~the~~ <u>which</u> law <u>governs</u> ~~applicable to~~ the contractual or other <u>non-property</u> ~~non-proprietary aspects of~~ rights or duties in respect of securities held with an intermediary, and in particular […] | USA (p.1) |
| | This paragraph should be **deleted**, as it might create more problems than it actually resolves. | Luxembourg (p.1) |
| **1(2)(d)**<br><br>**"transfer agents"** | We consider also that the exclusion set forth in Art. 1(2)(d) **needs an explanation**: Who are those "transfer agents" the Convention refers to? Would it not be helpful to include a cross-reference to Art. 2(4)? In relation to Art. 1 (2): Among the exclusion, should be added: - "the regulation of the issuance or trading, clearing or settlement of securities": -"the regulation of a securities intermediary" (already proposed by the USA delegation, March 2001). This will help to understand the scope of the convention, and it will facilitate its use by practitioners. | Spain (p.1) |

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| **2(1):**<br><br>**"titres" / "securities"** | The Canadian delegation is of the view that the definition of securities should be broadened and expressly include additional elements, in a manner similar to the definition of financial asset in Revised Article 8 of the U.S. Uniform Commercial Code. The definition should be broad enough to accommodate future developments in the securities markets.<br>La délégation canadienne est d'avis que la définition des titres devrait être plus générale et devrait inclure des éléments supplémentaires comme le fait l'article 8 du Code commercial uniforme des États-Unis en définissant l'actif financier. La définition devrait être assez générale pour inclure des développements futurs dans les marchés de valeurs mobilières. | Canada (p.1) |
| | We **support strongly** the proposed wording of the definition of securities, which adopts the descriptive approach rather than the fully fledged one. It is true that the definition is explicit enough to cover the typical securities, such as stocks, shares, bonds and options (which also fall within the definition of securities of the Greek L. 2396/1996), and flexible enough to leave room for the regulation of new securities. In this way, the main points that this Convention wants to establish and make clear, namely certainty and flexibility during transactions, are dealt with.<br>The fact that the proposed definition encompasses dematerialised securities is also very encouraging, since all shares listed on the Athens Stock Exchange are already dematerialised or turned into dematerialised ones. | Greece (p.2) |
| | We are in favour of a broad and flexible definition of securities. However, is the present wording **too broad**. The idea of the annotation (i.e. to make a difference between derivatives that are "securities" and derivatives that are not) should somehow be expressed in the definition itself. | Finland (p.2) |
| | Il est proposé de faire référence uniquement aux « titres de capital » sans faire référence aux « actions » qui devraient être couvertes par le terme de « titres de capital ». Dans un souci de cohérence plutôt que de se référer aux « obligations » il est proposé de faire référence plus généralement à des « titres de créances négociables ».<br>Les autorités luxembourgeoises s'interrogent sur la signification des termes "autres actifs" qui sont très vastes et vont bien au-delà des valeurs mobilières et instruments financiers qui sont essentiellement visées par la Convention. Il est donc proposé de supprimer ces termes.<br>Dans les commentaires faits sous la définition, il est indiqué que les instruments sur matières premières ne devraient pas être couverts par la définition du terme "titres". Il faut se demander si cette exclusion générale est opportune. Ainsi les warrants standardisés sur ces produits traités en bourse pourraient utilement être couverts par la Convention. | Luxembourg (p.1) |
| **2(1):** | The current comment on the definition of "securities" is **problematic**, in that it mentions the | USA (p.1/2) |

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| **"titres" / "securities"** | classification of a few forms of instruments, saying some are included and some not, without giving a good explanation of the basis of inclusion or exclusion. We think it would be useful for the comment to say something on the general issue, perhaps with an example that is clearly just an illustration. At present, there is a risk that interpretation would place undue emphasis on analogies to the specific items that happen to be mentioned. We **suggest that the comment be replaced** with something like the following:<br><br>"The definition of securities is deliberately left broad to accommodate future developments in the securities markets. The common forms of traditional securities--stocks, shares, and bonds--are, of course, included because the indirect holding system has developed principally to accommodate the need for rapid, safe, and efficient processing of transactions in these assets. Once developed, however, the institutions of the indirect holding system have proven to be useful for other forms of financial assets and instruments, and this development can be expected to continue. Because the Convention covers only conflict of laws issues for the indirect holding system, it necessarily applies only to financial assets or instruments that can be held through accounts with intermediaries in the fashion that has developed for traditional securities. For example, some forms of financial instruments, such as swaps individually negotiated between particular counterparties, would not be covered by the Convention because they are not obligations or interests issued by an issuer and credited to an account maintained by another financial institution; rather they are merely contracts for exchange of products or cash flows between the parties." | |
| **2(1):**<br><br>**"intermediary" – "to which securities may be credited"** | The definition of "intermediary" should be **modified to remove the words "to which securities may be credited" as this is already covered in the defined term of securities accounts.** Therefore the word "accounts" in the definition needs to be replace with "securities accounts". | Australia (p.1) |
| | The phrase **"to which securities may be credited" should be deleted** by using the defined term "securities account" as follows:<br>"intermediary" means a person that in the course of business maintains <u>securities</u> accounts ~~to which securities may be credited~~ and is acting in that capacity either for others or for its own account.<br>In the comment concerning "person," change as follows: " 'person' should be given its <u>broadest</u> ~~ordinary~~ meaning. <u>There is no intention to exclude any form of entity that acts as an intermediary. …"</u> | USA (p.2) |

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| | The Canadian delegation agrees with the US proposal to replace "derived" by "that result". Further, we suggest adding the following to the definition:<br>"securities held with an intermediary" means the rights of an account holder ~~derived~~ that result from a credit of securities to a securities account, whether such rights are property, contract or other rights.<br>La délégation appuie la proposition américaine de remplacer « découlant (derive) » par « qui résulte (that result) ». De plus nous suggérons d'ajouter les soulignés à la définition :<br>« titres détenus auprès d'un intermédiaire » détermine les droits du titulaire du compte ~~découlant~~ qui résultent de l'inscription de titres en compte qu'il s'agisse des droits de propriété, de contrat ou autres ; » | Canada (p. |
| **(1):**<br>**"intermediary" – "in the course of business"** | We **welcome the expression "in the course of business"** that requires from the intermediary some kind of **professionalism** (see our March 2001 comments on "securities intermediary" on p.2). | Finland (p.2) |
| **2(1):**<br>**"intermediary" – "control" or "supervision**". | Some authorities have expressed their concern about the concept of "intermediary" and the fact that the definition does not require any kind of **"control" or "supervision**". Can anybody have the status of intermediary only because "in the course of business [it] maintains accounts"? If latter Art. 5 requires implicitly a kind of supervision either over the intermediary or over the account, would it not be better to this in the definition? | Spain (p.1 |
| | We suggest considering whether the definition of "intermediary" should include the limitation of an **"intermediary subject to regulatory supervision of at least one jurisdiction".** This limitation is already implied by Article 5, and including it in the definition of Article 2 would exclude the consideration of intermediaries that do not operate on a commercial basis.<br>Moreover, we assume that the proposed Convention's reference to the law of the place of the relevant intermediary extends to the law applicable to the payment in so-called "delivery-versus-payment" arrangements. | Switzerland (p.2) |
| **2(1):**<br>**"intermediary" – definition** | We suggest that this definition should refer to securities account instead of "accounts to which securities may be credited".<br>Les termes « comptes de titres au crédit desquels sont inscrits des titres » devraient être remplacés simplement par «comptes de titres».<br>The Special Commission should consider whether the commentary should say that the | Canada (p.1) |

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| | definition may include national central securities depositories (CSDs) and international central securities depositories (ICSDs), since it is our understanding that such entities may not fall under the definition in certain circumstances. Finally, it should be made clear that the term "person" should be given the broadest meaning.<br><br>La Commission spéciale devrait peut-être considérer s'il est important de clarifier dans le rapport que la définition peut inclure des dépositaires centraux de titres nationaux (DCTN) et internationaux (DCTI), car nous comprenons que certains d'entre eux ne seraient pas inclus dans cette définition dans certaines circonstances. Il faudrait clarifier que le terme « personne » est utilisé de façon très large. | |
| | Does this definition include:<br><br>a) a person that maintains an account merely for **one person (customer)**?<br><br>b) a person, X, that maintains accounts for several customers, *i.e.* Y and Z, if at the upper-tier intermediary (the intermediary that maintains the account for X) the account is labelled as "X omnibus account on behalf of Y and Z"? In other words, **is X considered to be an intermediary even if the names of the X-customers are registered directly at the upper-tier intermediary?**<br><br>c) a **trustee**? That is, is a trustee considered to be an intermediary that maintains an account on behalf of the beneficiaries of the trust? Or should securities held by a trustee rather be considered held directly by the trust (leaving i.e. conflict between the beneficiaries and the creditors of the trustee to the law applicable to the trust)?. | Ulrik Rammeskow Bang-Pedersen / Denmark (p.1) |
| | Often the discussion is focused on pledges and title transfers made by a customer, who does not himself act as an intermediary at all. As stated in the July-draft, p. 5, the relevant intermediary in these cases is the customers own intermediary. However**, the determination of which intermediary is the relevant in conflicts arising due to a pledge made by (or insolvency of) a person, who acts as an intermediary may not be obvious.** Is it the intermediary in question that is the relevant or rather the intermediaries´ (upper-tier) own intermediary? For example, image that several customers, C, holds securities through a broker, B, who in turn holds the securities through a bank, D. If insolvency proceedings are initiated against B, is it then B or D that is the relevant intermediary when it has to be decided whether C or the general creditors of B is entitled to the securities? Personally, I would think D was to the relevant intermediary (but please note this is not meant as an official Danish position). Consequently, the customers should prevail if that is justified by the law of D. Of course, regardless of whether the customers prevail under the law of D, the customers should always be entitled to the protection afforded by the | Ulrik Rammeskow Bang-Pedersen / Denmark (p.1/2) |

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| | *lex concursus* (typically the law of B). Perhaps the latter principle should be stated explicitly in **Art 6**. Consequently, in case of insolvency of an intermediary, the customers of the intermediary should generally prevail, if that is justified by the law of the intermediary (*lex concursus*) or the law of the intermediaries´ intermediary (the law of the relevant intermediary). Regardless of which intermediary is to be considered the relevant one, it seems that it would be useful if further elaboration was made on this point, i.e. by examples in the explanatory comments to next draft. | |
| | Only the first paragraph of the **commentary** to the definition of "relevant intermediary" is pertinent to this definition. The rest is a discussion of the so-called **"page 37 issue**." We doubt that this issue warrants extended discussion in whatever form of commentary accompanies the final text. In any event, if the point is to be discussed, the appropriate place is in connection with the substantive rule in Article 4 rather than the definitions. | USA (p.2) |
| | The acquisition of securities is recorded on the purchaser's account. According to the definition of "relevant intermediary" and "securities account" in Article 2, paragraph 1, the relevant custodian is that of the **purchaser**. If a collateral arrangement is entered into, various courses of action are conceivable. If a lien is created, it is possible that there will simply be an entry on the collateral provider's account to the effect that the securities in question are serving as collateral in favour of a certain collateral taker. Ownership and possession of the securities therefore remain with the collateral provider. The relevant intermediary would then be that of the **collateral provider**. If, on the other hand, collateral is provided in the form of an outright transfer of title or similar collateral instrument, the collateral will be transferred to a collateral account of the collateral taker. The **collateral taker's custodian** would then be the relevant intermediary. The convention should take account of both alternatives. | The Association of German Banks (p.2/3) |
| **2(1):**<br><br>**"relevant intermediary" – "Super-PRIMA"** | We appreciate the paragraph on Super-PRIMA as an explanation of what has occurred but do not think it should be included in the commentary.<br><br>Nous reconnaissons que le rapport a comme but de donner un compte rendu des discussions à date concernant le Super-PRIMA. Cependant, nous sommes d'avis que ce paragraphe devrait être exclu du Rapport explicatif. | Canada (p.2) |
| | **No merit** in Super-PRIMA: not well adapted to complexity of modern indirect holding systems | Australia (p.1)<br>Czech Republic (p.1)<br>ISDA (p. 2) |

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| | We **share the concerns** against "Super-PRIMA" expressed in the annotation to "relevant intermediary" (see also our comment above at Art. 2, para. 2). At this stage, we support the present wording. As said, further discussions are necessary. | Finland (p.2) |
| | We note our **strong disagreement** with the notion that the Convention should establish that "a single law [would] govern proprietary aspects of all stages of a transfer between two parties who use different intermediaries." That suggestion is completely inconsistent with PRIMA, the realities of the modern securities holding system, and the elimination of the "look-through" approach. It is not "Super-PRIMA," but "Anti-PRIMA." | USA (p.2) |
| | La Convention devrait régler le problème du choix de l'intermédiaire pertinent à considérer pour déterminer à quel moment un transfert a été effectué. **Le fait qu'un transfert puisse impliquer l'intervention d'une série d'intermédiaires devrait dans les relations entre la partie qui transfère et la partie qui reçoit un titre être sans pertinence.** Il s'agit de déterminer entre ces parties **à quel moment** le transfert devient effectif. L'article 5 pourrait utilement couvrir ce point. | Luxembourg (p.1 and 2) |
| | We continue to believe that the precise definition of PRIMA requires further consideration. **Neither the splitting up of the law applicable to a particular transaction resulting from the current PRIMA approach nor the retrospective fixing of the applicable law under "Super PRIMA" is fully satisfactory in situations involving different intermediaries.** Again, we suggest that the possibility of exclusively applying the law of **either the transferor's or the transferee's intermediary** to the entire transaction could be discussed as possible alternatives to the current proposal. | Switzerland (p.2) |
| | Article 2, paragraph 1 defines the "relevant intermediary" as "the intermediary with whom the account holder maintains the securities account". If several intermediaries are involved, the question arises as to which of these custodians, each maintaining an account for one of the other parties involved (including other intermediaries), is the relevant intermediary when it comes to determining the applicable law. In Germany, this is clarified by section 17a of the German Safe Custody Act (Depotgesetz – DepotG), which states that this depends on the office maintaining the account of the recipient of the disposition of the proprietary rights. The **revised draft** outlines the debate on the application of PRIMA (place of the relevant intermediary approach). This approach **provides that the applicable law on each level of a multi-tiered holding system is determined by the intermediary who maintains the account. Under an alternative approach, the law is that of the last recipient of the proprietary rights, so that the proprietary rights are governed by only one legal system.** | The Association of German Banks (p.3) |

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| | The question is whether PRIMA is, in fact, at odds with the approach adopted by section 17a of the German Safe Custody Act. **Under section 17a DepotG too, a title transfer or provision of collateral which actually consists of several real dispositions of proprietary rights in the multi-tiered holding system (e.g. a series of assignments) would probably result in each disposition and the law applicable to it having to be considered individually.** It should be made clear that when – as in Germany – there is legally speaking a single disposition, this must be governed by a single set of laws. Such an application of a uniform regime is to be welcomed from the point of view of legal certainty. However, jurisdictions which work on the premise that there are several dispositions in a multi-tiered holding system may arrive at a different conclusion if the applicable law is determined on the basis of the intermediary of the recipient of the disposition. Against this background, the text of the convention is generally acceptable on this point, in our view. It should be stressed that irrespective of how the term "disposition" is understood in individual jurisdictions, implementing the PRIMA would make life considerably easier in practice. Adoption of the convention is therefore to be warmly welcomed and should not be called into question at this point. | |
| **2(1)**<br><br>**"securities account"** | Need to use a consistent term throughout the Convention.<br><br>Il est suggéré d'utiliser le même terme partout dans le texte de la Convention. | Canada (p.2) |
| | The definition of "intermediary" is crucial here. We must make it clear all the time that the Convention deals with indirectly held securities. So, the new Art. 2, para. 4 has great importance in sharpening the definition of "securities account". | Finland (p.2) |
| **2(1) F**<br><br>**" compte de titres"** | Dans la définition les termes **"*teneur de compte*" devraient être supprimés**, la notion de teneur de compte étant trop intimement liée aux seuls titres dématérialisés et ne figurant d'ailleurs pas dans le texte anglais du projet de Convention. | Luxembourg (p.2) |
| **2(1)**<br><br>**"securities account" / "cash"** | We understand the idea of drawing a line between cash in a "securities" account and cash in a "deposit account". However, there will be **great problems to actually *make* the difference**. At this stage, we prefer excluding cash from the scope of the Convention. However, we are open to new suggestions to define cash in a securities account. | Finland (p.2) |
| | Cash accounts and proceeds from securities accounts should **not be included** in the definition of "securities account" given the fact that in most legal systems, cash credited as proceeds to an account does not give rise to proprietary rights. | Germany (p.2)<br>(Greecep.2)<br>The Association of German Banks (p.2)<br>Czech Republic (p.1) |

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| | It may be appropriate **to discuss whether the Convention should apply if PRIMA leads to the application of a law of a State under which it is possible to have a proprietary claim to a cash account.** For example, if the intermediary sells the securities that he holds for its customers and the proceeds of the sale is credited to a specific bank account (held by the intermediary for its customers), it may be appropriate to apply the law of the location of the bank to the question of whether the customers are entitled to the bank account in case of insolvency of the intermediary. | Ulrik Rammeskow Bang-Pedersen / Denmark (p.2) |
| | The second paragraph of the **comment** concerning "cash" is confusing and should be deleted. As written, it blends two different issues: (1) the legal nature of a deposit account or claim against an intermediary with respect to "cash" or free credit balances; and (2) the question whether, or under what circumstances, such rights—however they may be described in a particular legal system—are treated when they are proceeds of a security interest in other property. Similarly, the words "as proceeds" should be deleted from the last sentence of the preceding paragraph. | USA (p.3) |
| **2(1)**<br><br>**"titres détenus auprès d'un intermédiaire"** | Le terme "détermine" devrait être remplacé par le terme "**désigne**" par souci de cohérence avec les autres définitions. | Luxembourg (p.2) |
| **2(1):**<br><br>**"securities held with an intermediary"** | Securities held with an intermediary should be clearly included in the definition to ensure that the Convention applies to situations involving multiple tiers of intermediaries.<br><br>Les titres détenus auprès d'un intermédiaire devraient être clairement inclus dans cette définition pour assurer que la Convention s'applique à des situations qui comprennent plusieurs paliers d'intermédiaires.<br><br>It would be very useful if the commentary expanded on what is included and what is excluded from this definition.<br><br>Il serait fort utile que le rapport contienne une explication plus élaborée sur ce qui est inclus et ce qui est exclus de cette définition. | Canada (p.1) |
| | As explained in the annotation, the nature of the interest ("right") of the account holder to the securities varies from one legal system to another. The actual rules are selected by using the choice of law rules of the Convention that should be "clean" from any kind of "material" rules. That is why any kind of definitions relating to the "right" itself should be omitted from the Convention | Finland (p.2) |

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| | To **clarify the point that the Convention applies to pledge or other dealings in securities held with an intermediary whether that package is a property right or contractual right**, we suggest the addition of language to the definition of "securities held with an intermediary," as follows:<br><br>"securities held with an intermediary" means the rights of an account holder that result ~~derived~~ from a credit of securities to a securities account, whether such rights are described as property, contractual, or other rights ;<br><br>The change from "derived" to "result" is a conforming change to a suggestion we make concerning Art 4(2), below. | USA (p.3) |
| **2(1):**<br><br>**"account holder"** | The phrase **"securities are credited" can be deleted** by using the defined term "securities account" as follows:<br><br>"account holder" means a person for whom an intermediary maintains a ~~to whose~~ securities account ~~securities are credited~~; | USA (p.3)<br>Canada (p.2) |
| **2(1):**<br><br>**"disposition" and "pledge"** | The Canadian delegation would prefer a definition of "disposition" that used stronger and clearer verbs to describe its principal intended meaning, and more general terms to catch other, less important, methods. For example, "disposition" includes any sale, pledge or other transfer by consent of the parties, or by operation of law.<br><br>La délégation canadienne est d'avis qu'il faut utiliser des termes plus solides et plus clairs pour décrire le principal sens du terme. Il faudrait aussi utiliser des termes plus généraux pour englober d'autres méthodes moins importantes. Par exemple, « transfert » inclut toute vente, sûreté ou autre disposition par consentement des parties ou par effets de la loi. | Canada (p.2) |
| | The **definition of "disposition" should be broad** so we support the omission of words "…of title". However, **we prefer not to include title transfer collateral arrangements to the definition of "pledge".** One solution is to omit the definition of a "pledge" altogether and broaden the definition of a "disposition" to cover all kinds of security interests, either possessory or non-possessory, including non-possessory pledges, possessory collateral arrangements and "full transfers of ownership" (e.g. sales). Note that "pledge" (unlike "disposition") is used nowhere else in the draft Convention than in the definition itself, so it is unnecessary from that point of view, too. | Finland (p.2/3) |
| | If "pledge" is defined, a **definition of "outright transfer"** should also be added. | Spain (p.2) |
| | The current draft, and the related commentary, posits a distinction between "pledges" on the one hand and "outright transfers" on the other hand. "Pledge" is defined to include a "title | ISDA (p.5) |

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| | transfer by way of security". These distinctions, however, require careful handling, and we are not sure that the current draft of the Convention achieves the right balance. Under certain legal systems (for example, in the United Kingdom), a title transfer collateral arrangement is based on outright transfer. The fact that the commercial purpose may be to achieve an effect comparable to the creation of a security interest (for example, by way of mortgage of or charge on securities) is irrelevant. Such a transfer is a sale, and the transferee is a purchaser of the securities.<br><br>By contrast, in other jurisdictions, such as Italy, there is a middle category between a security interest, on the one hand, and an outright transfer on the other hand, namely, the irregular pledge. It achieves a transfer of title of the relevant collateral securities to the transferee, but is otherwise treated as a form of pledge for other purposes.<br><br>It is therefore questionable whether it is helpful to subsume title transfer "by way of security" under the definition of pledge, since it risks confusing the genuine outright transfer approach (on which the majority of cross-border title transfer arrangements in the European privately negotiated derivatives market are based, according to our own research) with the irregular pledge approach. By assimilating the title transfer approach to the security interest approach in the definition of "pledge", the Convention may perversely raise legal uncertainty by increasing recharacterisation risk in relation to title transfer collateral arrangements in some jurisdictions.<br><br>We note that the current draft EU directive on financial collateral arrangements uses separate definitions for "security financial collateral arrangement" and "title transfer collateral arrangement", and we would propose that a similar approach be taken in the Convention. Our suggestion would be to amend the definitions of "disposition" and "pledge" and to add a new definition of "title transfer collateral", along the following lines:<br><br>**"disposition" means pledge, title transfer collateral or outright transfer (sale);**<br><br>**"pledge" means any form of security interest, whether possessory or non-possessory;**<br><br>**"title transfer collateral" means a sale and repurchase agreement or other collateral arrangement based on transfer of title, whether by way of outright transfer (sale) or by way of security, including irregular pledge;**<br><br>It appears that no other changes would be necessary to the current draft of the Convention, as the term "pledge" is only used in the definition of "disposition". Also, we are not in favour of the additional wording it is proposed to add to Article 4(1), but if that wording is added, then we would, of course, recommend amending the words to read "at the time of the pledge, | |

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| | title transfer collateral or outright sale transaction". | |
| | As far as dealings in indirectly held securities by way of title transfer are concerned, we would like to point out that, although there is no legal regulation of title transfer in Greece, title transfer is acknowledged and accepted today by both legal theory as well as jurisprudence in Greece. A new law (L. 2844/2000, valid from 13.10.2001), regulates the so called "fictitious pledge", that is a pledge perfected without the delivery of the possession of the movable asset (which is otherwise a prerequisite for the traditional pledge). However, commercial papers and cash are excluded from the application of the said law (Art. 2 L. 2844/2000). | Greece (p.1) |
| **2(1):**<br><br>**"sûretés" (F)** | Le premier terme "*comprend*" devrait être supprimé et remplacé par le terme "*désigne*" ceci par souci de cohérence avec les autres définitions et avec la traduction anglaise. | Luxembourg (p.2) |
| **2(1):**<br><br>**"perfection"** | The present definition could be read as only including perfection made by some sort of **positive act** (i.e. filing or notification) and not automatic perfection. If the convention is to deal with insolvency of the intermediary (Art 6), it may sometimes be necessary to determine whether the customers right to the securities held by the intermediary is "perfected" against the creditors of the intermediary (that is: whether the customers or the general creditors are entitled to the securities). Such "perfection" may not require a positive act, but e.g. merely that the intermediary has kept the securities on an account where the securities have not been commingled with securities actually owned by the intermediary. If Art 6 is to apply in situation where the customers prevail under the law of the relevant intermediary merely because no commingling was made, **it may be appropriate to revise Art 2(1) so that perfection is defined as "any steps" instead of "the steps".** | Ulrik Rammeskow Bang-Pedersen / Denmark (p.2) |
| | This is a new definition and **we doubt if it is necessary**. On the contrary, it is "material", referring to a concept of a "third party", a concept that varies from one jurisdiction to another. We recommend omitting the definition. | Finland (p.3) |
| **2(1):**<br><br>**"proprietary effects" / "effets réels"** | The Canadian delegation notes that this term should be replaced by the term property rights. We question whether this definition is adequate or necessary.<br><br>Nous suggérons remplacer ce terme par « droit de propriété ». On se demande si cette définition est appropriée ou nécessaire. | Canada (p.3) |
| | The Convention employs "proprietary rights" to define its purpose (Art. 1.1), but in Art. 2 it defines "proprietary effects". Will it not be better to employ the term in both places? | Spain (p.2) |

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| | The definition of "proprietary effects" is not accurate or helpful. Property issues can arise in a two-party setting, and contracts can affect third parties. Any attempt at a brief definition of "property" is doomed to failure, given the complexity of the issue and the likelihood of differences among legal systems. Trying to define the concept will likely cause more harm than good. **We suggest deleting the definition of "proprietary effects" and using the phrase "property rights" consistently throughout the Convention.** | USA (p.3) |
| | Pour harmoniser le texte avec la terminologie couramment utilisée en langue française et avec le texte anglais, la définition devrait lire comme suit: **"désigne des effets pouvant affecter les tiers"**. | Luxembourg (p.2) |
| **2(1) : "insolvency administrator" / "insolvency proceeding"** | See our March 2001 comments. We are **still concerned whether the definitions are broad enough.** | Finland (p.3) |
| | **The words "or body" can be deleted** from the definition of insolvency administrator since according to the notes on "intermediary", the term "person" covers legal persons, natural persons, unincorporated firms and partnerships. | The Association of German Banks (p.4) |
| **2(1): "office or branch"** | **Do we need a definition of the words "office or branch" (Internet)?**<br>See Prof. Roger's comments of 07/05/2001, and the Danish comments (*e.g.*, does the intermediary have to have at least one employee, is an agent sufficient or is there no requirements that "human means" is used at all?; p.4, see also *infra* under Art. 5) | Prof. Rogers<br>Ulrik Rammeskow Bang-Pedersen / Denmark (p.4) |
| **2(2): "transfer by operation of law"** | **Inclusion** of transfer by way of operation of law within the scope of the Convention **does not seem to be appropriate**. The Convention is primarily concerned with transfer under a legal transaction. We therefore support deletion of the reference to a transfer by way of operation of law. | Germany (p.2) |
| | Les transferts en vertu de la loi **devraient être maintenus**, la Convention étant si non fatalement incomplète, étant donné qu'elle ne pourrait régler le conflit pouvant exister entre des privilèges établis par la loi et d'autres sûretés ou droits pouvant exister sur des titres détenus auprès d'intermédiaires. | Luxembourg (p.2) |

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| | In relation to Art. 2.2, at first, it seems reasonable to protect "the transfer of securities by way of operation of law" as long as the reason of this law is to protect some particular creditors or systems as a whole. **But it introduces some difficulties. In some cases, those transfer may be characterized as transfer of public law nature, whilst the Convention only deals with private law questions.** The consequences can be dangerous; for instance, some people have asked if this rule covers **expropriations**. | Spain (p.2) |
| | We remain of the view that the bracketed language **is important and should be retained**. In some jurisdictions the critical need for certainty in the rights of an intermediary to liquidate account positions in the event of its customer's default has been met by statutory provisions creating clearing liens by operation of law. Without clarity on choice of law for this issue, the objectives of the Convention will not be met.<br><br>The defined term "relevant intermediary" should be used in place of "account holder's intermediary." New proposal:<br><br>"References in this Convention to a disposition of securities held with an intermediary include a disposition~~[~~, as well as a transfer by way of operation of law,~~]~~ in favour of the relevant ~~account holder's~~ intermediary." | USA (p.3/4) |
| **2(4)** | It is **very important to explicitly exclude indirect holding systems** from the scope of the Convention. Present formulation of Art. 2, para. 4 is one way achieve this end. The new Art. 2, para. 4 has great importance in sharpening the definition of "securities account". | Finland (p.2 and 3) |
| | **The understanding of Art. 2.4 has been rather problematic.** Several expert consider that from the text of the article is not easy to capture the situation. The categories "person recorded on a securities account purely in an administrative capacity" or "manager or agent for the account holder" are not always understood in the same way. Many intermediaries may be legally characterized as agent of the account holder, at least in legal systems where the intermediary holding pattern has not been expressly recognized by the lawmaker. The risk in this case is that the intermediary be not consider as such because of Art. 2.4. If the situation this article deals with is that in which both the name of the owner and the name of an account manager appear in the books of the CDS, and the account manager maintains parallel records, then this should be explicitly said in the text of the article. | Spain (p.2) |
| **2(4) (F)** | La terminologie française utilisée ne semble pas à tout endroit appropriée. Ainsi il est **proposé de remplacer le terme de "capacité d'administrateur" par "qualité d'administrateur" et le terme "agent" par celui de "mandataire".** | Luxembourg (p.2) |

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| **3:**<br><br>**"internationality"** | If the second sentence of this text is not meant to be exhaustive, then the Canadian delegation is of the opinion that it is not necessary. Therefore, we suggest to delete the second part of the text and keep only the first sentence on this Article as it is sufficient. The second part should instead be included in the commentary.<br><br>Si la deuxième partie du texte n'est pas exhaustive, nous suggérons qu'il serait préférable de la supprimer car elle ne semble pas nécessaire. Cependant, nous croyons important d'insérer cette deuxième partie dans le rapport. La première phrase devrait être conservée. | Canada (p.3) |
| | **Perhaps Art 3 is not needed.** If the persons listed in Art 3 are all located in the same State, it could seem as if application of the law of that State would follow from Art 4. Art 3 may give rise to some confusion as to the scope of the Convention. Imagine a situation where an issuer located in X issues securities through a CSD located in X and some of those securities are purchased by a person located in X. The buyer chooses to hold his securities through a bank (intermediary). The bank has its head office in X, but has a branch in Y. Does the convention apply? The answer seems to depend on whether the bank is considered to be located a) in all States where the bank has an office, b) in the State where the head office is, or c) in the State where the buyer chooses to open his account. If b) is the right understanding of Art. 3, the buyer would not be protected by the rules in the Convention if he opens his account at the office in Y. Even if the buyer chooses to open his account at the office in X, it could be argued that the Convention should apply so that the purchaser can rely on the application of the law of X. If so, it might be preferable not to condition the application of the Convention on some sort of "internationality". | Ulrik Rammeskow Bang-Pedersen / Denmark (p.3) |
| | This new provision is linked to the paragraph 2 of Art. 1. In disputes the issuer of securities involving, it is important to make sure that the PRIMA rule is applied only proprietary law questions. | Finland (p.3) |
| | In order to ensure a clear determination of the parties involved and thus as uniform an application of the Convention as possible, **the term "located" should be defined more precisely.** | Germany (p.2)<br>The Association of German Banks (p.4) |
| | **The second sentence is unnecessary.** It merely provides illustrations of circumstances that might pose a choice between the laws of different States. This should be covered in **explanatory comment** rather than in the Convention text. The listing is not truly effective as Convention text, because it relies on the concept of "location." As we have learned all too well, that concept is difficult to apply in this context. Moreover, the wording of **clause (e)** might be problematic as black-letter text in that it uses the colloquial notion of one intermediary holding "the securities" through another. That is a colloquialism that connotes | USA (p.4) |

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| | the "look through" approach that the Convention seeks to eliminate. Even in the commentary, **it may be better to omit discussion of element (e)**, since it is potentially confusing, and it is relatively unlikely that there are any significant cases of internationality covered by this element and not by any other. | |
| **4(1):**<br><br>**direct reference to the place of the relevant intermediary** | It would be **inappropriate** to include reference to the "place of the relevant securities account" in this provision. | Czech Republic (p.1) |
| | As we stated in our March 2001 comments, **we prefer taking directly the place of the account as a main rule.** | Finland (p.3) |
| **4(1):**<br><br>**[proprietary] [property] "rights"** | The word "**rights**" used in Art. 4, para. 1 (instead of "dealings") is acceptable. | Finland (p.1) |
| | The term "**proprietary**" should be added between governing and rights (that is, "the law governing proprietary rights..."). This keeps coherence with other articles. | Spain (p.2) |
| **4(1):**<br><br>**relationship with federal clause** | To clarify the relationship between Articles 4/5 and Article 10, discussed more fully under Article 10 below, we suggest adding the phrase "of the State" in Article 4, as follows:<br><br>Art 4(1) The law governing rights in securities held with an intermediary (the "applicable law") is the law of <u>the State in which</u> the place of the relevant intermediary <u>is located</u>. | USA (p.4)<br>Canada (p.3) |
| **4(1):**<br><br>**"particular moment in time" to be considered when determining the relevant inter-mediary** | **It may not always be obvious which particular moment in time that is the relevant.** For example, part of a pledge or title transfer agreement may be that the securities are to be transferred from one intermediary to another. If the person pledging the securities (or transferring these by a title transfer) enters into insolvency and the securities are subsequently transferred to the new intermediary (because the former intermediary had no knowledge of the insolvency proceedings), it may seem questionable whether law of the former or new intermediary is decisive with respect to the validity of the pledge/title transfer against the insolvency administrator. As to which moment of time is the relevant, it could be suggested to focus on the place of the intermediary at the time when the conflict of rights arose (*i.e.* at the time when a competing pledge was granted). **Perhaps Art 4(1) should not focus on which law governs the rights in the securities, but instead which law governs in a specific conflict concerning the securities.** Another way of dealing with the problem could be **address it in the definition of "relevant intermediary"** in Art 2 as the question of which moment in time is the relevant one often is similar to the question of which intermediary is the relevant one. | Ulrik Rammeskow Bang-Pedersen / Denmark (p.3) |
| | As we stated in our March 2001 comments, it is **crucial for us to clarify explicitly what is the relevant time** that determines the applicable law so that the parties would not be able | Finland (p.4) |

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| | to change the applicable law freely. We see the risks from an explicit rule being smaller than the advantages. | |
| | The notes address the issue of what moment in time should be considered when determining the relevant intermediary. German law normally differentiates between two points in time where dispositions are concerned: the real agreement on the transfer of title, and moment of disclosure (e.g. delivery/recording). When dealing with dispositions of securities, the moment of disclosure could be the recording of the securities on the securities account. **Determining the relevant intermediary should focus on the moment in time when the securities are recorded on the account in order to avoid possible uncertainty.** | The Association of German Banks (p.4) |
| | **ISDA endorses the current wording and agrees with the suggestion in the commentary that the inclusion of the words "at the time of the pledge or outright sale transaction" would not be helpful (possibly, in fact, the reverse).** However, if such wording is added, then we would recommend amending the words disposition, pledge and title transfer collateral to read "at the time of the pledge, title transfer collateral or outright sale transaction" | ISDA (p.6) |
| **4(2)(a):**<br><br>**"characterisation" / "proprietary** | We understand the Permanent Bureau's concerns about the word "characterisation," and agree that the phrase "legal nature" is better. The word "derived" might also be somewhat confusing, so we suggest changing as follows:<br>"(a) the legal nature of the rights that result derived from the credit of securities to a securities account;"<br>Nous préférons l'utilisation du terme « nature juridique ». On suggère encore une fois de remplacer « découlant » par « qui résulte ». | Canada (p.3) |
| | We are **not in favour** of using the term "characterisation" instead of "legal nature" in Article 4 (2) (a). As is stated in the comments, this expression is used in many different ways and means different things to different people. For reasons of legal certainty the term "legal nature" is preferred. | Germany (p.2/3)<br>The Association of German Banks (p.4) |
| | We find the **argumentation against** the word "characterisation" **convincing**. | Finland (p.4) |

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| | We understand the Permanent Bureau's concerns about the word "characterisation," and **agree** that the phrase "legal nature" is better. The word "derived" might also be somewhat confusing, so we suggest changing as follows:<br>"the legal nature of the rights that result ~~derived~~ from the credit of securities to a securities account;" | USA (p.4) |
| | For **consistency** in use of "proprietary …" change this provision as follows:<br>"the legal nature of, and property rights that result from, ~~and proprietary effects of~~ a disposition of securities held with an intermediary;" | USA (p.4) |
| **4(2)(c):**<br>**scope of applicable law / perfection requirements** | To **avoid any conclusions *a contrario***, it may be suggested to explicitly state in Art 4(2)(c): "and the effects of perfection or non-perfection and the priority between competing rights in the securities". | Ulrik Rammeskow Bang-Pedersen / Denmark (p.4) |
| **4(2)(d)** | Use **consistent** wording:<br>"whether a person's title to or other interest in securities held with an intermediary is overridden by or subordinated to a competing title or interest;"<br>"si le droit d'une personne sur des titres détenus auprès d'un intermédiaire peut être primé par ou subordonné à un droit concurrent ; » | USA (p.4/5)<br>Canada (p.4) |
| **4(2)(e** | Use consistent wording:<br>"the duties, if any, of an intermediary to a person who asserts a competing title to or other interest in ~~claim to~~ securities held with that intermediary; and"<br>The phrase "if any" is useful to clarify that there may be no such duties under the law of a particular State.<br>« les obligations, s'il y a lieu, d'un intermédiaire envers une personne qui revendique des droits concurrents ou d'autres intérêts sur des titres détenus auprès de cet intermédiaire ; »<br>Le terme « s'il y a lieu » indique la possibilité qu'il n'existe aucune obligation en vertu de la loi d'un État particulier. | USA (p.4/5)<br>Canada (p.4) |
| **4(2)(f)** | It might be helpful to include the words **"by an account holder"** after the words "that intermediary", to make explicit that this provision refers to a third party claimant competing with an account holder in relation to securities held indirectly by that account holder. | ISDA (p.6) |

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| | The concept of "**realisation**" makes sense only with respect to a pledge, hence **change (f) as follows:**<br>"the steps required for the realisation of a <u>pledge</u> ~~disposition~~ of securities held with an intermediary."<br>Le terme « réalisation » ne peut qu'être utilisé qu'en vertu d'une sûreté. | USA (p.5)<br>Canada (p.4) |
| | Dans un souci d'une approche logique des différentes étapes d'un transfert il est proposé de faire figurer le sous-point (f) actuel comme sous-point (b) de cet article | Luxembourg (p.2) |
| **5:**<br><br>**"account approach" v "branch/office approach"** | During a meeting of the Australian Delegation four proposals were made. We then asked industry representatives (particularly through ISDA) to consider our proposals. The Annex to this chart contains the proposals modified in light of the comments received. **See drafting proposal in the *Annex.***<br>Different States may find these proposals more or less attractive depending on their legal culture and traditions. If we put to one side existing agreements, it seems from our discussions here to date that **all of the options provide the minimum level of ex ante certainty that is being sought,** at least in the Australian context under the new Financial Services Reform Bill. Under the new regime (which is to come into effect in March 2002), even though it is the *provider* of custodial and depositary services who is to be regulated, by needing to have an Australian financial services licence, still the regulator, ASIC, has **supervisory powers over the *business of maintaining securities accounts*,** with an obligation on the licensee to do all things necessary to ensure that the financial services covered by the licence are provided efficiently, honestly and fairly.<br>If one includes existing agreements in the analysis, it appears that both proposals 3 and 4 should be acceptable, and possibly proposals 1 and 2 as well. Indeed the suggestion that Proposals 1 and 3 be combined may be the best solution. Under this proposal, if the intermediary cannot satisfy Proposal 1, before moving to the basket in paragraph 5(3) of the July Draft a certificate under Proposal 3 would suffice.<br>Please note that for each proposal the term "**regulatory supervision**" or "**regulatory oversight**" needs to be **defined** somewhere in the Convention to include *national or regional* supervision or oversight. | Australia (p.1/3) |
| | Canada would express a **slight preference for the Branch/office approach**. From a Canadian perspective, the Accounts approach creates a fiction and leads us in effect to the Branch/office approach in any event. We must also recognize that the Branch/office approach for example, in an electronic context, may also be a fiction.<br>We recognize that both approaches, locating the account or branch/office pose certain difficulties from the perspective of traditional private international law rules. We would | Canada (p.4/5) |

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| | encourage the Conference to seek a pragmatic solution that will work for all jurisdictions.<br>We would prefer Option B. As mentioned in the US comments, Option A is unworkable because regulatory agencies typically regulate the intermediary, not the account.<br><br>Le Canada préfère l'approche dite **«de l'établissement ou de la succursale»**. D'une perspective canadienne, l'approche dite « du compte » crée une fiction et nous mènerait de toute façon à l'approche de l'établissement ou de la succursale. On doit aussi reconnaître que l'approche de l'établissement ou de la succursale, dans un contexte électronique, par exemple, nous mènerait aussi à une fiction.<br>D'une perspective des règles traditionnelles en droit international privé, nous reconnaissons que les deux approches posent des difficultés. Nous encourageons la Conférence à chercher une solution pratique qui sera appropriée pour toutes les juridictions.<br>Nous préférons **l'option B**. Tel que mentionné dans les commentaires américains, l'option A ne fonctionne pas car les agences de réglementation régissent habituellement l'intermédiaire et non le compte. | |
| | The place of the **account** would seem to be **better in line with the traditional *lex rei sitae* rule.**<br>The place of the account (or register) is the conflict of laws rule in the EU legislation, e.g. Art 9, para. 2 of the EU Settlement Finality Directive. It is in our interest to avoid situations where the Convention and EU legislation are in potential conflict.<br>See our March 2001 comments under Article 3 and 4 (p. 3–4) where we favoured an objective way to determine the place of the account.<br>In practice this means backing a compromise model of letting parties to the custody agreement to agree on the place of the account but at the same time requiring that the agreed place has to have a real connection to the place of the account and the operations of the intermediary. As we stated, we prefer a rule that is connected directly with the intermediary's regulatory obligations concerning the account. That is why we prefer Option A in both the "account approach" and "branch/office approach". The text is overall simpler and clearer than before so we are flexible toward both the approaches. Option C of the account approach, however, gives too much freedom of choice to the intermediary. | Finland (p.4) |
| | Unambiguous determination of the place of the relevant intermediary is one of the central issues of the Convention. **Neither the "account approach", nor the "office approach" convinced the business representatives because the determination has been linked to additional distinctive criteria.** On the one hand, a link was established with regulatory supervision of the maintenance of the account, and on the other, with supervision over the intermediary. However, since intermediaries with cross-border activities may be subject to | Germany (p.3) |

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| | supervision by more than one state, **these links do not constitute suitable criteria**.<br><br>Following the ***lex rei sitae rule***, the Federal Ministry of Justice has submitted a proposal for determining the place of the relevant intermediary which is oriented towards practical needs; **See drafting proposal in *Annex*** | |
| | We are in favour of ***the branch/office approach***, together with ***Option B***, that is: **"The place of the relevant intermediary is the place of the office or branch of the relevant intermediary agreed between the account holder and the intermediary, provided that it is a place where the intermediary is subject to regulatory supervision".** In this way, two restrictions with regard to the choice of the relevant intermediary are placed on the parties: (a) The place of the relevant intermediary has to be contractually agreed between the parties, leaving no room for legal uncertainty and ambiguity, (b) Further to the contractual choice, certainty is corroborated by the administrative regulatory supervision on the intermediary. | Greece (p.2) |
| | Les autorités luxembourgeoises sont d'avis qu'il faut favoriser une solution qui donne aux parties à un transfert la sécurité juridique nécessaire *a priori*. Il faut cependant éviter que les critères retenus ne puissent mener à des solutions sans rapport avec la réalité. Il faut donc que soit **toujours maintenu un lien entre ce qui pourra être convenu par les parties et une certaine réalité**. Il est cependant considéré que cette réalité doit être une réalité **facilement vérifiable** pour les parties à un contrat sans qu'elles n'aient à faire d'enquête poussée auprès de tiers et éventuellement d'administrations pour obtenir confirmation qu'elles ont choisi la loi appropriée.<br><br>Dans ce contexte il est considéré que **la référence à une "surveillance réglementaire" n'est pas de nature à atteindre le but recherché de la certitude a priori, mais peut être une source d'incertitudes supplémentaires pour les parties à une transaction.** Ainsi se posera pour les pays membres de l'Union Européenne la question de savoir si les succursales d'établissements de crédit établies dans un Etat Membre y sont soumises à une surveillance réglementaire au sens de la Convention ou si cette surveillance réglementaire n'existe que dans le pays d'origine. Le renvoi à la surveillance réglementaire pourra également générer des débats sur la qualité de la surveillance, un tribunal pouvant éventuellement considérer qu'une surveillance effectuée dans un certain pays ne peut être considérée comme surveillance réglementaire au sens de la Convention faute de remplir certains standards.<br><br>**L'objection que soit la convention des parties soit une attestation pourraient conduire à des abus, doit être écartée** dans la mesure où la Convention ne peut pas raisonnablement prendre en considération l'hypothèse où les parties feraient de fausses | Luxembourg (p.3) |

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| | déclarations ou agiraient en fraude. Si les parties le faisaient elles engageraient leur responsabilité. La Convention doit partir de l'hypothèse de conventions conclues et d'attestations établies de bonne foi. La limitation décrite plus haut d'un certain critère de rattachement à un lieu où l'intermédiaire a un établissement devrait réduire de toute façon ce risque.<br><br>**See drafting proposal in *Annex***<br><br>We consider preferable the "**account approach**". It is true that the location of an account is rather fictitious, but (a) it is quite common among practitioners to think of an account as something that is located in one place or another, that is, in one office or another; (b) the account, and not the branch, is the "thing" to which the securities are credited and where the dispositions are recorded; (c) it is a connecting factor already used in different laws (The Finality Directive, Art. 9; or the Directive on the reorganization and winding up of credit institutions, Art. 24). We would prefer to keep coherence when these rules.<br><br>Between option A and B of the account approach, **option A seems preferable**. It offers a clear element of the effectiveness of the location of the account. Nevertheless, some expert raised the following problem: **what happen when the authorities of the place so agree does not "supervise" this account?** This rule presumes that the account is subjected to supervision in the place agree according to the regulation of that place. But, at the end of the day, this supervision depends on of the regulation in place in that country. It may be that according to the law of the place agreed by the parties, its authorities only supervise account which contain national securities. But they have no interest in supervising account which only maintain foreign securities. What will happen in this case?<br><br>We consider that **option C is misplaced**, and excessive. Its is not a real alternative to A and B. It tries to establish a presumption in favour of good faith parties, that can be reasonable. But as it is now, it creates a lot of problems and goes much further than its purposes. What the rule says is that the intermediary can decide unilaterally where to locate the account and that this location is conclusive. The rule does not require any real connection to the place designed in the certificate. Also, it contains a general rule, without requiring good faith in the parties concerned. | Spain (p.3) |
| | From the two basic approaches presented in Article 5, **we prefer the "account approach,"** for it appears better suited to deal with current and possible future realities in the securities markets. We further suggest **alternatively using both Option A and Option B so that it suffices that either of the two conditions is satisfied.** | Switzerland (p.2) |
| | The **"branch/office approach" would work better than the "account approach"** | USA (p.5) |

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| | because it minimizes the use of fictions. The starting point of our challenge in this project is the fact that accounts have no location and that increasing globalisation of this business has led intermediaries to disperse the various aspects of account maintenance across jurisdictions so that there is no obviously "right" answer to the location question. We think that elimination of the concept of location of an account may be a helpful step.<br><br>**With respect to the "nexus" test, we strongly prefer some version of the Option B approach to the Option A approach.** We believe that **Option A ("intermediary's maintenance of the securities account is subject to regulatory supervision") is unworkable, principally because regulatory agencies typically regulate the intermediary, not the account. With respect to Option B, we think that it could be improved.**<br><br>**See drafting proposal in *Annex.***<br><br>We understand that some have suggested that Option B could be improved by the addition of a requirement that **"the maintenance of that securities account forms part of that business in that place." We strongly disagree with that suggestion.** The suggestion is inconsistent with the entire concept of a "safe-harbor" test to provide ex ante certainty. Asking whether the maintenance of a particular account is "part of the business of" a particular office or branch is not a useful test of the question of the location of the relevant intermediary, it is just restating the question. The only way one could decide whether the "is a part of the business of" test is satisfied is by the multi-factor inquiry described in the "basket" clause in Article 5(3). Thus, adding an undefinable concept like that as a condition to the operation of the safe harbor is equivalent to deleting the safe-harbor test altogether and leaving only the "basket.' There has been substantial concern expressed for some time that reliance on the basket does not lead to the necessary degree of *ex ante* certainty. | |
| | Determining unequivocally the place of the relevant intermediary is one of the key issues of the convention. It is extremely difficult to find a solution which provides certainty and will be easy to implement. In Article 5, the draft offers various options. These proposals are likely to give rise to difficulties in practice, however. We would like to elaborate on this point below.<br><br>The draft first puts forward the "account approach" and the "branch/office approach".<br><br>**The branch/office approach seems to be the more direct**. It assumes that a branch or office actually exists at the location in question. This element should, in any event, be considered so that determining the place of the relevant intermediary focuses at least to this extent on tangible factors, and not only on the arrangements made by the parties involved.<br><br>***a) "Account approach", Option A*** | The Association of German Banks (p.5-7) |

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| | Under Option A of the account approach, the securities account is deemed to be maintained at the place of an office or branch of the relevant intermediary agreed between the account holder and the intermediary. A further criterion is that the intermediary's maintenance of the account is subject to regulatory supervision at this place. **In principle, it is to be welcomed that another tangible element must exist alongside the presence of an office or branch. Supervision of the maintenance of the account is not a suitable criterion, however, and should therefore be dropped.** In Germany, the above-mentioned section 17a DepotG also does not provide for this requirement. Custodians who are active on a cross-border basis, in particular, are often subject to the supervision of several countries. **In the European Union, solvency supervision is normally determined by the home country and market supervision by the host country, though a certain amount of overlap cannot be excluded.** On top of that, the creation of the European single market for financial services may also result in the establishment of a pan-European regulatory authority. Reference to the supervisory situation when determining the applicable law therefore introduces an element of uncertainty. The parties involved in dispositions of securities would first have to clarify comprehensively which authority was responsible for supervision – assuming that complete clarification of this point would be at all possible. Furthermore, it seems incongruous to make the PIL issue of determining the law applicable to a cross-border situation dependent on a previous clarification of supervisory questions. **Determining the relevant location on the basis of regulatory criteria is therefore to be fundamentally rejected**.<br><br>***b) "Account approach", Option B***<br><br>Option B of the "account approach" differs from Option A in that the intermediary itself, not the maintenance of the account, must be subject to regulatory supervision at the location in question. **As explained above, supervision is not a suitable criterion to determine unequivocally the location of the relevant intermediary.** If a determining factor is the supervision not just of a particular activity, but of the intermediary as a whole, the problem of double or multiple supervision is even exacerbated.<br><br>***c) "Account approach", Option C***<br><br>Option C of the "account approach" provides that a certificate issued by the intermediary will specify where the account is maintained. According to the text in brackets, either the intermediary's maintenance of the account or the intermediary itself must be subject to regulatory supervision at this location. The designation of a location on a certificate issued by the intermediary is **unlikely to prove a suitable criterion**. By ignoring the criteria of the account or the branch/office, there is no reference to any tangible factor. On the contrary, it is left to the discretion of the intermediary alone to designate the location at which the | |

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| | account is maintained. Moreover, the question arises as to how one can be sure that the same location is relevant to the maintenance of an account throughout the entire duration of a contract, such as a contract governing the provision of collateral, for example. In addition, as explained above, the **possible addition of the supervision criterion would not help to clearly determine the applicable law. This option should definitely not be pursued further.**<br><br>***d) "Branch/office approach", Option A***<br><br>Under Option A of the "branch/office approach", the place of the office or branch of the relevant intermediary agreed between the account holder and the intermediary is decisive, provided that the maintenance of the securities account is subject to regulatory supervision at this location. For the reasons outlined above, **reference to regulatory prerequisites will, in very many cases, render it no easier to determine the applicable law,** so this should not be made the standard approach.<br><br>***e) "Branch/office approach", Option B***<br><br>Option B of the "branch/office approach" differs from Option A in that the intermediary itself must be subject to regulatory supervision in the place agreed. As explained above, **reference to supervision of the intermediary is likely to make it difficult to determine the applicable law**, so this option should not be pursued.<br><br>***f) Connecting factor***<br><br>**The connecting factor could be the office where the account is maintained. This is the place where crediting takes place, namely the place where the securities account is administered on the basis of the agreement to establish an account. This place can ultimately be determined by the account number on the statement of account.** If it is not possible to identify the location of the account-maintaining office on the basis of this documentation, the **place where the agreement to open an account was concluded** could be taken as circumstantial evidence. A backup criterion might be the **head office** of the intermediary (administrative headquarters). The place of the **head office is preferable to the registered seat** indicated in the articles of association because linkage with an office which actually exists rather than with a registration or other formality is more in line with the methodology of the draft convention's approach to focussing on the relevant intermediary. Furthermore, it would be inappropriate if, for example, a bank had its head (or possibly only) office in one country, but the laws of another country were applied because the bank had its legal seat in another country for reasons of company law – a typical constellation in certain situations. In Germany, section 17a DepotG, moreover, also focuses on the "head or branch office which maintains the account", not on the registered office. The | |

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| | further criteria in Article 5, paragraph 3 could then be dropped. | |
| | While acknowledging the difficulties of locating an account, ISDA members nonetheless believe that the **account approach may have some advantages over the branch/office approach.** For example, some members believe it is intuitively more consistent with the traditional *lex rei sitae* rule and therefore may result in a formulation that is more acceptable to a broader range of jurisdictions. We believe it is premature to limit discussion to one approach or the other. **See proposal in *Annex*** | ISDA (p.2) |
| | We have focussed our attention solely on the text of Article 5 ("Determination of the place of the relevant intermediary"). While we recognize that other provisions raise important issues, Article 5 is the heart of the Proposed Convention. In the Association's view, Article 5 should accomplish five important objectives –<br><br>· The standards by which the place of the relevant intermediary is determined should provide as much certainty as possible. If the Convention does not provide certainty with respect to the law applicable to interests in accounts held by an intermediary, it will not have attained its goals.<br><br>· All parties should have an objective and easily accessible way of determining the place of the relevant intermediary with respect to a particular account so that they can ascertain and protect their rights under the appropriate law. The risk that a court will hold, after the fact, that a security interest in an account was not validly perfected because the secured party relied on the wrong set of laws should be very limited. To the greatest extent possible, the rights of the third parties that have acted in good faith should be protected.<br><br>· The intermediary and the account holder should have reasonable latitude, consistent with the norms of international law, to select the office or branch of the intermediary at which the account is deemed to be maintained. While we recognize that this proposition is controversial, we believe that an agreement between the parties, subject to appropriate limitations on the location they may select, is the most workable solution to the problem of creating certainty.<br><br>· The Convention should not require the re-negotiation of existing custody agreements. Therefore, the Convention should contain a mechanism for establishing the place of the relevant intermediary under existing agreements.<br><br>· As a corollary, the Convention should also provide a mechanism for addressing changes in the location of an account. Third parties who have perfected their rights based on the original location should be afforded a reasonable opportunity, after receiving notice of the change, to re-perfect in the new location or otherwise to protect their interests. | Association of Global Custodians |

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| | **Summary of the Association's Proposed Article 5**<br><br>To implement these objectives, the Association has drafted a version of Article 5 that combines aspects of Options B and C of the "Account Approach" set forth in the "Annotated July 2001 Draft" circulated by the Permanent Bureau. The Association's proposal consists of a three-tiered framework for determining the place of the relevant intermediary.<br><br>· Tier #1: Agreement - As under Option B of the Account Approach, a securities account would be deemed maintained at the place of the office or branch of the relevant intermediary as agreed between the account holder and the intermediary. Third parties could rely on a "Notice of Agreement" issued by the intermediary specifying the place where the account is maintained. The Notice of Agreement concept is intended to provide certainty concerning the place to which the intermediary and the account holder have agreed, without requiring that the custody contract itself be delivered to third parties or that third parties concern themselves with issues regarding the validity of that contract.<br><br>· Tier #2: Certificate – Absent an agreement, the intermediary could issue a "Certificate of Place" designating the place of the office or branch where the securities account is maintained. This aspect of the proposal mirrors Option C of the Account Approach. Such certificates could be issued in the case of contracts that contain no agreement regarding the place of the account. Certificates of Place could therefore be employed with respect to both existing and future contracts that are silent on the place of the relevant intermediary. As in the case of Notices of Agreement, a third party could rely on such a certificate in determining how to protect its rights.<br><br>· Tier #3: Fallback – In the event there is neither an agreement between the intermediary and the account holder concerning the place of the office or branch, nor a Certificate of Place issued by the intermediary, the parties (or a court) would look to a series of factors to determine the place where the account is maintained. Our proposal incorporates the factors in the July 2001 Draft. However, under our proposal, the need to apply these factors should be rare, since it should always be possible for the intermediary to issue a certificate.<br><br>We recognize that the certificate approach, described in Tier #2, has been previously discussed and that there may be sentiment to limit the ability of intermediaries to issue certificates to a fixed period of time (e.g., two years) following the effective date of the Convention. While we believe that it would be preferable to make the certificate option permanent, the most important function of intermediary certificates would be to avoid the need for amendments to existing contracts. We are open to debate and discussion as to whether this power should be permanent or time-limited. | |

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| | **Nexus Between the Intermediary and the Place of the Account**<br><br>As noted above, the Association's proposal follows in form the "Account Approach" set forth in the July 2001 Draft. The Account Approach provides that "[t]he place of the relevant intermediary is the place where the securities account with that intermediary is maintained." A fundamental issue is, of course, the nature of the nexus required between the place specified in an agreement or certificate and the intermediary. Under the Association's proposal, any place could be agreed upon between the parties, or designated in a Certificate of Place, provided that two requirements were met –<br><br>(1) the intermediary must have an office or branch (or other form of legal presence) in that place; and<br><br>(2) the intermediary must be either<br><br>(a) authorized to do business by a local regulatory authority in such place, or<br><br>(b) supervised by a local regulatory authority in such place.<br><br>The intent of this provision is to require that the intermediary have sufficient legal nexus to, and presence in, the place selected so that the intermediary would be subject to the jurisdiction of the local courts in litigation to enforce the rights of persons claiming an interest in the account.<br><br>**See proposal in *Annex*** | |
| | **Need for definition of "office" and "branch"** (see *supra* Art 2(1)<br>It may be that any operation which is subject to regulatory supervision will always satisfy the (chosen) requirements for a(n) office/branch, but if that is the case there is no need for a(n) branch/office-requirement (that is **Option C - last part - should be preferred**).<br>If there is a need for the Convention to uphold agreements with intermediaries, which are not subject to regulatory supervision, it could be considered (as Option D) simply to state that and account is maintained (located) in the State agreed between the account holder an the intermediary provided that the intermediary is subject to regulatory supervision in that State or the intermediary has a branch/office in that State (and consequently include a definition of office/branch, which requires an activity with human means).<br>In any event, it would be useful to receive information on to which extent *e.g.* brokers that operate in different States are subject to regulatory supervision in all those States. | Ulrik Rammeskow Bang-Pedersen / (p.4)<br>the comments re Art 5 are meant to be an input for further discussion and not an official Danish statement as to which solution should be preferred |
| | "For the purpose of relevant intermediary's seat specification, we suggest to stipulate as a site of an intermediary **an office or a branch of the intermediary, agreed mutually by** | Czech Republic (p.1) |

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| | **an account holder and the intermediary. It is in this place where the intermediary will be subjected to a regulator.**" | |
| **5:**<br><br>**"protection of third parties"** | The Canadian delegation is of the view that consideration must be given to adding a provision to protect third parties who must rely on the intermediary for information that the test has been satisfied.<br>We would support the US proposal that a version of the Option C approach be used in addition to the basic Option B test. This suggestion appears to be a useful mechanism to resolve uncertainty.<br>La délégation canadienne est d'avis qu'il faut étudier la possibilité d'ajouter une disposition pour protéger les tierces parties qui doivent se fier à l'information provenant de l'intermédiaire à savoir si les critères de connexité sont satisfaits.<br>Nous appuyons la proposition américaine qui suggère d'adopter une version de l'option C en plus du test de base de l'option B. Cette suggestion semble être une solution utile pour résoudre l'incertitude. | Canada (p.5) |
| | We also suggest that — whatever language is ultimately devised for a nexus test — consideration be given to adding a provision to protect third parties who must rely on the intermediary for information that the test has been satisfied. Any nexus test will require some degree of investigation and legal analysis to determine whether the location identified in an account agreement would be effective under the Hague Convention. The facts needed to make that conclusion would presumably be knowable only to the securities intermediary that is maintaining the account. Third parties would have no way of independently determining whether the nexus test had been satisfied, even in cases in which the securities have been moved into a special pledge account that the intermediary maintains for the pledgee. Thus, any nexus test inherently compromises the objectives of certainty and transparency. To reduce this problem we suggest that a version of the Option C approach be used in addition to the basic Option B test. That is, the location rule would be based on agreement plus nexus, but another provision would state that a certification or representation by the intermediary that the nexus is satisfied is conclusive in favor of a person other than the intermediary.<br>**See drafting proposal in *Annex.*** | USA (p.6) |
| **5:**<br><br>**"existing documentation"** | The Canadian delegation **strongly supports** the need for a transitional rule to deal with the problem of existing agreements. We look forward to further discussions in this area.<br>La délégation canadienne est **fermement en faveur** d'une règle transitoire pour traiter des ententes existantes. | Canada (p.5) |
| | Il faudra également veiller à ce que la Convention prévoie un système pouvant résoudre le problème des contrats de dépôt conclus dès aujourd'hui et qui ne contiennent pas une | Luxembourg (p.3) |

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| | désignation précise du lieu de tenue du compte. A cette fin la possibilité pour l'intermédiaire de produire une attestation pourrait constituer une solution fort utile. | |
| | The Convention **has to specify** whether both existing and future rights are within its scope or whether it only applies to future agreements. | Czech Republic (p.1) |
| | We consider **necessary** a rule dealing expressly with custody agreement already in place. That is, a rule establishing the application of the convention to those agreement. Otherwise, one could argue that the general rule is the non-retroactivity of the international conventions, and therefore that the Convention does not apply to those agreement. It is true that the convention only deals with proprietary rights. But as long as the location can be decided by an agreement between the parties (with the limits set for in Art. 5), there is a contractual element in it. The risk is that a judge apply the general principle according to which, the contract and its clauses shall be governed by the law in place at the moment when the parties enter into it. And therefore, that the convention does not apply to custody agreement signed before it. To prevent this interpretation it would be better a rule clarifying this point. | Spain (p.4) |
| | We continue to believe that it is **important to deal with** the problem of existing agreements. We understand that some have suggested that in cases where there is no agreed location, a certification by the intermediary have the effect of an agreement. We would support that approach. In addition, this problem might be handled by a temporary "transition" rule. That is, we would pick a date, perhaps two years after the Convention becomes effective. With respect to account agreements executed before that date we would have special interpretive rules along the lines of those we have suggested before. **See drafting proposal in *Annex*** | USA (p.6) |
| | The ideal rule would provide certainty for both future and existing agreements, without requiring a burdensome process of checking and/or (worse) amending existing agreements and without requiring onerous changes to the way securities account relationships are currently opened, maintained and documented. While not necessarily claiming to have achieved this in our proposals, we believe that this ideal should be kept in mind during further discussions on Article 5. **See drafting proposals in *Annex*** | ISDA (p.3) |
| **5(3):**<br><br>**fall-back rule based on objective factors** | The **closest connection test** should be explicitly mentioned. | Finland (p.4) |

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| **5(3):**<br><br>**fall-back rule based on objective factors** | **The relation between Art. 5 (3), the white list, and Art. 5 (4), the black list, is not clear**. The inclusion of both lists may have sense when there is a general clause such as the "most closest connection" or something equivalent. Actually, the words of Art. 5 (3) ("..the factors that may be considered...") seems to presume that kind of clause. But if this is so, it should be state explicitly. | Spain (p.4/5) |
| | We would, as we stated in our March 2001 comments, **delete reference to "internal or external reporting purposes".** "Regulatory and accounting purposes" would be a sufficient factor. | Finland (p.4) |
| **5(3):**<br><br>**"basket" vs "cascade"** | Article 5, paragraph 3 lists further possible criteria in the event that the applicable law cannot be determined on the basis of paragraph 2. **The possible criteria are listed in (a) to (e) in no order of precedence.** Some individual sub-paragraphs even contain several different criteria to be used in determining the place of the relevant intermediary (for example Article 5, paragraph 3 (a): "regulatory, accounting or internal or external reporting"). The question therefore arises whether this large number of different criteria will actually help to achieve legal certainty. **If the final version allowed the listed criteria to be applied without any order of precedence, there would be a danger for the parties to the agreement that a court of law might later arrive at a different conclusion after weighing up the various factors.**<br><br>The parties to the agreement must, however, be in a position to determine the applicable law without expending unreasonable time and effort. This also goes for the collateral provider, who may be required by the laws of the relevant jurisdiction to assume certain responsibilities in order to ensure the provision of collateral is effective. A backup rule should therefore ensure that the applicable law may be determined as unequivocally as possible. **The listed criteria should therefore not be presented without any order of rank and left to the discretion of the courts. Instead, they should apply in a descending order of precedence,** so that the next lower-ranking criterion is considered only if it has not proved possible to determine the place of the relevant intermediary on the basis of the previous criterion on the list. In the event that no branch or office can be identified on the basis of the relevant documents, it would also be conceivable to focus on the place of the intermediary's head office (administrative headquarters), as outlined above under 8 f). | The Association of German Banks (p.7-8) |
| **5(3)(a) :**<br><br>**"regulatory, accounting or internal or external** | This paragraph (a) can be **problematic** because it allows the intermediary to decide unilaterally where to place the account. The intermediary can move the account, even during the time the pledge is in place, and this can frustrate the legitimated expectances of the holder or even third parties. | Spain (p.4) |

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| **reporting purposes"** | | |
| **5(3)(c)** | Paragraph (c) is **misplaced**. If we are not wrong, this paragraph is dealing with situations where there is not an explicit location of the account, but an implicit location. That is, the Convention recognizes the possibility that the court may, in the light of the custody agreement, find that the parties have made a real choice about the location of the account although this is not expressly state in the contract. In this case, one can infer out of the terms of the custody agreement that there is a implicit understanding by the parties about where the account is located. We think that the Convention should allow these implicit agreements, but this must be established in Art. 5.1 or in a specific paragraph, but not in Art. 5.3. Art. 5.3 is dealing with the situation where there is neither explicit nor implicit agreement. | Spain (p.4) |
| **5(3)(d)** | Paragraph (d) has **two problems**: it raises the same risks of paragraph (a) and it overlap in a way with Art. 5. (1) option C (supra). | Spain (p.4) |
| **5(3)(e):**<br><br>**"applicable law"** | Il est proposé de **supprimer le point (e)** de l'article 5(3). La raison est d'une part que la clause de loi applicable est une clause qui souvent résulte d'un rapport de force établi entre parties et il faut donc éviter de lui donner trop d'importance et d'autre part le sous-point (c) couvre les termes mêmes de la convention et donc également la clause de loi applicable.<br><br>It is suggested to delete this provision. Choice of law clause may be imposed by stronger party. One cannot give to much weight to it. Furthermore, sub-paragraph c covers the terms of the custody agreement and thus includes the choice of law clause.<br><br>Paragraph (e) should be **deleted**: it does not offer an objective connecting factor, and it can provoke some confusion in a Convention which object are proprietary rights and where unlimited autonomy of the parties to locate the account is rejected. | Luxembourg (p.3)<br>Spain (p.4) |
| **6 in general** | Also compare Art. 6 with Articles 21 and 24 of EU Regulation on reorganisation and winding up of credit institutions; see also Danish comments under "in general" | Ulrik Rammeskow Bang-Pedersen / Denmark |
| | The intended operation of Article 6-in particular its interaction with Articles 4 and 9, requires **clarification**. The prospect of PRIMA law overriding domestic insolvency laws could give rise to sensitivities. Accordingly, Australia may wish to seek a **reservation** on the Article 6 insolvency exception. In particular, the following points may be not be sufficiently clear when reading the current draft:<br><br>Article 6(2) purports to preserve the application of some aspects of insolvency laws, in particular the ranking of claims, the avoidance of transactions and the enforcement of property rights. **Is it sufficiently clear that these particular aspects are not in the** | Australia (p.3) |

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| | **nature of "proprietary rights" that article 6(1) says are not affected by insolvency laws?**<br>If it is correct to assume insolvency laws per se do not affect proprietary rights in indirectly held securities then **is article 6(1) needed at all**, in light of article 4?<br>Article 6(1) does not express **what state's insolvency laws are referred to**. Are they the PRIMA state's insolvency laws or a non-PRIMA state's insolvency laws? Is there still a problem with forum shopping where a relevant party is insolvent?<br>Is Article 6(2) to be read **subject to Article 9**, so that even the types of insolvency laws referred to are overridden by PRIMA law unless the PRIMA law is mandatory contrary to public policy? Is this the intended operation, or was Art 6(2) supposed to 'save' at least those elements of domestic insolvency laws? | |
| | In other comments on the Convention we have expressed our **disagreement** with Art. 6 as it is now. We suggest two alternatives to this article.<br><br>**<u>Version A</u>**<br>"(1) The opening of an insolvency proceeding in a foreign State shall not affect the proprietary rights of creditors or third parties in respect of an account right, constituted and perfected in accordance with the law of the place of the relevant intermediary.<br>(2) Paragraph 1 shall not preclude any action for voidness, voidability or unenforceability which may be taken to set aside acquisitions or dispositions of an account right under the law of the relevant intermediary."<br><br>**<u>Version B</u>**<br>"The effects of insolvency proceedings in a foreign State on the proprietary rights constituted and perfected in accordance with the law of the place of the relevant intermediary shall be governed solely by the law of the place of that relevant intermediary."<br><br><u>Version A</u> is the rule of the **European Regulation**: the opening of an insolvency proceeding in a State *shall not affect* the rights in rem in respect of assets located in another State (Art. 5 of the Regulation), nevertheless detrimental acts can be voided according to the *lex rei sitae* (art. 13 of the Regulation). <u>Version B</u> is the rule **favoured by most of insolvency experts**: the opening of an insolvency proceeding in a State *shall affect* the rights in rem in respect of assets located in another State, *but the effects are governed by the lex rei sitae*. That is, all relevant rules on insolvency of the *lex rei sitae* apply (not only those rules referring to detrimental acts, as in version A). See nº 92 of the Explanatory Report to the European Regulation. | Spain (p.5) |
| | We consider the interrelation between the law identified by the proposed Convention and the | Switzerland (p.2) |

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| | *lex concursus* an **exceedingly important** aspect of the project and suggest that the possible impact of the various versions of Article 6 that have been discussed so far be studied further. | |
| | We have several suggestions to clarify this article. (Also the July draft used the older term "indirectly held securities" rather than the current defined term "**securities held with an intermediary"):**<br>(1) The opening of an insolvency proceeding shall not affect the validity of ~~proprietary~~ property rights in respect of securities held with an intermediary [indirectly held securities] that have been constituted and perfected in accordance with the law of the place of the relevant intermediary.<br>(2) Nothing in this Article affects the application of:<br>(a) any rules of insolvency law relating to the ~~[~~ranking of categories of claim or to the~~]~~ avoidance of a disposition ~~transaction~~ as a preference or a transfer in fraud of creditors; or<br>(b) any rule~~s~~ of insolvency procedure relating to the enforcement of rights to property that ~~which~~ is under the control or supervision of an insolvency administrator. | USA (p.7) |
| **6(1)** | The wording of paragraph 1 is **now clearer** than before. | Finland (p.4) |
| **6(1) (F)** | A l'article 6(1) la référence aux "titres intermédiés" devrait être remplacée par une référence à des "titres détenus auprès d'un intermédiaire". | Luxembourg (p.3) |
| **6(1) :**<br>**"time factor"** | La clause en question ne couvre pour l'instant pas l'élément temporel du transfert et il est **proposé de clarifier que la validité d'un droit réel n'est pas affectée dans la mesure où ce droit a été constitué avant l'ouverture d'une procédure d'insolvabilité.**<br>Time factor needed: provision has to specify that the validity of a proprietary right is not affected if it has been established before the opening of the insolvency procedure. | Luxembourg (p.3) |
| **6(2)** | On paragraph 2, see our March 2001 comments on Article 6 (p.7). The Convention should not interfere with local insolvency laws. Additionally, we share the concern on the possible disharmony with the EU Insolvency Regulation. As a solution, **we share the view of deleting paragraph 2 altogether.** | Finland (p.4) |
| **6(2)(a):**<br>**"ranking of categories or claim"** | The bracketed phrase in Art 6(2)(a) should be **retained**. | USA (p.7) |
| | Recommend the inclusion if these words (which are currently in square brackets) | ISDA (p.6) |

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| **7** | We appreciate the changed wording here. | Finland (p.4) |
| **9 (title) F** | Why keep the words "lois d'application immédiate" in the title if they do not appear in the text of the provision? | Prof. Bucher (CH) |
| **9 (in general)** | At present there are mandatory perfection requirements for charges in Australia that conflict with Article 9(2) of the July Draft. Consequently, Australia would need to be afforded the opportunity to make a **reservation** to Article 9(2). That being said, Australia may consider the trend in some other countries with similar legal regimes to remove such mandatory perfection requirements for securities held through intermediaries. | Australia (p.4) |
| **9 (in general)** | The exclusion of perfection and priority rules should apply to the public policy clause as well as the mandatory rules clause, as follows:<br>"(1) The application of the law designated by the provisions of this Convention may be refused only if its application would be manifestly contrary to the public policy of the forum, other than policy relating to requirements with respect to perfection or relating to priorities, in relation to matters dealt with in this Convention.<br>(2) This Convention does not prevent the application of those provisions of the law of the forum which, irrespective of rules of conflict of laws, must be applied even to international situations, other than any provision imposing requirements with respect to perfection or relating to priorities." | USA (p.7) |
| **9 (in general)** | We appreciate the new language of the public policy clause. | Finland (p.5) |
| **9(1)** | Why limit the reference to the public policy of the *forum*? | Prof. Bucher (CH) |
| | Amendment suggested by Permanent Bureau in the comments on 9(1) is approved: **only *effects*** of application are to be taken into consideration. | Finland (p.5)<br>Greece (p.3)<br>Luxembourg (p.3) |
| **9(1):**<br>**"effects of application of the designated law"** | See our March 2001 comments. | Finland (p.5) |
| **9(2) E+F** | Why use the word "effects" in the E text and not "results" like in the F text? | Prof. Bucher (CH) |
| | Le mot « même » est superflu. | Prof. Bucher (CH) |

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| **10:**<br><br>**Federal clause** | We have been informed that the Permanent Bureau intends setting up a subcommittee of interested member states to work on appropriate language. We would welcome this initiative and would be happy to participate in such a subcommittee. | Australia (p.4) |
| | Option B preferred | Greece (p.3) |
| **10:**<br><br>**Federal clause** | The United States delegation has a keen interest in the "Federal" clauses. Given the subject matter of the Convention, the issues raised by the Federal clauses have greater relevance than they might in other Hague Conventions. That may necessitate refinements to prior formulations of the Federal clauses.<br>We are pleased that the July 2001 draft includes, as Option B, the draft we had previously suggested on the issue of conflicts among the units of a multi-unit state. This is a **critical issue**. The issue is important not only for multi-unit states such as the United States. Rather, the issue is important to all other States and all parties engaged in transnational securities transactions, because in any case where the rules of Article 5 identify the place of the relevant intermediary as a place within a multi-unit State, the parties must be able to determine what rules govern the selection among the laws of such units. We do not think that Option A will work, because it neither deals with the situation of non-territorial units, such as federal versus state law in the US, nor does it adequately identify the rules that other States are to apply to conflicts among the laws of a multi-unit State. Our earlier draft (Option B) was intended to deal with those issues.<br>On further reflection, we think that our earlier draft could be improved. One objective is to make the relationship between Articles 4/5 and Article 10 clearer. The basic concept is that Articles 4 and 5 deal only with identification of the law of the State, e.g. The United States of America. If the Article 5 rules on place of the relevant intermediary point to place, e.g. New York City or Boston, that is located within The United States of America, then Article 4 tells us only that the applicable law is the law of The United States of America. Since The United States of America comprises multiple units, one should look to Article 10 to decide which units' law applies. To make this point clearer, we suggest adding the phrase "of the State" in Article 1 and Article 4, as noted above.<br>In addition to the possibility of having to select the laws of the different States of the United States, there is a likelihood in most cases of applying the Uniform Commercial Code as adopted by a particular State of the United States, which itself has conflict of laws rules that contradict the conflict of laws rules that would otherwise apply in that State. Moreover, Federal law and Federal conflict of laws rules apply in certain cases.<br>Next, we suggest the following revision of our prior suggested text for Article 10:<br>The following rules apply if the place of the relevant intermediary, determined under Article 5, is located in a State within which the State and one or more of its territorial or other units have | USA (cover-letter and comments p.7-9) |

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| | their own substantive rules of law or conflict of laws rules in respect of any matter dealt with in this Convention ("Multi-unit State"):<br>(1) If a court in another State must decide a conflict of laws issue within a Multi-unit State, it shall do so under the following rules:<br>(2) (a) If the Multi-unit State has made a declaration identifying the conflict of laws rules applicable within the Multi-unit State, the other State shall apply those rules.<br>(b) If the Multi-unit State has not made such a declaration, the other State shall apply the Convention to conflict of laws issues within that Multi-unit State.<br>(2) The Convention does not displace the conflict of laws rules applicable within a Multi-unit State to conflict of laws issues within that Multi-unit State. | |
| **11** | Endorse the current draft | ISDA (p.6) |
| **14 and 15** | We suggest that it might be clearer **if Article 14 dealt only with States, and Article 15 covered all issues concerning regional organizations**. While we do not have an objection in principle, we have *not yet* formulated a position on the role of regional organizations, because it will be necessary to test the draft provisions of the draft Convention to determine whether there would be any difference in implementation if done through an organization acting as a party to the Convention rather than an individual State acting as party to the Convention. We do note, however, that if regional organizations are included, it may not be wise to limit this to regional *economic integration* organizations. | USA (p.9) |
| **15** | See Danish comments under "in general" | Ulrik Rammeskow Bang-Pedersen / Denmark |
| **18** | Endorses principle of such a provision. | Czech Republic (p.1) |
| | Since a State's denunciation could have a significant impact on prior transactions and relations, **we believe that a longer lead time should be required to enable parties to make adjustments. We suggest a minimum of six months for effectiveness of a denunciation**. | USA (p.9) |
| **19:**<br><br>**Other final clauses** | There needs to be a provision on conflicting instruments | Czech Republic (p.1) [See also Ulrik Rammeskow Bang-Pedersen / Denmark (p.4)] |

# ANNEX: PROPOSALS SUBMITTED RE ARTICLE 5

## *AUSTRALIA*

**Proposal 1** (based on Option A in the July Draft):

"For the purposes of this Convention, the securities account is maintained at the place of the office or branch of the relevant intermediary agreed between the account holder and the relevant intermediary, provided that the relevant intermediary's [business][operations] of maintaining securities accounts [is][are] subject to regulatory [supervision] [oversight] in the place so agreed and the maintenance of that securities account forms part of the intermediary's business in that place."

**Proposal 2** (based on Option B in the July Draft):

"For the purposes of this Convention, the securities account is maintained at the place of the office or branch of the relevant intermediary agreed between the account holder and the relevant intermediary, provided that the relevant intermediary's [business][operations] of maintaining securities accounts is subject to regulatory [supervision] [oversight] in the place so agreed."

**Proposal 3** (based on Option C in the July Draft):

"For the purposes of this Convention, a certificate issued by the relevant intermediary as to the place where the securities account is maintained is conclusive, provided that the relevant intermediary's [business][operations] of maintaining securities accounts [is][are] subject to regulatory [supervision] [oversight] in the place so agreed and the maintenance of the securities account in question forms part of [that business][those operations] in that place."

**Proposal 4** (based on Option C in the July Draft):

"For the purposes of this Convention, a certificate issued by the relevant intermediary as to the place where the securities account is maintained is conclusive, provided that the relevant intermediary's [business][operations] of maintaining securities accounts is subject to regulatory [supervision] [oversight] in the place so agreed."

## *GERMANY*

(1) The place of the relevant intermediary is determined by the office maintaining the account for the recipient of the disposition (transferee/pledgee) and effecting the crediting for the recipient's benefit so as to establish the latter's title.

(2) The office maintaining the account for the recipient of the disposition is determined:

a) by the account number and bank code assigned to the securities account of the recipient of the disposition,
b) alternatively by the head office of the institution specified in the contract opening the securities account.

## *LUXEMBOURG*

(1) Le lieu de situation de l'intermédiaire pertinent est le lieu où le compte de titres du titulaire de compte auprès de cet intermédiaire est tenu.

(2) Le compte de titres est tenu au lieu désigné par l'intermédiaire pertinent dans une attestation ou au lieu convenu entre le titulaire de compte et l'intermédiaire pertinent, pour autant que l'intermédiaire pertinent ait au lieu désigné ou convenu un établissement ou une succursale.

* * *

(1) The place of the relevant intermediary is the place where the securities account of the account holder is maintained.

(2) The securities account is maintained at the place designated by the relevant intermediary in a certificate or at the place agreed between the account holder and the relevant intermediary, provided that the relevant intermediary maintains an office or branch at the designated or agreed place.

## *USA*

***(place of the relevant intermediary)***

The place of the relevant intermediary is the place of the office or branch of the relevant intermediary agreed between the account holder and the intermediary, provided that the intermediary's business of maintaining securities accounts is subject to supervisory oversight in the place so agreed ~~it is a place where the intermediary is subject to regulatory supervision.~~

***(protection of third parties)***

A certification or representation by the relevant intermediary stating that a particular branch or office is the place of the relevant intermediary under Article 5(x) [whatever section contains the agreement/nexus test] is conclusive in favour of a person other than the intermediary.

***(existing documentation)***

If an account agreement is entered into before the date two years after the effective date of this Convention and does not otherwise identify the location of the office or branch that maintains the account:

(1) a clause in the account agreement selecting the governing law shall be treated as an agreement that the account is maintained at a branch or office in the jurisdiction whose law is selected; and

(2) an identification of the intermediary as a particular branch or office, or other indication in the account agreement that the intermediary is acting by or through a particular branch or office, shall be treated as an agreement that the account is maintained at that branch or office.

**Article 5 Determination of the place of the relevant intermediary**

**(1) The place of the relevant intermediary is the place where the securities account with that intermediary is maintained.**

**(2)(a) For the purposes of this Convention, the securities account is maintained at the place of the office or branch (or other form of legal presence) of the relevant intermediary agreed in writing between the account holder and the intermediary, provided that it is a place where the intermediary is authorized to do business, or where the intermediary is supervised, by a local regulatory authority.**

**COMMENT #1**: The *account holder and the intermediary can agree on the place where the account is maintained. The parenthetical reference to other forms of legal presence is intended to incorporate evolving concepts of where an intermediary is located as electronic commerce, including internet-based banking, become more common.*

**COMMENT #2**: The *limitations on the ability of the account holder and the intermediary to agree on the place are that the place selected must (i) be the place of an office or branch (or other form of legal presence) of the intermediary, and (ii) be a place where the intermediary is either authorized to do business by a local regulatory authority, or supervised by a local regulatory authority. The intent of this provision is to require that the intermediary have sufficient legal nexus to, and presence in, the place selected so that the intermediary would be subject to the jurisdiction of the local courts in litigation to enforce the rights of persons claiming an interest in the account.*

**COMMENT #3:** We *intend that, if a court holds that the agreement concerning the place of the account is invalid because the place selected does not meet the requirements of Article 5(2)(a), or for any other reason, the selection of that place is still valid (with respect to rights that arose prior to the court's decision) as between the account holder and the intermediary. However, if one of these parties entered into the agreement regarding the selection of the place in bad faith, the place selection should be voidable at the option of the innocent party.*[*]

**(b) If the intermediary and the account holder have agreed as to the place of the office or branch of the relevant intermediary as set forth in Article 5(2)(a), the intermediary may issue a notice ("Notice of Agreement" or "NOA") stating the place of such office or branch (or other form of legal presence). In determining the rights of any person who receives an NOA from the relevant intermediary and acts in reliance thereon, the account shall be deemed conclusively to be maintained at the place specified in the NOA.**

**COMMENT:** *The purpose of an NOA is to provide evidence upon which a third party can rely concerning the selection of an account location in the agreement between the intermediary and the account holder. By receiving an NOA, a third party avoids the need to review a copy of the agreement itself. An NOA is only conclusive as to the rights of a third party if that third party has received the NOA directly from the intermediary. That is, NOAs, or copies of NOAs, that are received from some other source (e.g., the account holder) do not have conclusive legal effect.*

**(c) (i) If an account holder and an intermediary agree as to the place of the office or branch (or other form of legal presence) at which the account is maintained, and the intermediary subsequently ceases to maintain an office or branch (or other form of legal presence) in such place, or the intermediary ceases to be authorized to do business, or to be supervised, by a local regulatory authority in such place, the account shall continue to be deemed to be maintained at the place specified in the agreement unless and until the account holder and the intermediary agree otherwise.**

**COMMENT:** *This provision preserves the effect of an agreement as to the place of the relevant office or branch that was valid when made, but subsequently becomes invalid. The parties should be afforded ample time to amend their agreement without jeopardizing rights based on the prior agreement.*

**(ii) A change in the agreement between the intermediary and the account holder as to the place of the office or branch (or other form of legal presence) at which the securities account is maintained shall have no effect on the rights of any person who has received an NOA from the intermediary pursuant to the prior agreement unless and until a reasonable period of time after such person has received actual notice of such change.**

**COMMENT#1:** This *provision preserves the rights of third parties who have not received notice of a change in the agreement between the account holder and the intermediary with respect to the place of the relevant office or branch. A change in the place of the account is not effective as to such a person until it has received actual notice of the change and has had a reasonable period of time to perfect its rights in the account or to otherwise protect its interests in light of the change. Invalidity of the selection of a place in the agreement between the intermediary and the account holder (e.g., as a result of a judicial holding that the place selected is inconsistent with Article 5(2)(a), or of a change in circumstances, such as the intermediary's ceasing to maintain an office or branch or other form of legal presence in that place) will not effect the rights of a third party who has received an NOA from the intermediary, except to the extent that, as a result of such invalidity, the parties amend the agreement and give notice of such amendment to the third party.*

**COMMENT #2:** We *intend that, unless the successors expressly agree otherwise, an agreement between an account holder and an intermediary as to the place at which the account is maintained shall be binding as between a successor in interest to either the intermediary or the account holder, or both, to the same extent as between the original parties to the agreement.**

**(3)(a)** **If the relevant intermediary and the account holder have not agreed as to the place of the office or branch of the relevant intermediary as set forth in Article 5(2)(a), the intermediary may issue a certificate ("Certificate of Place" or "COP") designating the place of such office or branch (or other form of legal presence), provided that it is a place where the intermediary is authorized to do business, or where the intermediary is supervised, by a local regulatory authority.**

**COMMENT #1:** This *provision provides a mechanism by which an intermediary can address the situation in which its agreement with an account holder does not specify the place of the relevant office or branch. A COP could be issued in the case of a custody agreement entered into prior to the adoption of the Convention, in the case of a post-Convention agreement that is silent with respect to the place of the relevant office or branch, or in the case of an agreement that contains a place selection that is invalid under Article 5(2). In these situations, the intermediary could designate the place of the relevant office or branch (or other form of legal presence) by issuing a COP. The intermediary's ability to designate a place would be limited by the same nexus requirements as limit the ability of the intermediary and an account holder to agree on a place.*

**COMMENT #2:** We *intend that, if the relevant intermediary has issued a COP as set forth in Article 5(3)(a), the place designated therein is conclusive as between the intermediary and the account holder, unless the COP is contrary to the place selected in an agreement between the intermediary and the account holder in accordance with Article 5(2)(a). We also intend that a COP is conclusive with respect to the rights of a person (other than the account holder) who receives the COP directly from the intermediary and acts in reliance thereon.**

**COMMENT #3:** We *intend that, unless the successors expressly agree otherwise, a COP shall continue to be effective as between a successor in interest to either the intermediary or the account holder, or both, to the same extent as between the original parties to the agreement.**

**COMMENT #4:** We *intend that, if a court holds that the place designated in the COP is invalid for any reason, the designation of that place is still valid as between the account holder and the intermediary, unless it can be shown that the intermediary acted in bad faith in designating such place or in issuing the COP. In that event, the place designation should be voidable at the option of the account holder.**

**(b)** **In determining the rights of any person who receives a COP (or a copy thereof) from the relevant intermediary and acts in reliance thereon, the account shall be deemed conclusively to be maintained at the place specified in the COP.**

**COMMENT:** *A COP is only conclusive as to the rights of a third party if that third party has received the COP (or a copy) directly from the intermediary. That is, COPs, or copies of COPs, that are received from some other source (e.g., the account holder) do not have conclusive legal effect.*

**(c)** **(i)** **If the relevant intermediary has issued a COP designating the place at which a securities account is maintained, and the intermediary subsequently ceases to maintain an office or branch (or other form of legal presence) in such place, or the intermediary ceases to be authorized to do business, or to be supervised, by a local regulatory authority in such place, the**

**account shall continue to be deemed to be maintained at the place specified in the COP unless and until the intermediary rescinds the COP in writing.**

**COMMENT:** *This provision preserves the effect of a COP that was valid when issued, but subsequently becomes invalid. The intermediary should be afforded ample time to issue a new COP without jeopardizing rights based on the prior designation.*

**(ii) The rescission of a COP shall have no effect on the rights of any person who has received the COP (or a copy thereof) from the intermediary unless and until a reasonable period of time after such person has received actual notice of such rescission.**

**COMMENT:** *This provision preserves the rights of third parties who have not received notice of the rescission of a COP. We intend that third parties should be able to rely on a COP in determining or perfecting their rights without having to perform additional due diligence concerning the validity of the COP. The intermediary and the account holder should have the burden of informing third parties of the rescission of a COP. The rescission of a COP is not effective as to a third party until it has received actual notice of the change and has had a reasonable period to protect its interests in light of the rescission. Invalidity of the designation of a place in a COP (e.g., as a result of a judicial holding that the place designated is inconsistent with Article 5(3)(a), or of a change in circumstances, such as the intermediary's ceasing to maintain an office or branch in that place) will not effect the rights of a third party who has received the COP from the intermediary, except to the extent that, as a result of such invalidity, the intermediary rescinds the COP and gives notice of such rescission to the third party.*

**(4)(a) If the place of the relevant intermediary cannot be determined under paragraphs (2) or (3) of this Article 5, the factors that may be considered in determining the place of the relevant intermediary include the following:**

**(i) the location of the office or branch (or other form of legal presence) where the relevant intermediary treats the securities account as being maintained for regulatory, accounting or internal or external reporting purposes;**

**(ii) the location of any office or branch (or other form of legal presence) of the relevant intermediary with which the account holder deals;**

**(iii) the terms of the custody agreement, account agreement or any other agreement relating to the securities account between the relevant intermediary and the account holder;**

**(iv) the terms of account statements or other reports prepared by the relevant intermediary that reflect the balance of the account holder's interest in the securities account; and**

**(v) the State whose law governs the agreement establishing the securities account.**

**(b) In applying the provisions of this paragraph, no account shall be taken of the following factors:**

**(i) the places where certificates representing or evidencing securities are located;**

**(ii) the places where any register of holders of securities maintained by or on behalf of the issuer of the securities is located;**

**(iii) the place where the issuer of the securities is organized or incorporated or has its statutory seat, central administration, principal place of business or its registered office;**

**(iv) the place where any intermediary other than the relevant intermediary is located; or**

**(v) the places where the technology supporting the bookkeeping or data processing for the securities account is located.**

**COMMENT:** *In the event that the intermediary and the account holder have not entered into an agreement with respect to the place of the relevant office or branch and the intermediary has not issued a COP, the place of the relevant office or branch would be determined by application of the factors in Article 5(4). We assume that the need to resort to these factors would arise only rarely.*

## *ISDA*

(2 alternative proposals; please note that each of these proposals, while favoured by some members of ISDA, remains under study by others.)

**Proposal 1**

Development of the various options set out under the "account approach" in the annotated July 2001 draft:

(1) The place of the relevant intermediary is the place where the securities account with that intermediary is maintained.

(2) For the purposes of this Convention, the securities account is maintained at the place of the office or branch of the relevant intermediary agreed between the account holder and the intermediary, provided that the [intermediary/intermediary's business] is subject to [regulation][regulatory supervision] in the place so agreed and that the maintenance of that securities account forms part of the intermediary's business in that place.

(3) If the place of the securities account cannot for any reason be determined under paragraph 2, a certificate issued by the relevant intermediary as to the place where the securities account is maintained is conclusive, provided that the relevant intermediary's business is subject to [regulation][regulatory supervision] in the place so agreed and that the maintenance of that securities account forms part of that business in that place.

(4) If the place of the securities account cannot for any reason be determined under paragraphs 2 or 3, then the factors that may be considered in determining that place including the following:

[The text of sub-paragraphs (a) to (e) of Paragraph (3) of the annotated July draft to be inserted here]

(5) [The text of Paragraph (4) of the annotated July draft to be inserted here]

Paragraph (2), as in the case of Options A and B under "account approach" in the annotated July 2001 draft of the Convention, relies on the agreement between the account holder and the intermediary to determine the location of the account. The proviso to Option A, however, relies on the idea that the "maintenance of the securities account" is subject to regulatory supervision. Some ISDA members felt that it is the intermediary or the business of the intermediary that is subject to regulatory supervision (or regulation - as indicated above, there was some discussion of which is the more accurate term) rather than the maintenance, per se, of securities accounts. Also, some ISDA members felt that the proviso to Option A does not necessarily ensure that the relevant securities account is actually located in the jurisdiction agreed between the account holder and the intermediary. (Other ISDA members, as noted above, consistently questioned whether it is possible to say that a securities account is "actually located" anywhere.)

We understand that those who believe that some sort of constraint or “reality check” (in the words of your commentary) should be imposed on the agreement between the account holder and the intermediary do not currently believe that the proviso to Option B under “account approach” in the annotated July 2001 draft of the Convention is sufficient. On the other hand, those who believe strongly in the value of *ex ante* certainty are not entirely comfortable with the level of due diligence that may be necessary to match an account with a particular part of an intermediary’s business, as may be required by Proposal 1.

ISDA's first proposal attempts to deal with these concerns by focusing the proviso on the regulatory supervision (or regulation) of the intermediary's business, which seems to be a broadly acceptable formulation, while at the same time expressly tying the maintenance of the relevant securities account to the business of the intermediary regulated in that place.

We recognise that our formulation may reflect a trade-off between the fundamental objective of achieving ex ante certainty and the objective of making the formulation compatible with a broad range of legal traditions, including those with a commitment to the *lex rei sitae* principle. We believe, however, that it may represent an acceptable trade-off between these two worthy goals, subject to further discussion and study.

In relation to pre-existing account or custody agreements, we believe that "agreed" does not necessarily need to be read as an explicit reference to the location of an account in the account or custody agreement between the account holder and the intermediary. The agreement may be implicit, but nonetheless ascertainable on the basis of verifiable facts. Some of those facts may well be instances of the factors set out in sub-paragraphs (a) to (e) to Paragraph (3) the annotated July 2001 draft of the Convention. But other facts may also help establish the actual agreement of the parties in relation to the location of the account. An interpretative rule in relation to this point, as suggested in the commentary accompanying the July draft, is deserving of further consideration. As noted above, the ideal is to produce a rule that provides legal certainty for existing agreements without onerous due diligence or amendment.

Paragraph (3), which is a version of Option C under the "account approach", is another way of establishing ex ante certainty should Paragraph (2) fail to produce a clear result. The proviso is designed to prevent the intermediary from certifying an arbitrary location of the securities account and to permit a reading of the provision consistent with a more traditional approach to the *lex rei sitae* rule. The fact that the intermediary is a regulated institution should provide further comfort that it may not act in an arbitrary manner in relation to this certification.

As can be seen, we endorse the "cascade" approach of the annotated July 2001 draft of the Convention and agree that the remaining Paragraphs (numbered (4) and (5) in our first proposal) should only need to deal with a small number of cases.

**Proposal 2**

Our second proposal follows the text of our first proposal, except that Paragraph (2) is amended to read in its entirety as follows:

(2) For purposes of this Convention, the securities account is maintained at the place of the office or branch of the relevant securities intermediary agreed between the account holder and the intermediary, provided that the intermediary is subject to, covenants to comply with, or does comply with, the duties of an intermediary with respect to the securities account and the account holder imposed by the laws of that place on intermediaries in the business of maintaining securities accounts in that place.

This alternative version of Paragraph 2 prevents an agreement as to the account location from being effective for purposes of the Convention unless the intermediary acts or agrees to act in a way that is consistent with that agreement. For example, if the law of the agreed upon location requires intermediaries to have enough securities to satisfy the claims of all customers, to pass on the benefits of ownership to customers, or to record or report changes to the account in accordance with certain custody accounting rules, the intermediary would be required to comply or agree to comply with those requirements; otherwise, the agreement would not be determinative for purposes of the Convention. This approach may be superior to Proposal 1 in that it may impose a more potent constraint on the intermediary’s behaviour, without undermining the goal of ex ante certainty.