

Novembre/November 2001

**PROPOSITION DE DISPOSITIONS-CLÉS POUR UNE FUTURE CONVENTION
SUR LA LOI APPLICABLE À CERTAINS DROITS
SUR DES TITRES DÉTENUS AUPRÈS D'UN INTERMÉDIAIRE**

Propositions de nouvel amendement au texte contenu dans
le Document préliminaire No 3 de juillet 2001 (« projet annoté de juillet 2001 »)

soumis par le Bureau Permanent

(à désigner « projet de novembre 2001 »)

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**TENTATIVE TEXT ON KEY PROVISIONS FOR A FUTURE CONVENTION
ON THE LAW APPLICABLE TO CERTAIN RIGHTS
IN RESPECT OF SECURITIES HELD WITH AN INTERMEDIARY**

Suggestions for further amendment of the text contained in
Preliminary Document No 3 of July 2001 ("annotated July 2001 draft")

submitted by the Permanent Bureau

(to be referred to as the "November 2001 draft")

*Document préliminaire No 6 de novembre 2001
à l'intention de la Commission spéciale de janvier 2002*

*Preliminary Document No 6 of November 2001
for the attention of the Special Commission of January 2002*

BRIEF EXPLANATIONS

In the **title**, the reference to “proprietary” rights has been removed and replaced by the more general expression “certain” rights. This change is intended to reflect more adequately the fact that the law designated by PRIMA will not only apply if the rights resulting from the credit of securities to a securities account are *property* rights, but also if they are contractual or of any other nature. Hence, PRIMA will be the law to look at when determining the legal nature of an investor’s rights vis-à-vis its intermediary. This clarification is made explicit in **Article 2(1)(a)**. The way the Convention operates is, therefore, as follows: The law designated by PRIMA will determine whether the investor’s rights are property, contractual or other rights. If the rights are contractual, the Convention has at this point of time no further effect and the normal Private International Law rules on contractual obligations apply; however, if the investor’s contractual rights are then transferred or granted as a security interest to another party, the law designated by PRIMA will also determine the property rights resulting from such a disposition. The law designated by PRIMA will indeed apply to property rights resulting from any disposition of securities held with an intermediary. All the issues covered by the PRIMA law are enumerated in an exhaustive list contained in Article 2(1)(a)-(g). Sub-paragraph (g) appears in brackets, as it is still open whether the pledge of securities held with an intermediary extends to income, dividends and sale or redemption proceeds that are credited to a securities account. As Article 2 is a very important provision, comments on these various issues would be particularly welcome.

The new language in **Article 1(4)** is not intended to introduce any substantive change, but merely to express more clearly the underlying idea of the provision, which is to exclude a direct holding pattern that is particularly common in Nordic States from the Convention’s scope of application.

Article 4 is the core provision of the new draft. It states in paragraph 1 the PRIMA principle. Paragraph 2 has merged into one provision the “account” and “branch/office” approaches suggested in the “annotated July 2001 draft”. This is an important change, as the new provision establishes a significant reality test to localise the intermediary: the place of the relevant intermediary can only be a place where the latter has an office or branch. Paragraph (3) contains **6 different options** on how to determine the place of this office or branch.

Options A to E are all based on the idea that the account holder and the intermediary can **agree** on the place of the intermediary’s office or branch maintaining the securities account. At the outset, one has to stress that under all Options A to E, such an agreement is subject to the reality test contained in paragraph 2 (*i.e.*, the intermediary must have an office or a branch at the place agreed between the parties).

?? In **Option A**, the necessity for the intermediary to have an office or branch at the place agreed is the *only* qualification to the agreement between the account holder and the intermediary.

?? In the **Options B to E** different language is suggested to express an *additional* reality test that has to be fulfilled:

- In **Option B**, the *intermediary itself* has to be subject to supervisory oversight.

- In **Option C**, the relevant intermediary's *maintenance of the securities account* has to be subject to supervisory oversight.
- In **Option D**, relevant intermediary's *business of maintaining securities accounts* has to be subject to supervisory oversight.
- Finally, in **Option E**, the relevant intermediary has to be *subject to* or to *agree to comply with duties imposed by the laws of that place on intermediaries maintaining securities accounts in that place*.

?? All the **Options A to E** suggest, in square brackets, a **first fall-back rule**: in the absence of an agreement between the account holder and the relevant intermediary on the place of the relevant intermediary's office or branch maintaining the account, the relevant intermediary may issue a **certificate** attesting the place of this office or branch.

?? **Option F** is based on a **purely objective approach**: the place of the relevant intermediary is identified by the account number and bank code or, if there is no such code, any other identification code, assigned to the securities account. If there is no place so identified, the place of the relevant intermediary is the place of its head office. Here again, the reality test embodied in paragraph 2 remains applicable.

With a view to prepare as effectively as possible the January meeting and to reduce the number of Options to be discussed, the Permanent Bureau would be most grateful if Member States and observers could indicate **which of the Options contained in Article 4(3) they prefer, which Options they could also accept, and which Options they clearly reject**. As the key provision in the proposed Convention, it is crucial that we find one or more solutions that are acceptable in all legal systems if we are to achieve our goal in January 2002.

Article 4(4) is intended to protect all parties other than the relevant intermediary who rely on information contained in a certificate issued or representation made by the relevant intermediary with regard to the proviso on "supervisory oversight" contained in Options B, C, D or E (Options A and F are not mentioned in the bracket because they have no such proviso). According to this provision, any party is enabled to assume that the information contained in the **certificate or representation** is accurate. The provision appears in brackets, as the principle of such a rule has never been discussed by the Plenary.

It is important to note that Article 4(4) does not relate to the entire paragraph of Options B, C, D or E, but only to the *proviso* contained therein. It has, however, also been suggested that the relevant intermediary might issue a **Notification of Agreement (NoA)** stating the place of its office or branch maintaining the securities account. Such a NoA would therefore only relate to the text *preceding* the proviso. The main practical advantage of such a NoA is that it would allow parties to a custody agreement relating to a securities account to be able to inform secured creditors and other interested parties of the place of the relevant intermediary without having to make available the full custody agreement. Again, comments on this issue would be particularly helpful.

For a detailed comment on **Articles 9 (Federal State extension clause) and 10 (Federal State interpretation clause on applicable law)**, see Preliminary document No 4. Both Options of Article 10 are based on the same approach: if, as a result of

Article 4, the applicable law is the law of a State which comprises several territorial units and in which there are rules identifying which law or set of rules of law is applicable, that law or set of rules of law applies. The difference between the two Options is that in Option A the approach follows directly from Article 10, whereas in Option B, the State has to make a declaration to that effect.

Article 17 is a transitional rule and addresses the issue whether the Convention applies in a Contracting State to dispositions concluded *before* the entry into force of the Convention for that State (**existing documentation**). The provision appears in brackets, as it has never been discussed by the Plenary. Also, it goes without saying that the final text of this provision is subject to the ultimate wording of Article 4. The suggested draft of Article 17 is based on a proposal made by the United States (see accompanying chart); contrary to that proposal, however, the text suggested in Article 17 is not based on a declaration mechanism. Paragraph 2(c) (i) and (ii) have been put in brackets, as these provisions are particularly sensitive in this context.

The Permanent Bureau avails itself of this opportunity to thank the Member States and observers again for their extremely valuable and effective assistance. We apologise again for the short time-frame resulting from the "fast-track procedure" adopted for this project.

The Hague, 12 November 2001

Christophe Bernasconi
Richard Potok

Article 1 Definitions and interpretation**(1) In this Convention –**

“securities” means any shares, bonds or other financial assets or instruments, or any interest therein;

“intermediary” means a person that in the course of business maintains securities accounts either for others or for its own account and is acting in that capacity;

“relevant intermediary” means the intermediary with whom the account holder maintains the securities account;

“securities account” means an account with an intermediary to which securities are credited;

“securities held with an intermediary” means the rights of an account holder resulting from a credit of securities to a securities account, whether such rights are property, contract, or other rights;

“account holder” means a person in whose name an intermediary maintains a securities account;

“disposition” means any transfer of title whether outright or by way of security and any grant of a security interest whether possessory or non-possessory;

“perfection” means completion of any steps necessary to render a disposition effective against persons who are not parties to that disposition;

“insolvency administrator” means a person, including one appointed on an interim basis, authorised in an insolvency proceeding to administer the reorganization or liquidation of the debtor’s assets or affairs;

“insolvency proceeding” means a collective judicial or administrative proceeding, including an interim proceeding, in which the assets and affairs of the debtor are subject to control or supervision by a court or other competent authority for the purpose of reorganisation or liquidation.

(2) 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 account holder’s intermediary.

- (3) References in this Convention to a disposition of securities held with an intermediary include a disposition of a securities account.**
- (4) A person shall not be considered an intermediary for the purposes of this Convention merely because –**
- (a) it acts as registrar or transfer agent for an issuer of securities; or**
 - (b) it records in its own books details of securities credited to securities accounts maintained by an intermediary in the names of other persons for whom it acts as manager or agent or otherwise in a purely administrative capacity.**

Article 2 Scope of the Convention and of the applicable law

- (1) This Convention determines the law applicable to the following issues in respect of securities held with an intermediary –**
- (a) whether the rights resulting from the credit of securities to a securities account are property, contract, or other rights;**
 - (b) the legal nature of a disposition of securities held with an intermediary, and the property rights resulting from such a disposition;**
 - (c) the requirements, if any, for perfection of a disposition of securities held with an intermediary;**
 - (d) 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 other interest;**
 - (e) the duties, if any, of an intermediary to a person who asserts a competing title to or other interest in securities held with that intermediary;**
 - (f) the steps, if any, required for the realisation of a disposition of securities held with an intermediary; and**
 - [(g) whether a pledge of securities held with an intermediary extends to income, dividends and sale or redemption proceeds that are credited to the securities account.]**
- (2) This Convention does not determine –**

- (a) the contractual rights and duties of parties to a transaction in securities;
- (b) the contractual rights and duties arising from relations between an intermediary and an account holder; or
- (c) the rights and duties of an issuer of securities or of an issuer's registrar or transfer agent.

Article 3 Internationality (territorial scope of application of the Convention)

This Convention applies in all cases involving a choice between the laws of different States.

Article 4 Determination of the applicable law

- (1) The law applicable to the issues specified in paragraph 1 of Article 2 is the law of the place of the relevant intermediary.**
- (2) The place of the relevant intermediary is the place of its office or branch which maintains the securities account.**
- (3) For purposes of this Convention, that place is**

Option A (place agreed [+ certificate])

the place agreed between the account holder and the relevant intermediary [or, in the absence of such agreement, the place certified by the relevant intermediary].

Option B (place agreed [+ certificate] and relevant intermediary subject to supervisory oversight)

the place agreed between the account holder and the relevant intermediary [or, in the absence of such agreement, the place certified by the relevant intermediary], provided that [in either case] the relevant intermediary is subject to supervisory oversight in that place.

Option C (place agreed [+ certificate] and relevant intermediary's maintenance of the securities account subject to supervisory oversight)

the place agreed between the account holder and the relevant intermediary [or, in the absence of such agreement, the place certified by the relevant intermediary], provided [in either case] that the relevant intermediary's maintenance of that securities account is subject to supervisory oversight in that place.

Option D (place agreed [+ certificate] and relevant intermediary's business of maintaining securities accounts is subject to supervisory oversight)

the place agreed between the account holder and the relevant intermediary [or, in the absence of such agreement, the place certified by the relevant intermediary], provided that [in either case] the relevant intermediary's business of maintaining securities accounts is subject to supervisory oversight in that place.

Option E (place agreed [+ certificate] and relevant intermediary subject to or agrees to comply with duties imposed by the laws of that place on intermediaries maintaining securities accounts in that place)

the place agreed between the account holder and the relevant intermediary [or, in the absence of such agreement, the place certified by the relevant intermediary], provided that [in either case] the relevant intermediary is subject to or agrees to comply with the duties of an intermediary with respect to the securities account imposed by the laws of that place on intermediaries maintaining securities accounts in that place.

Option F (place designated by identification number; head office)

the place identified by the account number and bank code or, if there is no such code, any other identification code, assigned to the securities account; or, if there is no place so identified, the place of the head office of the relevant intermediary.

[(4) A certification or representation by the relevant intermediary that the proviso in [Option B, C, D or E] is satisfied is conclusive in favour of a person other than the relevant intermediary.]

(5) If the place of the relevant intermediary cannot be determined under paragraph 3, that place is

Option A (central administration)

the place where the relevant intermediary has its central administration.

Option B (closest connection test)

the place of the office or branch of the relevant intermediary with which the securities account is most closely connected.

[If Option B is retained, the following “black list” should be added:

(6) In applying the provisions of the preceding paragraph, no account shall be taken of the following factors –

- (a) the places where certificates representing or evidencing securities are located;
- (b) the places where any register of holders of securities maintained by or on behalf of the issuer of the securities is located;
- (c) the place where the issuer of the securities is organised or incorporated or has its statutory seat, central administration, principal place of business or its registered office;
- (d) the place where any intermediary other than the relevant intermediary is located; or
- (e) the places where the technology supporting the bookkeeping or data processing for the securities account is located.]

Article 5 Insolvency

(1) The opening of an insolvency proceeding under a law other than the law of the place of the relevant intermediary does not affect a disposition of securities held with an intermediary that has been made and perfected in accordance with the law of the place of the relevant intermediary.

(2) Nothing in this Convention affects the application of –

- (a) any rules of insolvency law relating to the [ranking of categories of claim or to the] avoidance of a disposition as a preference or a transfer in fraud of creditors; or

- (b) any rules of insolvency procedure relating to the enforcement of rights to property which is under the control or supervision of an insolvency administrator.

Article 6 General applicability

This Convention applies whether or not the applicable law is that of a Contracting State.

Article 7 Exclusion of choice of law rules (*renvoi*)

In this Convention, the term “law” means the law in force in a State other than its choice of law rules.

Article 8 Public policy and internationally mandatory rules

- (1) The application of the law designated by the provisions of this Convention may be refused only if the effects of its application would be manifestly contrary to the public policy of the forum.**
- (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.**
- (3) This Article does not permit application of provisions of the law of the forum imposing requirements with respect to perfection or relating to priorities (unless the law of the forum is the law designated by Article 4).**

Article 9 Applicability of Convention in States with more than one legal system

- (1) If a State has two or more territorial units in which different systems of law are applicable in relation to matters dealt with in this Convention, it may at the time of signature, ratification, acceptance, approval or accession declare that the Convention shall extend to all**

its territorial units or only to one or more of them and may modify this declaration by submitting another declaration at any time.

- (2) Any such declaration shall be notified to the depositary and shall state expressly the territorial units to which the Convention applies.
- (3) If a State makes no declaration under this Article, the Convention is to extend to all territorial units of that State.

Article 10 Determination of applicable law in States with more than one legal system

Option A (see Preliminary Document No 4: Memorandum on federal clauses)

Where, under Article 4, the place of the relevant intermediary is located in a State which comprises two or more territorial units each of which has its own system of law or set of rules of law in respect of matters covered by this Convention, the following rules apply –

- (a) if there are rules in force in such a State identifying which law or set of rules of law is applicable, that law or set of rules of law applies;
- (b) in the absence of such rules, any reference in this Convention to the place of the relevant intermediary's office or branch which maintains the securities account shall be construed as referring to the place in a territorial unit.

Option B (see the Annex to Preliminary Document No 4)

The following rules apply if the place of the relevant intermediary, determined under Article 4, is located in a State within which the State and one or more of its territorial or other units have their own substantive rules of law or conflict of laws rules in respect of any matter dealt with in this Convention ("Multi-unit State") –

- (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 –

- (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;
 - (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.
- (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.

Article 11 Uniform interpretation

In the interpretation of the Convention, regard is to be had to its international character and to the need to promote uniformity in its application.

Article 12 Review of practical operation of the Convention

The Secretary General of the Hague Conference on Private International Law shall at regular intervals convene a Special Commission to review the practical operation of the Convention.

Article 13 Amendments to the Convention

To be completed.

Article 14 Signature, ratification, acceptance, approval or accession

- (1) The Convention shall be open for signature by all States [and Regional Economic Integration Organisations].**
- (2) The Convention is subject to ratification, acceptance, approval or accession by the signatory States [and Regional Economic Integration Organisations].**
- (3) The instruments of ratification, acceptance, approval or accession shall be deposited with the Ministry of Foreign Affairs of the Kingdom of the Netherlands, depositary of the Convention.**

[Article 15 Regional organisations]

For the purpose of this Convention, Regional Economic Integration Organisation means any organisation constituted by Sovereign States to which their Member States have transferred competence in respect of matters governed by this Convention, including the competence to enter into international agreements in respect of these matters.]

Article 16 Entry into force

- (1) The Convention shall enter into force on the first day of the month following the expiration of three months after the deposit of the third instrument of ratification, acceptance, approval or accession referred to in Article 14.**
- (2) Thereafter the Convention shall enter into force for each State subsequently ratifying, accepting, approving or acceding to it, on the first day of the month following the expiration of three months after the deposit of its instrument of ratification, acceptance, approval or accession.**

[Article 17 Transitional Rule]

- (1) This Convention applies in a Contracting [Party][State] to all dispositions of securities held with an intermediary concluded after its entry into force for that [Party][State], and, subject to the following provisions, to all dispositions concluded before its entry into force for that [Party][State].**
- (2) In the respect of dispositions concluded before this Convention entered into force for that [Party][State],**
 - (a) this Convention shall not affect the validity of a disposition of securities held with an intermediary that has been made and perfected in accordance with the applicable law designated by the conflict of laws rules of that [Party][State] in force before this Convention entered into force for that [Party][State], even if the applicable law was not the law of the place of the relevant intermediary determined under Article 4 of this Convention;**

- (b) a party to a disposition of securities held with an intermediary may perfect in accordance with the law of the place of the relevant intermediary determined under Article 4 of this Convention;
 - (c) in determining the place of the relevant intermediary for the purposes of Article 4 of this Convention, the following rules may also be taken into account in the absence of an express agreement between the parties as to that place –
 - [(i) a provision in the account agreement designating the applicable law may be treated as an agreement that the securities account is maintained at an office or branch in the jurisdiction whose law is designated;
 - (ii) in the absence of a clause designating the applicable law, an identification of a particular office or branch as the place of the relevant intermediary, or other indication in the account agreement that the intermediary is acting by or through a particular office or branch, may be treated as an agreement that the account is maintained at that office or branch.]
- (3) A Contracting [Party][State] may declare at the time of ratification, acceptance, approval or accession that it will extend the application of the rules contained in sub-paragraph (c) to dispositions concluded during a specified period, not to exceed two years, after the Convention entered into force for that [Party][State].]

Article 18 Denunciation

- (1) A State [or Regional Economic Integration Organisation] Party to this Convention may denounce it by a notification in writing addressed to the depositary.
- (2) The denunciation takes effect on the first day of the month following the expiration of six months after the notification is received by the depositary. Where a longer period for the denunciation to take effect is specified in the notification, the denunciation takes effect upon the expiration of such longer period after the notification is received by the depositary.

Article 19 Notifications by the Depositary

To be completed.

[Other final clauses]

To be completed.