

### **Possible Agenda for Legal Experts Group**

**1. Identify the “securities account” legal issues which require an EU solution.**

The experts group must be practically focused on issues which are of real concern, and must not discuss “problems” which do not arise under EU countries’ laws.

See the attached list for possible issues; whether an issue is one of real concern is to be determined, as not all of these issues will be relevant.

**2. Identify the legal issues with asset servicing which require an EU solution for harmonization and removal of cross-border barriers.**

Asset servicing issues include income and benefits payments, mandatory and voluntary corporate actions, voting, tax reclaims, etc.

**3. Identify legal issues which restrict or prevent issuers choosing a “location” for their securities.**

It may be necessary for the Legal Experts Group to consider the effects of the Hague PRIMA Convention, and if so the Group should report on its practical implications. (Note, however, that Group should not debate the merits of the text of the Hague PRIMA convention.)

**4. Make recommendations for new EU legislations to remove anomalies and areas of legal uncertainty in relation to the above.**

The Legal Experts Group should consider the interplay with (and existing inconsistencies in) the Settlement Finality, Collateral and Winding-up Directives and the Insolvency Proceedings Regulation.

## **Securities Account Certainty Issues**

### **1. Securities Holding through Intermediaries**

#### **a. Nature of account-holder's interest**

An account-holder's interest can be classified as a property right, an interest under a trust, or a purely contractual right, with very different legal consequences. For various legal purposes, such as selling requirements, taxation, investment restrictions imposed on funds, etc it is necessary to categorise an item of property as a security or something else, such as a claim.

#### **b. Finality of receipt**

Whether a security has been transferred to a recipient is largely a question of reversibility by the intermediary which has effected the credit entry to the recipient's account. Finality may not, however, be determined by the credit entry itself, but by the finality of the receipt by the intermediary of the security at a higher level (the "provisional credit" issue).

#### **c. Effect of shortfalls on account-holders**

If an intermediary becomes insolvent and cannot buy-in to cover shortfalls, how will the losses be shared among claimants? Answers can range from "they rank alongside creditors of the estate" via bewilderingly complex and unpredictable forensic accounting to "rateably".

### **2. Transfer of Securities by an Intermediary**

#### **a. Procedural requirements to effect a transfer of account-holder's interest**

National rules for transfer of "securities" are not only different inter se but also differ from national rules for transfer of contractual rights or rights in a trust. How the account-holder's rights are characterised locally can affect the rules for transfer, which ought in any event to be harmonized.

#### **b. Net settlement**

If an intermediary has received offsetting instructions from its account-holders, it may not always be effective to implement such instructions by a single netted change in the balances held by the intermediary at a higher level. Instead it might be necessary to process each instruction separately

### **3. Third Party Claims**

#### **a. Procedural requirements to obtain and enforce a security interest in account-holder's interest**

The Collateral Directive has largely removed differences where it applies, but the scope restrictions in that Directive have allowed member states to retain local rules imposing widely differing formal requirements on taking and enforcing security interests over account-holders' interests, and associated issues such as re-use of collateral and recognition of title transfer collateral arrangements.

**b. Determining priority among competing claimants to an account-holder's interest**

Priority contests can arise between (for example) purchasers, free-of-payment transferees, security-interest holders, borrowers, judgment creditors, the insolvency officer, theft victims, persons whose rights arise by operation of law, etc. National rules differ as to the outcome in such contests. In particular, there is no uniformity as to whether a good-faith buyer takes free from prior claims.

**c. Ability to undercut account-holder's interest through "upper tier attachment"**

An account-holder's interest in a security may be regarded as property available to be seized (by attaching creditors, or an insolvency officer) in the country in which the issuer is located. If this occurs, the intermediary's holding could be diminished even if no action has been or can be taken against the account-holder in the country where the account is maintained. At worst the intermediary's entire holding could be frozen while the problem is resolved.

**d. Insolvency proceedings**

Insolvency proceedings affect property rights. In particular insolvency officers can (a) act to reverse pre-insolvency transactions; (b) treat property disposals occurring on or after insolvency as void; (c) freeze foreclosure on security interests; (d) allow privileged creditors to share preferentially in the proceeds of liquidation of certain asset types or certain security interests. Such rules differ widely between countries, yet it is often unclear which country's insolvency laws apply.

**4. Rights Against the Issuer**

**a. Exercise of voting rights**

An account-holder's right to vote or exercise other rights under securities held indirectly may not be recognised if the account-holder is not directly registered as the holder. Worse, national laws may not allow an intermediary to vote part of its holding one way and the remainder the opposite way.

**b. Whether account-holder can exercise set-off against issuer**

An account-holder may have a counterclaim against the issuer. Whether the account-holder has a right to set off the issuer's obligations against such counterclaim (and the consequences, where set-off is allowed) differs between countries.