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**NOTE FOR THE FILE**

**Subject: Second informal meeting on corporate actions, 9<sup>th</sup> March 2007**

**Salvatore Lo Giudice** reminded the group of the aim of these informal meetings of experts on corporate actions. This is to exchange views in order to establish a common understanding of the legal and fiscal compliance issues which impact or may impact on the full dismantling of Giovannini barrier 3 (*Differences in national rules relating to corporate actions, beneficial ownership and custody*). The final objective should be to achieve clarity and ideally agreement on the interdependences among barrier 3 and legal and fiscal compliance issues.

He recalled the progress made by the organisations involved in dismantling Giovannini barrier 3. The ECSDA's and ECSAs' findings were in particular mentioned.

On the basis of the agenda, the following topics were discussed.

**Agenda item 1: Report on the Legal Certainty Group (LCG) February meeting, in particular as regards corporate actions**

**Agata Waclawik-Wejman** gave an update of the Legal Certainty Group proceedings and reported on the LCG meeting held in Brussels on February 26<sup>th</sup> and 27<sup>th</sup>, the first after the July 2006 Advice was released. Three strands for future work by the LCG were identified: (i) legal effects of book-entries; (ii) corporate actions processing; and (iii) location of issue of securities. For each subject a sub-group has been set up within the LCG.

The initial findings of strand 2 – which is the one dealing with corporate actions processing and thus directly involved in this context – were reported. The work on strand 2 will focus on the specific problems of the legal investor-issuer relationship which derive from the circumstance of the securities being held through intermediaries. Company law aspects of corporate actions (rights vested in securities) should be clearly distinguished from the problems related to intermediaries' activity. Only the latter should be addressed by the LCG since its mandate only refers to problems arising from the fact that securities are no longer represented by paper documents. Answers to Question 34 of the LCG Comparative Survey (the "Jumbo Report") will be in particular analysed so as to draw a comprehensive matrix of all the existing problems relating to cross-country divergences on practical management of corporate actions. This framework will be used for a further discussion in order to find a feasible solution to Giovannini barrier 3.

**Agenda item 2: Moment of transfer of "ownership"**

In general, the question is whether a smooth transfer of securities is hampered by the lack of legal harmonisation across EU as regards the moment of transfer of ownership.

**Patrick Poncelet** gave a general introduction to the European Banking Federation (EBF) document on transfer of ownership and remarked that the beneficial owner, rather than the legal owner, should be considered when discussing the topic.

**Didier Hermans** reported on the EBF note dealing with two set of issues: (i) ex date, record date and market claims; (ii) the moment of transfer of ownership.

A lively discussion followed on the possible inconsistencies related to different practices for the transfer of ownership. Among the consequences of these inconsistencies, tax issues were raised. **Philip Kerfs** explained that the fiscal treatment of market claims varies depending on the moment of transfer of ownership. If the transfer is considered to be made on trade date, market claims are regarded as dividends and a withholding tax will apply; on the contrary, if the transfer is considered to be made on settlement date, market claims are deemed to be compensations, and no withholding tax will apply.

The discussion distinguished between market transactions and OTC transactions. As regards market transactions, it was argued that uncertainty as to the exact moment when ownership is transferred may be problematic if market participants have the choice of the settlement provider. A possible example is France prior to the recent legislative reform, where the moment of transfer of ownership was on trade date. The following question was asked: what were the consequences in case the transaction was settled through a CSD which was linked to the French CSD and in whose country the moment of transfer of ownership was on settlement date? On a request by the Commission, **Philippe Langlet** provided a graphical example. The discussion was not conclusive.

As regards OTC transactions, the issue seemed to be that CSDs – contrary to what is the case for market transactions – do not usually have the information as to when the trade has taken place. Without such information, CSDs cannot process market claims. A counter-argument was made that ECSDA standard 27 specifically deals with this issue: "*For all bilateral input trade date must be a matching field*". **Salvatore Lo Giudice** stressed that the aim of the group is not to discuss the appropriateness of standards developed by the associations working on Giovannini barrier 3, but rather to discuss about the possible problems due to the possible interdependencies between barrier 3 and legal and fiscal compliance barriers. Again, the discussion was not conclusive.

► Even though there continued to be no agreement on the relevance of the issue of moment of transfer of ownership as a legal barrier to a full dismantling of Giovannini barrier 3, the lively discussion confirmed the importance of the issue.

In order to put the group in the conditions to further look at the issue with the required background information, it was agreed that representatives from the private sector associations would provide practical examples or scenarios where problems related to the issue of the moment of transfer of ownership would be made evident. April 16<sup>th</sup> was identified as the deadline to provide the practical examples.

**Agenda item 3: Report on FISCO February meeting and discussion of the draft second report on solutions to "Fiscal compliance barriers related to post-trading within the EU" of February 2007**

**Philip Kerfs** gave an update on the last FISCO group meeting. Most discussions, e.g. those referring to the issue of "shifting withholding responsibilities to foreign intermediaries", were not of substance. The only issue which was heavily debated from a substantial point of view was that of "transaction tax".

Two opinions were identified among the FISCO members. According to some members, the mere existence of a transaction tax represents a barrier in itself. For instance, not every CSD is apparently able to debit cash accounts relating to tax collection, so that the duty to withhold charges may represent a limitation to cross-border activity. In other members' opinion, a barrier arises only if the procedures imposed for tax withholding are discriminatory towards foreign settlement services providers or CSD participants. In its future work, the FISCO group will try to reflect both such opinions. The final report should be finalised in June.

A discussion followed on the draft FISCO Second Report on Solutions, with comments in particular from the ECSDA and ECSAs representatives. As regards the issue of shifting withholding responsibilities to foreign intermediaries participants expressed a strong preference for the US taxation system, as compared in particular with the Japanese system. **Paola De Antoni** expressed the view that the report should clearly give the option between at source relief procedures and quick or even standard refund procedures, as the latter might be preferable for small intermediaries. Moreover, the need for a sharper distinction between "pooled accounts" and "omnibus accounts" was expressed.

Another set of comments focussed on the institutions to which the report refers. It was noted that the report is often ambiguous when it refers to a "nominee" (e.g. p. 28) or when it refers to intermediaries. In the last case, it is not clear whether CSDs are or are not included in the definition of intermediaries. **Carla Bachechi** expressed the view that the report should make it clear that CSDs are either included in the definition of intermediaries or, in any case, included in the scope of the report. All sentences that seem to restrict the scope of the document to banks need to be amended accordingly (for instance, on p. 20).

► The Commission encouraged members of the group to provide written comments. Comments to the draft Report should be sent as soon as possible, as a new draft will be available by mid April.

#### **Agenda item 4: Classification of events**

**Patrick Poncelet** gave a presentation of the document prepared by ECSAs and ECSDA regarding the "Classification of events and definitions". The aim of the document is twofold: on the one hand, it provides a common framework for definition and taxonomy, especially for non-experts. On the other, it gives a clear picture of the organisations involved in the standardisation process and their relative tasks. Under the proposed classification, the general meeting is regarded as a separate corporate action because of its peculiarities. A wide agreement was expressed on the contents of the document.

#### **Agenda item 5: Other potential legal and fiscal compliance barriers**

Finally, the other items raised in the ECSAs and ECSDA document on legal and fiscal compliance constraints, which have already been discussed at the first meeting, were quickly addressed.

*Impact of lengthy and cumbersome withholding tax procedures on payment date*

The Common Deliverable on payment date (PD) calls for PD to be as close to Record Date (RD) as possible; ideally, PD should be the day after RD. However, lengthy and cumbersome withholding tax procedures make it very difficult for this common deliverable to be implemented. One of the main thrusts of the FISCO second Report on solutions is precisely to eliminate or reduce such lengthy and cumbersome withholding tax procedures.

► Starting from the previous observation that one of the main thrusts of the FISCO second Report on solutions is precisely to eliminate or reduce lengthy and cumbersome withholding tax procedures, the Commission concluded that the interdependency between fiscal compliance barriers and Giovannini barrier 3 due to the "impact of lengthy and cumbersome withholding tax procedures on payment date" is accepted and, even more, clearly recognised by the FISCO group.

The Commission will keep this line in the follow-up to these informal meetings.

#### *Legal basis for definition of dates*

The issue is that even though dates – such as RD and PD – exist for practical reasons in every market, they are not legally fixed concepts in each Member State.

The issue was not considered by the group to be a legal constraint to dismantling of Giovannini barrier 3. Market forces were recognised to provide the best solution to the issue. Standardisation, rather than a legal intervention, was consequently identified as the preferential tool in this field.

► On this basis, the Commission concluded that the fact dates are not legally fixed concepts in each Member State is not considered to be a legal constraint to dismantling of Giovannini barrier 3.

#### *Legal basis for and mandatory dissemination of electronic communication by issuers*

Apparently, not all Member States recognise the legal validity of electronic communication by issuers. This was recognised to hamper the standardisation regarding the filing of electronic and formatted communications, which is one of the common deliverables to be agreed by the associations working on the dismantling of barrier 3.

According to the members, the filing of electronic communication should at least be allowed in all Member States, while no agreement was reached on the opportunity/feasibility of a specific duty in this field, whereby issuers should be mandated to disseminate information electronically.

► On this basis, the Commission concluded that the issue of the legal basis of electronic communication by issuers is a legal constraint to the full dismantling of Giovannini barrier 3.

On the contrary, the issue of mandatory dissemination of electronic communication by issuers is not a legal constraint to the full dismantling of Giovannini barrier 3. Rather, it is an issue which, in line with the recommendation of the second Giovannini report, is left to the private sector to deal with.

### *Issuers' liability when translating documents*

No legal basis was identified for such duty. It was agreed that it should be regarded as a policy issue not to be addressed by the informal group or by the LCG.

► The Commission concluded that the issue of the issuers' liability when translating documents is not a legal constraint to the full dismantling of Giovannini barrier 3. Rather, it is an issue which, in line with the recommendation of the second Giovannini report, is left to the private sector to deal with.

### **Follow-up**

► If deemed appropriate by the members in light of the documents to be filed in the meantime, a new meeting of the informal group might be fixed towards May 20<sup>th</sup>.

► The Commission – taking into account the conclusions of the informal meetings on corporate actions and also the further input which the associations might want to submit as regards in particular the issue of the moment of transfer of ownership – and in cooperation with the FISCO group and the LCG, will prepare a note in which it will summarise the work on the interdependencies between Giovannini barrier 3 and the other Giovannini barriers along with the other possible fiscal compliance or legal constraints.

This note will most likely be presented at the next CESAME meeting.

Salvatore LO GIUDICE

**Participants:** Patrick PONCELET, Didier HERMANS, Paola DE ANTONI, Ben VAN DER VELPEN (ECSAs); Carla BACHECHI (ECSDA); Salvatore LO GIUDICE (Commission); Agata WACLAWIK-WEJMAN, Philippe LANGLET, Matteo GARGANTINI, Sébastien COCHARD, Juergen THAN, Philipp PAECH (LCG); Philip KERFS, Tomas THORSEN (FISCO)