Questionnaire to the Expert Group of the European Securities Committee

To facilitate cross-border investing the CMU Action Plan envisages for 2017 a targeted action on securities ownership rules and third-party effects of assignment of claims. The action is further clarified in the CMU Communication of September 2016 as a legislative initiative to determine with legal certainty which national law shall apply to security ownership and to third party effects of the assignment of claims. The purpose of this questionnaire is to learn Member State's preferences with regard to different options for the upcoming policy initiative.

This is in follow-up to the questionnaire sent to EGESC in December 2016, asking about national conflict of laws rules and the transposition of EU Directives. We would like to take this opportunity to thank those replying to the questionnaires for their valuable input. We received 18 replies, which helped us evaluate existing European legal provisions.

The public consultation on the policy initiative closed on 30 June 2017. The 39 replies came mainly from market participants, although 5 Member States also expressed their opinions. In July 2017 a High Level Group of legal experts, set up by the European Commission, worked out possible alternative legal solutions on book-entry securities. One of the options they proposed has not been tested in the public consultation: a mixed approach between the "place of relevant intermediary approach" (PRIMA) and the Hague Securities Convention.

The current questionnaire was drawn up after analysis of the public consultation results and analysis of the legal solutions put forward by the Expert Group, in order to get information from Member States about the preferred options. Annex 1 contains the list of options for different classes of assets and contains the questions we would like to receive your written answers to by 25 September 2017 to the following address: FISMA-C2@ec.europa.eu

Detailed background information on the initiative is provided in the public consultation document[1]. In case you need any further information please do not hesitate to contact us.

[1] https://ec.europa.eu/info/sites/info/files/2017-securities-and-claims-consultation-document_en.pdf

Annex 1

Possible legislative solutions to specify the law applicable to proprietary aspects of transactions in the following asset classes

1. Non book-entry securities

Stakeholders often question whether the scope of the initiative should cover non-book entry securities. The options are to either:

1. **Not take any action** or
2. **Harmonise the conflict of laws** breaking down non book-entry securities to the following categories:
   - certificated non-book entry securities: law of the country where the certificate is located
   - non-book entry securities represented by entries in an issuer register (& certificated registered shares): law applicable to the issuer
   - non-book entry securities constituted by entries in an operator register: law of the register (optionally: law of the register if allowed by the law of the issuer)

Preferred option:

It would be of very limited use to harmonise rules on non-book entry securities (traditional paper securities) when these hardly exist. Moreover, we wonder whether most Member States already have more or less the same conflict of laws rules. If so, official harmonisation is not of great use.

Besides, international bodies such as the *Global Forum on Transparency and Exchange of Information for Tax Purposes* and the *Financial Action Task Force* urge States to abolish traditional securities (like non-book entry securities), because owners can hide their identity by using them. This could facilitate money laundering and financing of criminal activities (terrorism, bribery). Harmonising rules on non book-entry securities could be a wrong signal.

Therefore, we prefer option 1 NOT TO TAKE ANY ACTION

Main advantages of the preferred option:

Main arguments against the other options, if any:

1. Book-entry securities

For book-entry securities three alternative options are being considered, with the option 3 aiming to reach a consensus between supporters of option 1 and supporters of option 2:

1. **Ratification of the** Hague Securities Convention: Law governing the account agreement as expressly agreed by the contracting parties, provided that the intermediary has an office in that state;
2. **Exhaustive legal definition of the applicable law:** Law of the intermediary or branch where account was opened for the client;

3. **Mixed approach (legal definition of the applicable law with a contractual element):** Law of the intermediary where account is maintained[2]; where the account agreement specifies a foreign branch, then the law of that branch, provided it is indeed that branch maintaining the account.

The three options differ in terms of the freedom of choice they allow to the transacting parties and in terms of offering either regional consistency only (throughout the EU) or global consistency (not only throughout the EU but also between the EU and third-countries). However all three options would designate the law governing the settlement system under Art 2 (a) SFD to govern proprietary aspects of transactions is book-entry securities in securities settlement systems.

Options for book-entry securities	**1. Choice of law under the Hague**	**2. Exhaustive legal definition**	**3. Mixed approach**
Extent of contractual freedom	Extensive (reality test is whether there is a branch or office in that state)	none	Limited (reality test is whether the account is maintained by the branch in that state)
Regional or global consistency	=Global consistency	=Regional consistency	=Global consistency possible
Book entry securities in a securities settlement system	The law of the Member State applicable to the SSS as defined in SFD Art 2 (a)		

Preferred option:

Main advantages of the preferred option:

Ratification of the Hague Securities Convention

Main arguments against the other options, if any:

There are some ambiguities; not all States may interpret the Convention the same way. Nevertheless, the Convention is far better than nothing at all.

3. <u>Claims constituting financial instruments</u> (other than book-entry securities and/or other claims traded on financial markets)

The two options for conflict of laws rule on third party effects of assignment of such claims are:

1. **The law of the assignor's habitual residence**

2. **The law governing the assigned claim**

Preferred option:

[2] Maintaining the account could be defined as effecting or monitoring entries into securities accounts, administering payments or corporate actions or other regular activity necessary for administration of securities accounts. To make the test clearer, it could be a sequential test.

The preferred option by far is the law governing the assignment contract between the assignee and the assignor (cf. Art. 14 par.1 Rome I). This conflict rule has been (and is still) used in the Netherlands to cover all property law aspects for over 20 years and it has not encountered any problems.

We are disappointed that this option of the law governing the contract between the assignor and the assignee, is not mentioned as a third option. It became clear at last week's meeting between the Commission and the Member States that there is not nearly a majority of the Member States in favour of the option regarding law of the assignor's habitual residence. Therefore, it seems highly premature to discard the option regarding the law governing the contract between the assignor and the assignee at this point in time. Moreover, the law governing the contract between the assignor and the assignee is mentioned as an option in question 6. We do not see why there should be a difference in possible answers between question 3 and 6.

Main advantages of the preferred option:

Main arguments against other options, if any:

Adding a third applicable law - the law of the assignor's habitual residence - to any international assignment means complicating this type of transaction enormously. Rome I, Art. 14 already has two applicable laws involved for assignment. It would be very disadvantageous to have yet another law to be taken into account for each transaction.

4. Cash held in accounts

The two options for the conflict of laws rule for determining the third party effects of assignment of cash held in accounts:

1. **The law of the place where the cash account is located**
2. **The law governing the assigned claim**

Preferred option:

Main advantages of the preferred option:

The law governing the assigned claim

Main arguments against other options, if any:

5. Assignment of credit claims

The two options for the conflict of laws rule for determining the third party effects of assignment of credit claims are:

1. **The law of the assignor's habitual residence**
2. **The law governing the assigned claim**

Preferred option:

We are disappointed that the third option, the law governing the contract between the assignor and the assignee, is not mentioned. Only 5 member states replied to the public consultation held in June 2017, so one cannot know what option is preferred by the majority of member states. It seems that one option is excluded beforehand, which is not appropriate.

Moreover, the law governing the contract between the assignor and the assignee is mentioned as an option in question 6. We do not see why there should be a difference in possible answers between question 5 and 6.

We would prefer to make as little distinction as possible between different types of transaction. We would therefore, prefer to treat questions 3, 5 and 6 all in the same way.

Main advantages of the preferred option:

Main arguments against other options, if any:

6. Claims used as underlying assets in securitisation – the three alternative options are:

1. **The law of the assignor's habitual residence**
2. **The law governing the assigned claim**
3. **The law applicable to the contract between assignor and assignee**

Preferred option:

Main advantages of the preferred option:

The law applicable to the contract between assignor and assignee.

Main arguments against other options, if any:

See our answers to questions 3 and 5

With any questions you can contact Ms Barbara Gabor. Please send your replies by 25 September 2017 to FISMA-C2@ec.europa.eu Thank you.