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## CONSULTATION BY THE COMMISSION

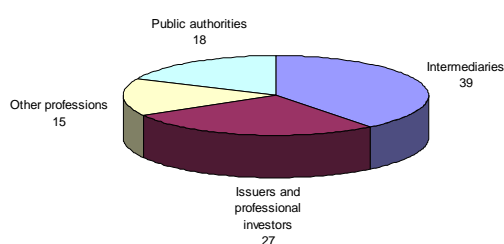
### Summary of responses received in respect of the consultation document legislation on legal certainty of securities holding and transactions.

#### 1. INTRODUCTION

In response to the public consultation<sup>1</sup> on “Legislation on legal certainty of securities holding and dispositions”, the Commission received 99 contributions from stakeholders: 34 from registered<sup>2</sup> organisations, 45 from individuals<sup>3</sup>, 18 from public authorities. All but two responses (following requests from the contributors) are published on the EU Commission's website<sup>4</sup>.

Concerning the background of the respondents<sup>5</sup>, 39 are intermediaries, 27 are issuers and professional investors<sup>6</sup>, 15 other professions (mostly CSDs and stock markets) and 18 are public authorities. No contributions were submitted by non-professionals, acting whether as citizens or as retail investors<sup>7</sup>. Of course, these categories are not always clear-cut, since for example, many intermediaries are at the same time issuers and/or investors. Issuers and investors are often symmetrically opposed in other contexts, such as corporate law. Still, in the present context of book-entry securities, these categories helped identifying the major groups of respondents, with a rather strong correlation between their main activity and the concerns expressed in their respective answers.

**Figure 1: number of responses by categories of stakeholders**



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<sup>1</sup> [http://ec.europa.eu/internal\\_market/consultations/2009/securities\\_law\\_en.htm](http://ec.europa.eu/internal_market/consultations/2009/securities_law_en.htm)

<sup>2</sup> Registered on the Register of interest representatives

<sup>3</sup> "Individuals" referred here are private organisations who failed to register, whose answers are therefore assumed having been sent by the individual who signed it and not by their respective organization. They should therefore not be confounded with natural persons acting as investors or EU citizens.

<sup>4</sup> [http://circa.europa.eu/Public/irc/markt/markt\\_consultations/library?l=/financial\\_services/harmonisation\\_securities&vm=detailed&sb=Title](http://circa.europa.eu/Public/irc/markt/markt_consultations/library?l=/financial_services/harmonisation_securities&vm=detailed&sb=Title)

<sup>5</sup> We counted associations depending on who they represent

<sup>6</sup> Issuers and professional investors were counted together since most professional investors that answers could be also counted at the same time as issuers (mostly from the insurance sector).

<sup>7</sup> Except from the Commission sponsored Financial services users expert group, ...

The geographical distribution of the respondents is based on the registered office of the latter. This is why a few of the respondents are labelled as coming from outside the EU, although their activity is partly located within the EU. Associations with an obviously European-wide representation were included in the "EU" category. As it can be seen in the table below, the responses cover all EU15 Member States. Conversely, responses from only a third of EU12 Member States were received.

**Figure 2: Number of responses by countries**

<b>Austria</b>	1	<b>Greece</b>	1	<b>Portugal</b>	1
<b>Belgium</b>	1	<b>Ireland</b>	1	<b>Slovenia</b>	1
<b>Czech Rep</b>	2	<b>Italy</b>	5	<b>Spain</b>	5
<b>Denmark</b>	3	<b>Luxemburg</b>	2	<b>Sweden</b>	4
<b>Finland</b>	2	<b>Malta</b>	1	<b>UK</b>	11
<b>France</b>	15	<b>Netherlands</b>	4	<b>Associations covering EU</b>	10
<b>Germany</b>	24	<b>Poland</b>	2	<b>Third countries</b>	3

In the analysis below, each respondent is counted as a separate respondent, although one may note the similarity (or even identity) of some of the responses. Some contributions addressed the questionnaire only partially or in general terms. In such cases their positions, when expressed, were reflected in the statistics, while counting blank answers as "no answer".

**2. SUMMARY OF FINDINGS**

The initiative was unanimously welcomed by almost all respondents who confirmed problems caused by the absence of a harmonised legal framework in the four areas covered by the consultation. However, there was considerable divergence in the answers concerning the method to be used for tackling each of the relevant areas.

**2.1 Holding and disposition of book-entry securities (questions 1 to 16bis)**

Most of the divergence concerns whether any future legislation on this issue should or should not stick to the functional approach as proposed by the Legal Certainty Group. This concerns in particular the type of methods for acquisitions and

dispositions (other way referred as "book-entry methods") that should be admitted, the mechanisms imposed to grant the integrity of securities' issues and the consequences of book-entries on ownership rights, especially if the latter are covered by a harmonised conflict of law rule.

- **Extent of the EU legislators' intervention (questions 1 and 3)**, respondents were evenly divided between supporters of a purely functional approach, close to the one proposed by the Legal Certainty Group addressing the different methods of book entries, and supporters of an extensive EU legislation addressing the legal consequences of book-entries on ownership.
- **Rights of account holders (question 4)**: A majority supported the recognition of the rights to exercise "rights enshrined in securities" and to have their "instructions executed". However a small majority considered that the right of the account holder to "choose the holding method" could suffer exceptions, if balanced by a regime warranting the restitution of the securities whatever the holding method.
- **Book entry methods (question 5 and 6)**: a strong majority supported including both "debit-credit" and "earmarking" among the mutually recognised book-entry methods, while a majority opposed the inclusion of "control agreements", except for enforcement purposes in the context of insolvency of the account provider.
- **Effectiveness (question 7)**: A majority of respondents supported unconditional effectiveness of acquisitions and dispositions effected under one of the harmonised book-entry methods, except for DVP systems.
- **Reversal (questions 8 and 9)**: However the possibility for an account provider to make a reversal was largely acknowledged as concerns the 3 proposed cases for reversal, subject to the protection of the good faith acquirer.
- **Integrity of the securities issue (question 11, 12, 13)**: an overwhelming majority supported, as a minimum duty, the obligation for the account provider to maintain at least as many securities as the aggregate number of securities credited to its clients' accounts. A majority supported this being checked through a daily reconciliation, under the auspices of the CSD. In case of shortfall, many respondents suggested a complete set of procedures for the recovery of lost securities (such as recuperation from faulty upper tier account providers, compensation mechanisms involving a guarantee fund, etc.) before having recourse, as last resort, to pro-rata sharing of the remaining lost securities
- **Conflict of laws (questions 14 to 15bis)**: Most respondents argued that future European legislation should contain a conflict-of-laws rule which governs also the issues within the scope of the Settlement Finality Directive (SFD), the Financial Collateral Directive (FCD) and the Winding Up Directive (WUD). Regarding the content, the majority favoured a location rule similar to the current rules contained in the three directives, however institutionalising a more complete and reliable criterion for the identification of the applicable law. Others argued for the law of the issuer to apply throughout the holding chain or for a rule based Article 4 of the Hague Securities Convention.

- **Complexity and costs related to Giovannini barrier 13 (questions 2, 16 and 16bis):** Respondents reported a wide range of situations concerning costs, depending on their respective position (intermediary, issuer, investor or CSD), the size of their institution and, above all, the degree of regulation of the Member State they are operating from.

## 2.2 Processing of rights flowing from securities"

Respondents are shared between supporters of a detailed legal framework governing the processing of rights by account providers and those who prefer referring to contractually agreed solutions. However, it seems that, as concerns pecuniary rights (most corporate actions) there is an agreement in favour of creating a general obligation to act in the best interest of the account holders, without it being necessary to go into further details.

- **Facilitation of the exercise (questions 18 & 19):** A majority of respondents were in favour of inserting such obligation for account providers to facilitate the exercise of rights flowing from the securities, but the details of which should be arranged by service-level agreement (SLA).
- **Exercise of rights by an account provider on behalf of the investor (questions 20-22):** Answers differed depending on the nature of the rights concerned. Yet, most of the opponents focused against the possibility for the investor to unilaterally renounce exercising voting rights. However, In the case of "pecuniary rights" a majority of answers supported an obligation for account provider to exercise such rights when the account holder is not in a position to exercise them itself, especially for the exercise of conversion or reorganisation rights and the collection of dividends or other payment and subscription". In any case, a strong majority considered that the account provider should be submit to an obligation to act in the best interest of the investor, even without express consent of the latter to exercise such rights.
- **Passing up and down of the necessary information (questions 23-25):** A vast majority of the respondents was in favour of an account provider obligation to pass on information with respect to book-entry securities. when such information is necessary to exercise a right enshrined in the securities. However, most of these respondents suggested that such an obligation should be limited to a "best effort" and should not oblige the account provider to take additional duties like retrieving information (question 23). A majority of the respondents was in favour of limiting passing down to the sole information which is received through the holding chain and not directing it to all investors in securities of that description.
- **Costs related to legal aspects of Giovannini barrier 3 (question 26-26bis):** There was a general agreement concerning the excess of costs, but not on the amount, varying from "insignificant" to "a dozen times more".

### 2.3 Free choice of initial entry of securities (questions 27 to 30)

There is a strong agreement on the purpose, but not necessarily on the appropriate means.

- **Concerning "importability" and "exportability" of the issue (questions 27 and 28):** An overwhelming majority of respondents supports the proposal for any issuer to be allowed to issue into a CSD which is not the domestic one (55 "yes" to question 27) and for allowing CSDs which are governed by the law of an EU Member State to be open to securities issued under the law of another EU Member State (58 "yes" to question 28). This is seen as a major step towards improving both the rationalisation and harmonisation of the European post-trade framework. Opponents consider this issue is closely related to corporate law and that it is thus not feasible to have a choice between two different legal frames. Moreover, such choice would make the exercise of rights more complicated. Scandinavian respondents have indicated the need to take into account the specificities of the Nordic CSDs' framework (direct holding of investors with CSDs).
- **Concerning other CSD related issues (question 29):** a huge majority of the respondents consider that other CSD related issues need to be solved previously (question 29); such as harmonising corporate and tax law. Furthermore many respondents submitted importability and exportability to the prohibition of splitting a same issue between different CSDs, while one respondent proposed to make a clear distinction between holding and settlement. Last, many respondents considered that importability and exportability of the issues should be accompanied by a level playing field among all CSDs in all countries.

### 2.4 Duties of account providers (question 31 to 32bis)

There is a clear majority in favour of account providers being regulated via the MIFID, although some concerns are expressed that only some specific provisions of the MIFID are relevant.

- **As concerns the personal scope of such a regulation,** a huge majority of the respondents do consider that it should apply to all account providers without any kind of exemption.
- **Regarding the kind of EU legal instrument** needed to cover all account providers, a strong majority of respondents favoured a solution amending the MIFID rather than having a separate legal instrument. As concerns the opponents to an extension of MIFID to account providing services, the most often quoted reason was the difference in scope of application of the MIFID.

### 3. ANALYSIS

#### Legal framework of holding and disposition of book-entry securities

##### 3.1 Question 1

###### 3.1.1 Question:

The far greatest part of securities are held and administered through securities accounts maintained by an account provider (e.g., a bank, a broker, a custodian or similar). What is your estimate regarding the percentage of securities, which are not held through a securities account?

###### 3.1.2 Figures

Estimated percentage of non book entry securities (expressed in value), for EU Member States:

<b>Austria</b>	less than 1 %
<b>Belgium</b>	
<b>Bulgaria</b>	
<b>Czech Rep</b>	0 % for listed companies. From 0 to 100% for others, depending on the category
<b>Cyprus</b>	
<b>Danemark</b>	0 % for listed companies. But 5 to 10 % of the total securities are still in paper form.
<b>Estonia</b>	
<b>Finland</b>	less than 0,1%
<b>France</b>	0% for all kind of companies (insignificant exceptions remain)
<b>Germany</b>	Below 1% (no breakthrough concerning the kind and size of the concerned companies)
<b>Greece</b>	0 %
<b>Hungary</b>	

<b>Ireland</b>	Less than 1 %
<b>Italy</b>	0 % for securities traded on regulated market. A minority, for the other securities. Total less than 2%
<b>Latvia</b>	
<b>Lithuania</b>	
<b>Luxemburg</b>	Negligible (although holding of paper form securities is authorized )
<b>Malta</b>	Negligible
<b>Netherlands</b>	"Small" and likely to reduce after a law allowing dematerialisation
<b>Poland</b>	0% for treasury bills. Unknown for the rest
<b>Portugal</b>	0% for listed securities on registered market , small percentage for the rest
<b>Romania</b>	
<b>Slovakia</b>	
<b>Slovenia</b>	3%
<b>Spain</b>	0% for listed securities on "registered" market. Very residual for the rest since obligation to register investors with Iberclear
<b>Sweden</b>	0 % of securities traded on regulated markets in Sweden. Some public companies and most of the private company's securities are still paper-based.
<b>UK</b>	Between 1 and 25 % for FTSE100 / in average between 15 to 25 % held outside securities account/ 6% for liquid and mid-cap securities (i.e. the top 350 listed at LSE). 15% by value for equities, 2% by value for debt securities, 0% by value for money market instruments.

### 3.1.3 Synthesis

Respondents understood that this question addresses the material scope of the future legislation, since it tries to define the percentage of book entry securities in all Member States.



Therefore, respondents provided factual answers on non book entry securities concerning 18 Member states. Information could not be obtained concerning Belgium, Bulgaria, Cyprus, Estonia, Hungary, Latvia, Lithuania, Romania and Slovakia.

All answers point toward the fact that non book entry securities represent in value a very small amount of securities portfolio, varying from 0% in France or Greece to a maximum of 15% in the UK. However, in number of securities, and/or in number of issuers, the situation may be somewhat different. Further information concerning the situation in 25 Member States can be found in the comparative survey achieved by the Legal Certainty Group in 2006 <sup>8</sup>..

Many respondents stressed the necessity for the draft initiative to address only "book-entry transfers" and neither "dematerialisation" <sup>9</sup>, nor the distinction between "nominative" or "bearer" securities<sup>10</sup>, because both issues pertain to corporate law as well as to financial law. However, an important number of answers (mostly German and UK issuers/investors and French banks) expressed the view that a generalisation of "book-entry transfers" should not render intermediation compulsory and should leave the choice to investors, "as legal owners of the securities", to hold these securities directly with the issuer.

#### **a) Distinction between book entry transfers, dematerialisation and intermediation**

- The answers revealed sometimes confusion between "book entry transfers" and "dematerialisation". Dematerialisation only refers to the method of issuance of the securities, not to the method of holding. If dematerialisation often implies book entry transfers, "materialised" systems (by immobilisation of a certificate or of a global note) do not necessarily imply that the securities are paper based. The distinction between "book entry securities" and "paper based securities" only deals with transfers, not with issuance. Hence, book entry securities are the securities the transfer of which is not subject to the remittance of an individual paper **but to a record on an account**. Such account may itself be either paper based or electronic, either individual or omnibus.
- Some answers seemed to confuse "bearer securities" with "book entry securities", while Member States' experience shows that "both bearer securities" and "nominative securities" can take the form of either book entry securities or of paper based securities.

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<sup>8</sup> [http://ec.europa.eu/internal\\_market/financial-markets/docs/certainty/background/comparative\\_survey\\_en.pdf](http://ec.europa.eu/internal_market/financial-markets/docs/certainty/background/comparative_survey_en.pdf)

<sup>9</sup> "Dematerialisation" refers to the method of issuance of the securities and does not necessarily imply that the securities are transferred via book-entries.

<sup>10</sup> "Nominative" and "bearer" securities refer to the method of identification of the investors and can both be transferred either by book-entries or through paper based remittance and custody.

- Other answers (mostly German and UK issuers + French banks) expressed concerns that a generalisation of book entry transfers would render intermediation compulsory and would not leave the choice to investors, "as legal owners of the securities" to keep these securities directly with the issuer. On the opposite view, one UK bank expressed the wish that CSDs be imposed as a minimal level of intermediation, at least for regulated markets.

## **b) Accuracy of the data about paper based securities**

One may also distinguish those countries that can provide reliable data about paper based securities and those that cannot:

- Paradoxically, the countries that furnish the most accurate data on paper based securities are those which, like the UK, have not imposed any obligation of book entry transfers, except for money market instruments. This lack of legislation of book entry transfers is balanced by the fact that most categories of securities issued under such legislations are subject to registration. Hence, in these countries, a distinction is made between bearer paper based securities and nominative/registered paper based securities. For the latter one, the registrar system constitutes an embryo of dematerialisation as well as an alternative to CSD.
- Other countries provide a summa divisio between securities issued with the local CSD and securities not issued with the CSD, or between securities traded on regulated markets and securities traded on the OTC market. The latter are left in oblivion, although they may represent a substantive part, not in value, nor in volume but in number of securities issuers.

## **c) Variety of situations concerning residual paper based securities**

- According to the answers, Member states impose transfers of securities to occur via book-entries depending:
  - on their method of issuance ("dematerialised" under the form of an issuance account or "immobilised" under the form of a paper voucher or a global note)
  - on their level of holding (with the issuer, with the CSD, with the intermediary, with the investor),
  - on their type of holding (nominative or bearer)
  - on their kind or form (shares, debt securities, money market instruments),
  - and more generally, on the nature of the market (regulated or not regulated).

- All in all, there is a positive correlation between, on one hand, the generalisation of book entry securities and, on the other hand, the degree of dematerialisation of the issuance, the degree of intermediation of the holding, the degree of anonymity of the investor, the level of liquidity of the securities and the degree of regulation of the market.
- However, the most commonly used criterion for the obligation to transfer securities via book entries seems to be **the distinction between regulated and non regulated markets**. To that respect, the answers helped distinguishing four categories of countries:
  - Countries that impose book entry transfers for regulated as well as non regulated markets: France, Greece and Finland.
  - Countries that impose book entry transfers for all regulated markets and have a residual percentage of paper based securities on non regulated markets : Austria, Malta, Spain.
  - Countries that impose book entry transfers for all regulated markets but have a substantial percentage of paper based securities on non regulated markets, Luxemburg, Poland, Slovenia, Denmark, Portugal, the Czech Republic, Germany, Belgium, Ireland, Italy, Sweden.
  - Countries that have a residual percentage of paper based securities on regulated markets and a substantial percentage of paper based securities on non regulated markets: UK, Poland.

### 3.2 Question 2

#### 3.2.1 Question:

**Do you assume that the application of the legal framework for acquisition or disposition of book-entry securities, including the creation of collateral interest, is more complex as soon as there are cross-jurisdictional elements to be taken into account?**

#### 3.2.2 Figures for question 2

considerably more complex =	21	<b>43</b>
more complex =	22	
slightly more complex =	38	<b>40</b>
No more complex =	2	
I don't know (or no answer) =	16	

### 3.2.3 Synthesis

Question 2 concerns the complexity of cross border transfers of book entry securities. Indirectly it questions the opportunity of the future legislation, since its main objective is to reduce complexity as well as legal uncertainty in cross border transfers of securities.

Four types of answers were proposed: (1) Considerably more complex, (2) more complex, (3) slightly more complex, (4) not more complex. For the ease of analysis, we may divide them in two groups: those who emphasize the increased complexity and those who tend to minor or to negate it.

The first group leads by a short advance (43 against 40). 16 respondents have not answered, on the ground of their lack of practice concerning book entry transfers.

Consistently, the "relativists" are essentially composed by French banks and German issuers, certain central banks and some small CSDs, which could indicate some distance towards the envisaged legislation, but not necessarily, since some strong supporters of the project also fall among the "relativists".

Besides this two sides distinction, the arguments contained in the answers tell us something more, about:

- The actual scope of added complexity (apparently, outside SSS and financial collateral).
- The nature of added complexity (partly legal, partly operational).
- The current ways followed to by-pass complexity in the absence of legal harmonization (partly through contractual arrangements, partly through the consolidation of the CSD industry).

#### a). **Scope of the complexity**

##### aa) **Domestic versus crossborder aspects :**

- As concerns the volume of transactions, nobody negates the fact that crossborder operations represent a substantial part of nowadays securities activity.
- ECB recalls that "in 2008 about 48% of collateral was held under crossborder basis". Though the figure probably refers to collateral held within the central banks of the Eurozone for monetary policy purposes, this percentage confirms the share of crossborder transfers of securities.

**ab) Payment systems versus outright transfers**

- Half of the answers advocated that there is no increased complexity when the transfers are conveyed via payment systems (EU savings banks, French banks, German issuers), while insisting that 99% of the settlements flow pass through an SSS (French banks).
- However most answers recognized that problems remain as concerns outright transfers, especially in holding chains, each link of which being potentially submitted to a different jurisdiction with consequences on the definition of the "ultimate holder" (ECB).

**ac) Book entries versus paper based custody :**

- One answer reported that there is no problem when the securities are paper based.
- Another member confirmed that legal issues surrounding the acquisition or disposition of securities and the creation of security interests in such securities is far more complex when it is "held in collective custody (book entry form)" (A German intermediaries association).

**ad) Omnibus holding versus individual holding :**

- Two answers reported that when cross border holdings are almost exclusively held via "nominee" structures (In particular in the case of CSDs), this creates a more complex situation both for the shareholder, and potentially the issuer, when trying to ascertain ownership of their shares (two UK registrars).

**b) Nature of the complexity**

The answers can be shared between those who attributed increased complexity to legal problems, and those who denied it or linked it to more operational problems, currently outside the scope of the envisaged legislation:

**ba) The legal concerns reported by the respondents concern mostly:**

- Risk of non recognition of certain holding structures: for example, the holding of assets via trusts constituted abroad is not recognized by Spanish law (A Spanish law firm), which prevents the use of the correct legal holding structure because of national impediments (an ICSD , and an Italian intermediaries association) and incurs a distortion of competition detrimental to countries that discourage investors because of their legislation on holdings (A Dutch authority).
- Risk of re-characterization of ownership structures : for example a full ownership may be re-characterized into a pledge and vice versa (Czech Authority, an Austrian intermediaries association, several European intermediaries associations).

- Such risks necessitate "ensuring legal validity from local legal counsels, which is time consuming and causes remarkable extra costs" (A Swedish and a Finnish intermediary).

**bb) Several answers tended to negate such risk of re-characterization :**

- Such a risk is already tackled by the SFD and above all by the FCD (A German Authority, an Italian intermediaries association, a Slovenian CSD)
- In crossborder context, the question whether an account holder is a resident or non-resident vis-à-vis the account provider is not an element of complexity (a French Intermediary).
- Conversely, crediting and debiting securities accounts, as well as putting up securities as collateral, take similar forms, irrespective of where the account provider and the account holder are located. (A French issuers association).
- If added complexity were sought, it would relate to the negotiation of the account agreement between entities with different legal background (two French and German issuers association).
- However, as far as corporate law aspects are concerned, the exercise of rights attached to securities appear to be more complex and uncertain in a cross border environment (a French issuers association), especially if the perspective of the final investor is considered (an Italian intermediaries association).

**bc) One must also note that many answers attributed the increased complexity to operational/non legal problems:**

- Direct tax issues as already dealt under barriers 11 & 12 (an Italian intermediaries association, a UK intermediaries association)
- Different corporate actions procedures (an Italian intermediaries association)
- Different procedures and requirements also easily lead to failures in processing (A Finnish Intermediaries Association)
- Necessity to exchange cumbersome documentation (A European stock markets association)
- The opacity of the intermediary chain (German investors and issuers) regardless of its international aspect (French Intermediaries).

**c) Ways to by-pass complexity:**

In the absence of harmonized legal framework, several respondents reckon on the following methods:

**ca) Contractual methods, whether bilateral or multilateral.**

This solution is privileged by German banks and CSDs:

- An ICSD notes that *"statutory and contractual arrangements of certain account providers and the legal frameworks governing securities settlement (especially in Europe) can be shown to have eliminated this complexity in a number of important instances"*.
- A German Intermediaries association promotes pragmatic solutions consisting in clustering law applicable to custody with law applicable to securities: *"For this reason, the German banking industry decided as early as the 1960s that securities transactions executed and settled abroad shall be regulated in the so-called "Special Business Conditions for non-domestic securities transactions". These special business conditions are intended to exempt the German securities account holder from the legal difficulties of cross-border securities transactions resulting from the fact that the German depository bank acquires the securities abroad and holds them in trust for such a securities account holder. These Special Business Conditions also stipulate that German law shall be exclusively applicable to the securities account holder and his only relevant legal relationship - i.e. that to his German depository bank. The complexity of cross-jurisdictional elements is thus clearly and deliberately reduced. The German depository bank constitutes the bridge to international law and the international holding chain: The German bank enters into the non-German jurisdiction where it acquires a legal title under the relevant (non-German) law. However, this legal title is not transferred directly to the bank's client in Germany. Instead, the bank holds the non-German legal title for and on its client's behalf in a fiduciary capacity"*.
- In the same manner, another German intermediaries association notes that some custodian banks try to reduce the risk by imposing contractually to their foreign depository to exercise their rights only to the extent permitted under the laws of the country of the former who commissions the disposition to the foreign depository (In Germany it is called *"Three Point Declaration/Drei-Punkte-Erklärung"*).

**cb) CSD Consolidation process :**

T2S has raised strong expectations among certain respondents:

- A Greek stock markets association notes *"It should be mentioned though that pan European ventures on the way (as is the case with Link Up Markets) which aim at linking up CSDs improve efficiency and reduce costs of cross-border securities processing"*.
- Two UK registrars stated *"We believe that it is vital that this is addressed as part of the T2S project, which creates a very good opportunity for improving the current situation"*

- A French issuers association concludes that a CSD offers a unique point of entry and facilitates the application of legal rules (in this case, the applicable rules are those of the country where the CSD is located).

### 3.3 Question 3

#### 3.3.1 Question:

**Do you think that harmonisation of the law of holding and disposition of book-entry securities should be done by way of minimum harmonisation, i.e. that in general, Member States' law shall continue to define the general legal characterisation of book-entry securities, whereas certain characteristics of book-entry securities are harmonised? [Yes/No/I don't know; please specify]**

#### 3.3.3 Figures:

<b>Yes minimum harmonisation with no proprietary aspects</b>	<b>48</b>
minimum harmonisation	40
minimum harmonisation extended to corporate law	8
<b>No or Yes for an harmonisation including proprietary aspects</b>	<b>48</b>
minimum harmonisation extended to proprietary aspects	14
maximum harmonisation	34
<b>No answer or don't Know</b>	<b>3</b>

#### 3.3.3 Synthesis:

Question 3 concerns the level of harmonization and, therefore, questions the approach supported by the LCG, other way known as "functional approach". As a matter of fact, question 3 defines the "minimum harmonization" by the scope of the envisaged legislation, i.e.: "*that only certain characteristics of book entry securities should be harmonized*", while the so called "*proprietary aspects*" should remain outside.

Despite this, some respondents seem to have understood that minimum harmonization was more a matter of identity of transposition than a matter of scope,



and have therefore expressed opinions based on the subsidiarity principle. This misunderstanding blurs the interpretation of the results and has led us to subdivide the answers, depending on the actual understanding of minimum harmonization:

- Group 1: minimum harmonization fully compliant with the functional approach ;
- Group 2: minimum harmonization partially compliant with the functional approach (i.e. asking for the recognition of certain corporate law specificities)
- Group 3: minimum harmonization not compliant with the functional approach (i.e. asking for the recognition or reconciliation of certain proprietary aspect specificities)
- Group 4: clear refusal of minimum harmonization and of functional approach, trying to impose certain ownership concepts.

It is then possible to separate the respondents in two groups depending on the compatibility of their preferences with the functional approach. All in all :

- 48 answers support a minimum harmonization compatible with the functional approach followed by the LCG
- and 48 answers support an harmonization addressing to some extent proprietary aspects that were excluded from the functional approach.

The analysis of the arguments presented by the four groups of answers, tells something more:

**a) Group 1 answers favoring minimum harmonization argue that**

- the less one regulates, the better it is for the market (UK authority, Czech authority, European stock markets association, a UK stock market and a UK Intermediary) especially when the respondents do not provide full support to the project (a German Authority, a Slovenian CSD);
- pragmatism commands refraining from a maximum harmonization (a Dutch authority, an ICSD, a European intermediaries association, an Italian CSD, a Swedish intermediary), especially because harmonization of proprietary aspects would also imply regulating the role of the CSDs (another ICSD);
- However such minimum harmonization should be transposed identically in all Member States (a German intermediaries association);
- One should note that certain supporters of minimum harmonisation request at the same time that their proprietary specificities be recognised (a Swedish intermediaries association).

**b) Group 2 answers wishing to extend minimum harmonization to certain corporate law issues :**

- in particular "as concerns the timeliness of information flows" and because that would "further steps towards harmonisation of record dates and voting deadlines" (a European issuers association, a Dutch issuers association);

- in order to have efficient and transparent cross border proxy voting processes and systems (another Dutch issuer association).
- In order that the rights of investors to maintain a direct relationship with the issuer in whom they invest are not compromised.

**c) Group 3 answers wishing to address certain proprietary aspects**

- belief that proprietary rules of Member States are compatible and that the future legislation should try to reconcile them instead of creating a competition between them (another European issuers association, a French intermediaries association, a UK registrar);
- impose mechanisms of restitution of the securities to the final investor, even when they are held at an upper tier level (a French intermediaries association, a Spanish intermediary);
- *"aggregated (own and client) securities holdings at an upper tier level should correspond at any time to the amount held at the upper tier level at any time"* (the European Central Bank, the French Central Bank)

**Group 4 wishing maximum harmonization and refusing functional approach**

- For reasons of efficiency, proprietary aspects should be addressed as well (a Finish intermediaries association, A Greek stock markets association, an Italian intermediaries association, a Spanish law firm, a UK intermediaries association, a UK Registrar).
- Refusal of the Unidroit functional approach (a French issuers association and all French intermediaries).
- Refusal of any contractual approach that denies rights "in rem" (the German central bank, all German Issuers and many issuer associations from other Member States).
- Refusal of the book entry system as a basis for securities ownership (one German issuer).
- Fear that the functional approach does not prevent proprietary aspects from other countries being clandestinely introduced in the domestic legal system (an Italian intermediaries association).

**3.4 Question 4**

**3.4.1 Question:**

**Do you think that book-entry securities should confer upon the account holder the following minimum rights [Yes/No/I don't know, please specify and indicate whether additional elements should be harmonised]:**

- a) the right to exercise and receive the rights attached to the securities, as far as the account holder itself is identified by the issuer law as the person entitled to these rights;**
- b) the right to instruct the account provider to dispose of the securities;**

c) the right to instruct the account provider to arrange for holding the securities with another account provider or otherwise than with an account provider, as far as the applicable law allows holding otherwise than with an account provider.

### 3.4.2. Results:

	Regulate Rights of account holders to exercise	Regulate Duties of the account provider to facilitate the exercise	Refuse to regulate this matter	No answer
A = Rights enshrined in securities	39	45	1	11
B = book entry instructions	44	41	1	12
C = Choice of holding method	44	36	2	14

### 3.4.3 Synthesis:

#### a) Grouping the answers:

- Question 4 expands the content of a minimum harmonization that would consist in the definition of "core functional rights" to the benefit of the account holder. As a consequence, the answers to question 4 can be read in conjunction with question 3:
  - For this purpose, we have distinguished answers favoring the functional approach based on "rights " (the "proponents") and answers criticizing such an approach (the "critics"). The arguments brought by the latter are either that the rights of the holders should be converted into duties of the providers and / or that a distinction should be made between "investors" and "simple account holders".
  - Since these critics do not express a rejection of the legislative project, but only a reversal of the envisaged provisions, we have separated them from the very few respondents that definitely refuse this matter to be regulated.
- The repartition between "proponents" and "critics" is detailed 3 sub-questions addressing respectively (a) the exercise of the rights enshrined into the

securities, (b) the disposal of such securities and (c) the choice of the holding method of the securities. The proposal to crystallize these actions into core "rights of the account holder" implies a separate analysis for each sub-question.

**b) All in all, it is possible to conclude that the traditional opposition observed in the rest of the questionnaire between "supporters" and "critics" is particularly crystallized under question 4:**

- On one side, the supporters stem mostly from the UK and the US, the Benelux, Nordic and central European countries, as well as major European intermediaries associations.
- On the other side, the critics are composed of a well identified bloc of French intermediaries and issuers, German issuers, the German central bank, a German authority, Italian intermediaries and a European issuers association. The higher score of the critics on question 4 was reached by the rallying of German banks associations (except one major German intermediary) and of a European intermediaries association who, although they favor a minimum harmonization under question 3, expressed a position in favor of a "list of duties" approach" with an "investor protection" orientation, which somewhat overcomes the functional approach based on the "account holder-account provider" duality. Many of the critics accompanied their answers with a draft list of duties varying from 4 to 7 points. However the critics expressed by German banks and by the European intermediaries association were not as unconditional as the one expressed by the traditional bloc.

**c) Going further into detail, the answers often vary depending on the three sub-questions:**

(ca) Sub-question (a) proposes recognizing account holders a right to exercise the rights enshrined into the securities.

- Among the 39 answers favoring the "account holders rights" approach :
  - 5 answers suggested leaving the detailed definition of such rights to bilateral or industrial agreements instead of the future directive (mostly Nordic and UK intermediaries). 4 answers asked to extend these rights in order to oblige intermediaries to report to the issuer, consistently with the transparency concerns expressed by issuers in the UK (including a UK stock market, and two UK authorities). This debate between banks and issuers is mostly internal to the "semi-transparent" UK holding system, whereas in fully transparent systems such as the Nordic systems, this debate is already overcome by the CSD holding arrangement. Nordic specificities reemerge under sub-question b and c.

- One may note also that 3 answers out of the 39 answers wish that the definition of account holder refer to the law governing the account relationship rather than to the law of the issuer, which is consistent with their concerns as Scandinavian intermediaries (two Swedish intermediaries associations), more surprising, as concerns VNO, a Dutch issuers association.
  - An Italian CSD insists that the right to exercise rights enshrined into the securities benefit to non EU account holders as well, which reflects the Italian legislation that currently prevents such exercise of rights.
  - A Polish authority, questions the enforceability of such rights in the context of a repo, where the account holder is legally no more the owner of the securities.
- There is nothing very specific to be said about the 44 answers suggesting a reversal of the "core rights approach" into "a core duties approach", except that:
    - A European issuers association is particularly insists on that the law of the issuer actually defines "who" the final investor is.
    - Luxemburg respondents want the concept of investors be recognized solely in the context of sub-question (a), whereas the functional approach would remain valid for sub-questions (b) and (c).

(cb) Sub-question (b) proposes recognizing account holders with a right to instruct the account provider to dispose of the securities

- 44 answers agree with this approach, whereas 39 answers prefer duty for the account provider to prompt on instructions of account holders + 1 "refusal to address this issue in a text on holding of securities".
  - The "proponents" of the functional rights approach did neither argued nor qualified their answer, which is partly linked to sub-question (c).
  - The number of critics has been slightly reduced by the support to the functional approach on this issue expressed by the Luxemburg respondents and the German foreign banks. Otherwise the critics have provided extensive descriptions of what duties would implied under sub-question (b), should the "duty approach" be followed : duty to execute any valid instruction given by the account holder, including the instruction of restitution of securities in case of insolvency, duty to take all necessary care in the custody of the securities registered to securities accounts and duty not to use the securities otherwise than for the benefit of the account holder and upon instruction of the account holder."

(cc) Sub-question (c) proposes recognizing account holders with the right to define the holding method of the securities

- 44 answers agree with this approach, whereas 35 answers prefer duties to be imposed to account providers + 2 "refusals to address this issue in a text on holding of securities".
  - Among the proponents (44) :
    - The UK and US proponents often insisted on the necessity to allow omnibus holding of securities. However, one may note that some UK proponents (a UK authority, and a UK intermediaries association) suggested adding a regime granting the restitution of the securities, a suggestion which could be related to the Lehman case. This proposal was also supported by a Spanish intermediary, at the same time a fervent supporter of the functional approach. The fact that this suggestion is placed under sub-question (c) instead of sub-question (b) suggests that the proponents of the functional approach consider that insolvency rivindications concern mostly sub-custody and or omnibus holding of securities.
    - The Nordic proponents insisted on that transparent systems specificities be taken into account. In particular, they would like that, among "account provider", a clear line be drawn between "transparent CSDs" (acting as legal "depositors") and other intermediaries acting as "service operators".
  - The further reduction of the number of critics (36) stem mostly from the defection of Société Générale and Credit Agricole who seem to consider that some leeway should be conferred to the account provider concerning the holding method of securities, in particular the recourse to sub-custody arrangements.

**In conclusion**, besides the opposition between "proponents" and "critics" of the functional approach, many voices are expressed in favor of the isolation of the function of "investor" among account holders and of "CSDs" among account providers. Besides this, a demand for a right of restitution of securities in the context of sub-custody and omnibus accounts seem to transcend both camps.

### 3.5 Question 5

#### 3.5.1 Question:

**Do you think that a fix set of methods for acquisition and disposition of book-entry securities (crediting an account; debiting an account; earmarking book-entry securities in an account, or earmarking a securities account; removing of such earmarking; concluding a control agreement; concluding an agreement with and in favour of an account provider) should be available to market**

participants throughout all EU jurisdictions? [Yes/No/I don't know; please specify]

**3.5.2 Figures:**

	Yes	Yes subject to conditions	No	No answer
Debit/Credit	45	32	6	16
Ear-marking	29	36	18	16
Control agreement	17	19	47	16

**3.5.3 Synthesis:**

Question 5 addresses one of the core aspects of the functional approach, which concerns the methods actually used to acquire or dispose securities. Question 5 proposes, in accordance with the second LCG report, to limit the book entry methods used in the EU to a "fix set of six methods".

For presentation purposes, we have grouped these six methods into 3 pairs of methods : (1) debit/credit, (2) earmarking and (3) control agreements.

In the table above we have detailed the preference expressed for each of these three pairs of methods by using three notes: Yes, Yes subject to conditions and No.

**(a) The results can be summarized as follows :**

- debit credit methods reach a large agreement : 45 Yes, 32 Yes subject to conditions, 6 No ;
- ear marking methods are more debatable : 29 Yes, 36 Subject to conditions, 18 No ;
- Control agreements are rejected by a large majority: 17 Yes, 19 subject to conditions, 47 No.
- The 11 unconditional "Yes" (for all three groups of methods) were mostly found among UK, US and Nordic respondents.

- The 6 unconditional "No" (for all three groups of methods) were mostly found among German authorities and one German issuer, an ICSD, A French intermediaries association and the Slovenian CSD.

**(b) As concerns the general outcome, one may note:**

- **A clear refusal of control agreements**, especially on the ground that it is not a book entry method, that it is not "transparent" and that it is alien to most MS practices (except perhaps UK). Certain respondents conditioned their acceptance of control agreements to publicity formalities.
- **A strong demand from continental European** countries that ear-marking be limited to collateral operations, and in particular to pledge, in order to avoid any duplication of securities.
- **A strong demand not to limit the list of book entry methods**, either by defining it as a non exclusive list (it seems in particular that other methods are used in the context of SSS, such as pre-matching, matching, flow-collateralization , etc), or by replacing control agreements by other book entry methods currently in use, such as "retention right" or "security interest created by law".
- **A demand for leeway concerning the existence of a direct relationship between the use of the book entry methods and their ultimate consequence: effectiveness.** In particular Spanish respondents have prepared a list of sub conditions rendering debit/credit and ear marking effective (evidence of the interest, irreversibility, disposition). A parallel can be made between these sub-conditions and the so called "perfection conditions" that are authorised under article 1.5 and 3.1 of the FCD.

### **3.6 Question 6**

#### **3.6.1 Question:**

**In the event of not all six methods listed in Question 5 becoming available to market participants in all Member States: do you think that the law of any Member State should recognise, in particular in an insolvency proceeding, acquisitions and dispositions effected by one of these methods under the law of another Member State, even if the law of the first Member State does not provide for that method? [Yes/No/I don't know; please specify]**



### 3.6.2 Figures

Yes mutual recognition among the MS even in case of insolvency <b>of any acquisition/disposition method</b> used in another MS	1
Yes mutual recognition among the MS even in case of insolvency of <b>the six proposed methods of acquisition / disposition methods</b> when used by another MS	44
Yes mutual recognition among the MS even in case of insolvency of <b>four acquisition/disposition method</b> when used in another MS ( <b>no recognition of control agreements</b> )	27
No obligation of mutual recognition in case of insolvency	4
No answer	23

### 3.6.3 Synthesis

Question 6 complements question 5: in case of refusal to enforce a fix set of methods in each Member State, an alternative solution would consist in providing a regime of mutual recognition of these methods among Member States including, in case of bankruptcy, of the account provider conducted under a different law and jurisdiction than the law governing the acquisition of the securities.

#### (a) The results can be summarized as follows :

As for the previous questions, most members wanted either to enlarge or pick out their preferred method of acquisition, therefore we have distinguished four types of responses :

- **1 "Yes"** recognition by the law of the MS of insolvency of acquisition/disposition performed by any methods under the law of another MS
- **48 "Yes"** recognition by the law of the MS of insolvency of acquisition/disposition performed by any of the 3 pairs of methods under the law of another MS
- **27 "Yes"** recognition by the law of the MS of insolvency of acquisition/disposition performed by only the 2 first pairs of methods (debit/credit and earmarking) under the law of another MS
- **4 "No"** obligation of mutual recognition in case of insolvency

**(b) As concerns the general outcome, one may note:**

- The 47 respondents that were counted as proponents of a mutual recognition covering all six methods did not always explicitly mention their wish to include "control agreement" into the mutual recognition. Nevertheless we counted them in this category because they did not express any clear refusal, even though they may have opposed to such an inclusion of "control agreements" under question 5. Therefore, this apparently favorable figure to the mutual recognition of control agreements should be interpreted cautiously.
- The 27 proponents of mutual recognition limited to the two first pairs of methods (excluding control agreements) were mostly recruited among a kernel of German issuers, and of French intermediaries + a German authority, an Italian intermediaries association and the ECB. One of the reasons of the exclusion of control agreements from the mutual recognition is that it currently corresponds to the state of play organized by the FCD and by the WUD which both organize mutual recognition of book entry securities transfers limited to credit/debit and to ear-marking.
- The 4 "no" were counted partly among partisans of a fix set of methods, as proposed under question 5, or among opponents to any mutual recognition.
- One may note that a UK stock market (but also, seemingly, an Italian CSD) suggests that the mutual recognition should contain, as for the SFD, a cut-off time upon which the opening of an insolvency prevents the recognition of any acquisition through whatever method.

### **3.7 Question 7**

#### **3.7.1 Question:**

**Do you think that future legislation should leave to Member States the possibility of making the effectiveness of an acquisition or disposition subject to a condition contractually agreed upon between account holder and account provider, in particular a condition that a corresponding acquisition or disposition occurs? [Yes/No/ I don't know; please specify]**

#### **3.7.2 Analysis**

<b>Yes</b>	<b>22</b>
<b>No</b>	<b>48</b>
<b>Yes and No</b>	<b>11</b>
<b>No opinion</b>	<b>18</b>

### 3.7.3 Synthesis

Question 7 concerns the concept of "effectiveness", that is to say a certain point of time as from which a book entry is enforceable to third parties. It is a very complicated question, since the possibility for contractual leeway left in its implicit proposal opens a gateway to further proposals in different directions by proponents as well as by critics of the functional approach. However, we could sort the respondents into three groups (see table above).

**(a) The results can be summarized as follows:**

- As concerns the **"Yes" group (22 answers)**, it is formed by many supporters of the functional approach who try to streamline the functional approach as much as possible in order to articulate book entry methods with conditions agreed during the trade phase of the operation : their main argument is that many operations are enforceable on a trade date basis or on a conditional basis. In the latter case, ear-marking would be used to identify conditional credits and conditional debits (and would therefore not be limited to the identification of collateralized securities or to set-off).
- As concerns the **"No" group (48 answers)**, it is constituted by many critics of the functional approach who try to push towards a solution of "maximum harmonization" according to which "pure" book entry operations ("debit-credit") would also imply a transfer of ownership. This goes against the definition of functional approach according to which ownership issues should be left to the national legislator. This ownership issue is itself closely linked to the principle "no credit without debit" which is applied in a number of Member States, but does not work in all jurisdictions and was therefore discarded by recommendation 9 of the LCG report concerning "integrity". The principle "no credit-without debit" is particularly stressed as concerns shares, the issuers of which want to avoid situations where more voting rights are expressed than what was actually issued.
- However, not all traditional critics of the functional approach joined the "no" group. In particular German authorities showed some flexibility concerning the issue. One answer based on the German experience, suggested establishing a somewhat indirect connection between book entry and ownership aspects, suggesting that non DVP conditional operations should lead to final operations with transfer of ownership only as from the moment of credit, hence transforming the original "no credit without debit" principle into a "no more credits than debits" principle.

**(b) Among the interesting comments, one may note:**

- Several answers, stemming mostly from Nordic countries as well as from UK firms and European associations, stressed, for legal certainty reasons, on the

necessity to create a single uniform market with no possibility of derogation. Some of them reinforced the "No" group, whereas most of them constituted the bulk of the "Yes-No group".

- Insensitive to such concerns, other respondents argued for the possibility for Member States to derogate in a stricter manner to possible leeway concerning conditional credits and debits, hence implicitly joining the camp of the supporter of derogations.
- Crossing these views, other suggestions were made, such as the necessity to set apart SSS (in particular DVP systems as fostered by CESR recommendation n°19). This concern was expressed by 10 respondents (central banks and CSDs).

### 3.8 Question 8

#### 3.8.1 Question:

**Do you think that there should be a short, harmonised list of conditions giving rise to a reversal of an acquisition or disposition, notably (a) the consent of the account holder; (b) the credit or debit which was made in error; (c) the debit or earmarking or removal of an earmarking which was not authorised. [Yes/No/I don't know, please specify, indicating which one to add/delete, if any]**

#### 3.8.2 Figures

	Yes	Yes and No	No	No answer
a) the consent of the account holder	46	2	36	15
(b) the credit or debit which was made in error	47	2	35	15
(c) the debit or earmarking or removal of an earmarking which was not authorised.	46	2	36	15

#### 3.8.3 Synthesis

Question 8 addresses the possibility of making reversals, by exception to the principle of "effectiveness" reviewed under question 7. The answers to Question 8

are rather difficult to analyze, since they largely depend from answers provided by each respondent to question 7 and to question 4.

**(a) The results can be summarized as follows:**

- On the paper, the positions are shared between a majority of "yes" (45), who favor the regulation of reversal cases and a strong minority of "no" (36).
- However, the analysis of the "no" answers shows that, the latter do not oppose to the principle of reversal but rather oppose to the recourse to regulation to set the cases of reversal.
- As a matter of fact, those who have answered "no" to contractual derogations to the effectiveness of book entries under question have answered "no" to the possibility of reversal under question 8. This is especially the case of the kernel of the "critics" composed of French intermediaries and German issuers. However, their motivations do not push towards a prohibition of reversal, but rather towards leaving this issue to contractual freedom. Hence, most "no" respondents consider that, once a clear list of duties will have been imposed to account providers, in accordance with their "counter-proposition" concerning "a list of duties" set out under question 4, it will not be necessary any more to regulate the conditions for reversal, since it will derive directly from their duty to prompt on any instruction of the account holder to make a reversal and/or to correct "erroneous" as well as "non authorized" book entries. Paradoxically, the supporters of a maximum regulatory approach covering proprietary aspects tend to support a contractual approach, once the question deals with the conditions of execution of transfers.
- As a consequence, the number of real opponents to the possibility of making reversals is very low.

**(b) Interesting comments**

- Two Italian intermediaries, counted among the opponents to reversal, were concerned by the compatibility between the possibility of reversals and the principle of irrevocability of transfer orders in settlement systems, as it is provided by the SFD.
- In the same way, a major concern, expressed, by at least 17 answers, concerns the consequences of a reversal on third-parties, especially the upper tier levels of a holding chain, in particular when these upper tier levels cannot

themselves reverse their book entry due to the irrevocability of book entries in securities settlement systems.

- Such a concern for coherence may, according to certain answers, be accommodated by synchronization rules defining the time limit as from which no reversal will be possible (5 answers). The regulation of reversals should also, according to one answer, encompass third parties from third countries, in order to organize this synchronization in a holding chain with non EU countries.
- Furthermore, two comments expressed concerns with rights of creditors in case of insolvency, since a reversal would incur an impoverishment of the initial beneficiary of the book entry.
- Last, while some qualifications were expressed concerning the definition of "errors" and or of "non authorized" transactions, two German answers suggested extending the cases of reversal to operations considered as null and void by virtue of law, hence introducing the concept of "fraus omnia corrumpit".

All in all, the arguments pointed by most answers are very similar to those invoked to set the limits of the finality and irrevocability concepts in the context of the SFD.

### **3.9 Question 9:**

#### **3.9.1 Question**

**Do you think that account holders in whose favour a credit has been made should be protected against the reversal unless they knew or ought to have known that the credit should not have been made? [Yes/No/I don't know; please specify]**

#### **3.9.2 Figures**

<b>Yes</b>	<b>67</b>
<b>No</b>	<b>13</b>
<b>No answer</b>	<b>19</b>

### 3.9.3 Synthesis

Question 9 addresses the delicate question of the protection of bona fide account holders against reversals.

**(a) The results can be summarized as follows:**

- Respondents answered to question 9 in accordance with the perception of this issue by their jurisdiction of origin. As a matter of fact, almost all of the 67 "yes" answers (supporting the recognition of a bona fide acquisition principle stem from countries that actually recognize bona fide Whereas, most of the 13 "No" answers refusing the recognition of such a principle to warrant book entry acquisition stem from common law countries.
- However there were some notable exceptions, stemming mostly from respondents conducting a European or worldwide activity.

**(b) Interesting comments:**

- Many answers (including among the "yes") seem to confuse the actual scope of a possible "good faith acquisition" principle, since they consider that the good faith principle challenges the right for reversals dealt under question 8. The articulation between effectiveness, reversal and good faith principle should be better explained.
- Some answers, clearly insisted on the necessity that good faith purchases only benefits to third party purchasers, especially in the context of collateralization (a Czech authority, a Danish intermediaries association, Luxembourg and Maltese respondents, a European). Some of them also suggested that good faith be assessed under the auspices of a public authority (Spanish respondents).
- Many answers also supported an "absolute good faith presumption" in favor of purchaser, meaning that good faith presumption should also benefit to purchasers who, due to their profession or to the circumstances, ought to have been aware about a wrongful acquisition. Such a presumption would imply a reversal of the burden of proof at the expense of the vindicating party. Such a presumption is already implicitly provided by the SFD in the context of security settlement systems.

- Though it opposed to the introduction of a good faith principle, a UK authority recognized the usefulness of a text dealing with the burden of proof in the context of SSS, at least as concerns "un-certificated securities" that already benefit from a specific regulation concerning this subject.

### 3.10 Question 10

#### 3.10.1 Question/

**Do you think that interests in book-entry securities, notably security interests, which are "visible" in the account, should have priority over book-entry securities which are not "visible" in the account? [Yes/No/I don't know; please specify]**

#### 3.10.2 Figures

Yes	<b>48</b>
Yes and No	<b>15</b>
No	<b>11</b>
No answer	<b>25</b>

#### 3.10.3 Synthesis

This question is partly linked to question 5 concerning the list of 3 pairs of fixed book entry methods (credit/debit, earmarking and control agreements). Under question 5, many respondents rejected control agreements on the ground that it is not a real book entry method and that it is not visible enough.

Question 10 suggests prioritizing these three pairs of book entry methods in case of competition between liens, implicitly suggesting that the two first pairs would supersede control agreement.

#### **(a) The results can be summarized as follows:**

- As, it can be expected, there is a vast majority (47 yes against 11 no) in favor of such a prioritization, although, many respondents (22) did not answered on the ground that they did not understood the question.



- All in all those who said no to control agreement answered yes to their putting in the back of the priority list, while the supporters of control agreement insisted on their being treated equally.
- However, most of the "yes" (48) and "yes and no" (15) answers were subject to the condition that certain non visible methods of acquisition should always prevail when their origin is a direct effect of law instead of an agreement: this is the case in particular of intermediary's right of lien for unpaid securities, or retention rights which are protective of account providers.

**(b) Interesting comments**

- Among the "no" answers, one may find a detailed argumentation provided by two German authorities according to which the priority should be based on the traditional "first come first serve basis" and that the account should be used as a "deposit" tool and not only as a way to register collateral.
- Several "no" answers also noted that such a prioritization rule might contradict the FCD as well as the current Unidroit negotiations on intermediated securities.

**3.11. Question 11**

**3.11.1 Question:**

**Do you think that there should be a legal obligation for account providers to maintain, for securities of the same description, a number of securities or book-entry securities that corresponds to the aggregate number of book-entry securities of that description credited to the accounts of the account holder's clients plus those securities held for its own account, if any? [Yes/No/I don't know; please specify]**

**3.11.2 Figures:**

Yes	<b>80</b>
Yes and No	<b>2</b>
No	<b>2</b>
No answer	<b>15</b>

### 3.11.3 Synthesis

Question 11 concerning the integrity of the issue is at the same time the most consensual and the most debated question.

#### (a) The results can be summarized as follows:

It is the most consensual, since only 2 respondents answered "no" (a German intermediaries association and an Irish intermediaries association) against 80 "Yes" answers. However this apparent agreement masks rather diverging views.

- On one side 43 respondents (the traditional kernel of critics + German and French authorities, + some Italian, Spanish and Dutch respondents) insisted on the necessity to reach a permanent equation between the number of securities deposited and the number of securities issued at each level of the holding chain, with no possibility of variation. Some respondents required that this goal be reached by a daily reconciliation, whereas other respondents required the application of a "no credit without debit" principle with the systematic recourse to double entry accounting and end-to-end audit trails as recommended by ESCB/CESR rule number 12 which also provides for a periodic assessment by the competent authorities of **Regulatory** and **accounting** standard.
- On the other side, 10 respondents (two ICSDs, another German intermediaries association as well as a Swedish intermediaries association) insisted on the necessity to reach such reconciliation at the upper level, under the auspices of the CSD. One of the underlying arguments is that errors committed by upper tier account providers should not incur the responsibility of lower account providers. The correction of faulty debits and credits would therefore be implemented by the recourse to reversal, which would imply adding a fourth category of reversal to the list set out under question 8. The description by the two UK respondents of the UK reconciliation system at the CREST level could also join this second group of answers.

#### (b) Interesting comments

- Parallel to these arguments, some respondents (at least 8) requested that integrity rules should not deprive the account provider from agreeing with the account holder the possibility to use for its own account securities credited on its account, in particular for securities lending purposes, short selling, hedging and/or contractual settlement.

- Other answers (6) criticized the terms of the equation formulated in the question: in particular, the segregation principle contained under the MIFID prevents from including the securities kept by the account provider for its own account into the balance defined for the integrity of the issue.

### 3.12 Question 12

#### 3.12.1 Question:

**Do you think that, in case of insolvency of the account provider, securities kept by it for its own account shall be attributed to its account holders, as far as the number of securities kept by the account provider for its account holders is insufficient? [Yes/No/I don't know; please specify]**

#### 3.12.2 Figures:

Yes	<b>59</b>
Yes and No	<b>7</b>
No	<b>14</b>
No answer	<b>19</b>

#### 3.12.3 Synthesis:

Question 12, suggesting, in case of shortfall, a direct attribution to Account holders of Account provider's own securities, apparently reaches a certain consensus among respondents, with 58 Yes against 14 No.

However, among the 59 "Yes" answers, 31 answers considered the proposed solution as an ultima ratio solution that should not prejudice the prior application of strict segregation and integrity accounting principles. These respondents are composed of the kernel of "traditional "critics", who supported a full integrity approach under question 11.

Furthermore, 13 answers considered that such a direct attribution should be possible only after having traced responsibility and established a faulty behavior of the account provider. 6 respondents suggested that such an attribution could be better dealt in the context of the Investors Compensation Scheme Directive (which is currently under review) while 1 respondent suggested that it should be dealt consistently with the current Unidroit negotiations on intermediated securities.

19 respondents, including most of the "no" answers, insisted that the final solution would be of a political nature addressing insolvency law as well as securities law, since it requires an arbitration between the interests of the account holders, on one side, and the interests of the creditors, on the other side. The establishment of a faulty behaviour by the account provider might serve as a criterion in favour of a direct attribution, but it would imply a lengthy procedure.

**3.13 Question 13**

**3.13.1 Question**

Do you think that a remaining shortage should be shared amongst account holders of that account provider, in the case of its insolvency? [Yes/No/I don't know; please specify].

**3.13.2 Figures**

<b>Yes</b>	<b>59</b>
<b>Yes and No</b>	<b>11</b>
<b>No</b>	<b>11</b>
<b>No answer</b>	<b>16</b>

**3.13.3 Synthesis**

As for question 12, loss sharing between account holders reaches an apparent consensus of 58 "yes" answers against 11 "no" answers.

- However among these 59, 18 answers (mostly German issuers) suggested that the loss sharing is calculated on the basis of the sole securities kept by the account provider for its own account, which corresponds, in practice, to the direct attribution solution suggested under question 12. Therefore the loss sharing solution is, in its full understanding, supported by 40 respondents.
- Most of the latter 40 respondents, insisted that this loss sharing solution be put at the very end of the different recovery solutions. Four respondents even proposed an order of succession in four steps of the different recovery solution consisting in (1) first, addressing loss to party that has caused the loss, (2) recovering from account providers own assets, insurances, guarantees and other similar means, (3) having recourse to possible common guarantee funds (funded jointly by all account providers), and (4) having recourse to loss

sharing amongst account holders. Some diverging views were expressed concerning, under step (1), the identification of account providers (but also, possibly account holders) responsible for the shortfall.

- Furthermore, 24 respondents (mostly French intermediaries and issuers) insisted that such ex-post recovery procedures do not hamper the prior establishment of an ex ante duty of integrity as suggested under question 11.
- Several respondents insisted again, on the necessity to deal this issue either in the context of the Investor Compensation Scheme Directive (ICSD) or in the broader context of insolvency law, whereas two answers dealt with the question of sharing responsibility between account providers in the context of sub-custody : The first one (a Dutch authority) suggested creating a kind of solidarity between account providers of a same holding chain in favour of the ultimate account holder, whereas the second one, insisted that no such solidarity is established, and that the liability of the lower tier depositor be limited to reasonable care in choosing the sub custodian.

### 3.14 Question 14

#### 3.14.1 Question

**Have you encountered difficulties in the application of the legal framework regarding holding and disposition of book-entry securities that could be fully or partially attributed to an unsatisfactory conflict-of-laws regime? [Yes/No/I don't know; if yes, please specify the difficulties]**

#### 3.14.2 Figures

Yes we have encountered difficulties	<b>32</b>
No we have not encountered difficulties	<b>43</b>
We do not know because we are not practitioners	<b>10</b>
No answer	<b>14</b>

### 3.14.3 Synthesis

This question 14 relates to difficulties encountered in the application of a legal framework and primarily addresses practitioners. Generally, the answers may fall into three groups:

- Group 1: Practitioners that have encountered difficulties (32)
- Group 2: Practitioners that have not and (43)
- Group 3: Other parties which cannot tell because they are not practitioners (10).

Beyond actually answering the question, many respondents communicated their general agreement or disagreement with the existing conflict-of-laws regime. Most of those who feel comfortable with the current regime are in Group 2, whereas those who feel unease are in Group 1.

Within Group 1, most replies were rather general. Some of the more elaborate answers did not provide details but rather general statements (e.g.: Yes, there are difficulties, because the existing rules are not appropriate) and comments on how important a common rule is and how it should look like.

Among the few answers that went more into details, it was stressed that differences in implementation and interpretation of the existing *acquis* remained and that the limited personal and material scope of the *acquis* had not yet yielded a fully satisfactory legal environment, especially for the provision of collateral. The limited and slow advancement of CSD links was partly attributed to the uncertainty on both the law applicable to such cross-border holdings and the applicable substantive law as such.

Within Group 2, a large number cited as reasons for the absence of difficulties the well-functioning of the current legal framework of the Community *acquis*.

### 3.15 Question 15

#### 3.15.1 Question:

**Do you think that future legislation on the legal framework of book-entry securities holding and disposition should harmonise issues of substantive law as well as the question of which law is applicable to holding and disposition of book-entry securities, including the creation of security interests? [Yes/No/I don't know; if yes, please specify]**

### 3.15.2 Figures:

<b>Group 1: In favour of a European conflict-of-law rule</b>	<b>76</b>
a) Preference for issuer's law	4
b) Location rule, more elaborate than the current one	39
c) Contractual freedom close to Hague Convention	9
d) No preference expressed	24
<b>Group 2: Against a European conflict-of-law rule</b>	<b>12</b>
e) Contractual freedom by ratification of The Hague convention	6
f) The current location rule	6
<b>Group 3: No answer</b>	<b>11</b>

### 3.15.3 Synthesis

This question inquires into respondents' view whether a future legal instrument should contain both harmonization of substantive law and a conflict-of-law rule. The answers to the questions can be put into three different groups:<sup>11</sup>

- Group 1: In favor of a European conflict-of-law rule (76)
- Group 2: Against a European conflict-of-law rule (12)
- Group 3: No answer (11).

**Group 1:** many respondents specified reasons for their approval and gave their opinion as to how a future conflict-of-laws rule should look like. Here, one could identify three different approaches:

- a) Preference for issuer's law (4)
- b) Location rule, more elaborate (39)

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<sup>11</sup> While most respondents who fall within Group 1 will have answered Question 15 with "yes", a few of them who answered with "no" nevertheless belong into that category as the reason for the negative answer was not an opposition against a conflict-of-laws rule as such, but against the simultaneous passing of a conflict-of-laws rule and harmonization of substantive law.

c) Contractual freedom close to Hague Convention (9)

**Group 2:** most respondents in this Group had similar motives as the respondents in Group 1 c). They expressed their opposition to a European "Sonderweg" away from the rule of the Hague Convention (2 e). Quite to the contrary, others opposed to a conflict-of-law rule because they regard the current PRIMA regime of the SFD/FCD/WUD as being sufficient (2 f):

e) Contractual freedom by ratification of The Hague convention (6)

f) The current location rule (6).

### **3.15bis      Question 15bis**

#### **3.15bis.1      Question:**

**If yes: do you think that a uniform conflict-of-laws rule should govern the issues within the scope of the Settlement Finality Directive, the Directive on Winding-Up of Credit Institutions and the Financial Collateral Directive plus the aspects which are to-date not included in the scope of the three directives? [Yes/No/I don't know; if yes, please specify]**

#### **3.15bis.2      Figures:**

<b>In favor of a general rule</b>	<b>70</b>
<b>Against a general rule or not sure</b>	<b>6</b>
<b>No answer</b>	<b>23</b>

#### **3.15bis.3      Synthesis:**

The question goes into more detail as to the scope of a possible conflict-of-laws rule in the new legal instrument, namely if it should be a general rule also encompassing the specific conflict-of-laws rules in the SFD/WUD/FCD. The answers can be grouped as follows.

- Group 1: In favour of a general rule (70)
- Group 2: Against a general rule or not sure (6)
- Group 3: No answer (21).



**Group 1:**

Some respondents favoured a uniform comprehensive conflicts-of-law regime for all holdings and dispositions of book entry securities since financial market infrastructure could no longer only be addressed in a way limited to individual subject matters or entities, as currently addressed by the three EC directives mentioned in question 15.

Some respondents also indicated their preferences as to how such a rule should look like. In this case, the answers reflect the tendencies already expressed in the responses to Question 15 (Location criteria versus Contractual freedom). If respondents favoured a general application of the current Location criteria rule, they sometimes indicated how such a rule should look like (e.g. containing a "black list" containing elements which do not sufficiently qualify as constituting the location of the security).

**Group 2:** Reasons cited by some respondents against a general rule were the sufficiency of the existing legal framework. For matters outside the scope of the three directives, some favoured the introduction of a conflict-of-laws rule pointing to the issuer law. Another reason for opposing a general rule was the need for further investigation into the appropriateness of a "one-size-fits-all" approach.

**3.16 Question 16**

**3.16.1 Question**

**Do you think that holding and disposition of book-entry securities is more costly in cases where the situation involves a cross-jurisdictional element?  
[Yes/No/I don't know; please specify]**

**3.16.2 Figures**

	<b>Total</b>	Intermediaries	Investors & issuers	Others	Authorities
Yes or probably yes	<b>40</b>	19	4	12	5
No or slightly yes	<b>35</b>	13	18	2	2
No answers	<b>24</b>	7	5	1	11

### 3.16.3 Synthesis

This question 16 concludes chapter 1 of the questionnaire and tries to assess the costs incurred by legal uncertainty covered by questions 1 to question 15bis (Giovannini barrier 13). It can be paralleled with questions 2, 26 and 30 of the questionnaire concerning respectively the complexity of cross border operations and the costs incurred by corporate action processing (Giovannini barrier 3) and by impediments to cross-border issuance (Giovannini barrier 9).

Since most of the answers to question 16 were neither “Yes” nor “No”, but rather “probably yes”, “surely yes”, “we guess yes”, “it could be slightly more”, “we don’t know”, or “no answer”, we shared the respondents into two groups : a first group observing a definite increase of the costs (“yes or probably yes, surely yes, we guess yes”) and a second group tending to minor the costs (“slightly more” or “no”).

The first group leads by 40 and is mostly constituted by Anglo-American, Nordic and European wide intermediaries associations. The second group (35 answers) is mostly represented by the kernel of critics constituted by German issuers and by French intermediaries.

In the first group, the supposedly sharp increase of the costs is felt by the intermediaries more than by the issuers and by the investors. The second group could have been larger, if some “Yes” responding issuers had not confused question 16 with question 26 concerning costs incurred by corporate actions. A small majority of the first group is constituted by intermediaries (19 out of 40), from which one might infer that costs incurred by a non harmonised book entry legislation are specific to intermediaries, although French intermediaries tend to negate the existence of such costs. Indeed, as we will see under question 16bis, most of the costs acknowledged by the first group under question 16 concern the excess of book entry regulation of certain EU Member States.

#### 3.16bis Question 16 bis

#### 3.16bis Question:

**If yes [to question 16] , could you give your best estimate of the additional cost and specify what types of cost arise?**

**3.16bis Figures:**

	Yes “emphasising” costs group	No or minor costs group	Total comments
Legal costs associated with book entry securities	18	2	20
Legal costs associated with regulatory and tax procedures	13	0	13
Operational costs associated with book entry infrastructures (absence of CSD, multiple chain of AP)	19	2	21
Operational and legal costs for investors	1	32	33
Figures	8	0	8
No answer to question 16bis	8		

**3.16bis Synthesis:**

Question 16bis addresses those who answered “yes” to question 16. However, many respondents from the second group (tending to minor or to negate the existence of additional costs) answered to question 16bis as well, mostly in order to point towards other costs stemming from obstacles to corporate actions rather than from obstacles to book entry transfers.

However, even among respondents from the first “yes” group, only a small half provided examples of costs directly linked to the non harmonisation of book entry transfers (18 examples out of 40 “yes” answers), highlighted in green in the table below). The other half either did not provided examples (8 out of 40 “yes” answers) or provided examples connected to tax barriers (barriers 11 and 12) and or to other fields of law, such as company law and registration procedures. A stronger group (19 out of 40 yes answers) pointed out infrastructure obstacles such as the absence of compulsory CSDs and multiple chain of intermediaries (operational barriers and perhaps also barrier 9), implicitly calling for a legislative instrument on this issue.

As concerns figures, only 8 answers addressed the issue. Estimation varied from an increase of 10% due specifically to legal obstacles to book entry transfers (a German intermediaries association) to 100% (a Spanish law firm), while a UK Bank characterised this increase of costs as “non negligible”. Only a UK intermediaries association estimated the increase of associated costs “up to 500%”, while it is not certain whether this concerns only legal costs associated with barrier 13 or other costs associated with the other Giovannini barriers.

Several answers also invited the Commission to refer to the Oxera report, as well as to the ECB report on the impact of T2S, which again shows confusion between purely legal costs incurred by barrier 13 and costs associated with other barriers.

### **Processing of rights flowing from securities**

The purpose of questions 17 to 25 is to assess the appropriateness of a legislation tackling the legal aspects of Giovannini barrier 3, concerning the difficulty to exercise rights flowing from securities.

#### **3.17 Question 17**

##### **3.17 Question**

**Do you think that investors face difficulties in exercising rights flowing from securities as soon as they hold through a cross-border holding chain? [Yes, considerable difficulties/Yes, slightly more difficulties than in a domestic context/No/I don't know, if yes, please specify the difficulties]**

##### **3.17 Figures**

Yes considerable difficulties	61
Yes slightly more difficulties	
No difficulties	4
No answer or no info	34

### 3.17 Analysis

- An overwhelming majority of respondents (61) indicated that investors face difficulties in exercising rights flowing from securities as soon as they hold through a cross-border holding chain. Only four negative answers have been received: these highlight that the Law is clear and indicate that it is not regulatory or legal obstacles but rather the way investors have set up their shareholding management that create inefficiencies.
- Most of the answers mentioned some examples of encountered problems, but not necessarily related to the exercise of rights flowing from securities (barrier 3). Besides, issues related to general meetings, the most frequently mentioned problems were related to tax issues (Giovannini barriers 11 and 12). The need for conflict-of-laws rules was also mentioned several times. Finally, language problems and issues with omnibus accounts were also quoted.

### 3.18 Question 18:

#### 3.18.1 Question

**Do you think that the law of Member States should bind account providers to facilitate the exercise of rights flowing from the securities (e.g. by providing the investor, upon demand, with a certificate confirming his holdings; or, by making the investor the account provider's representative with respect to the exercise of the relevant rights {proxy}), where the exercise of rights would be impossible or cumbersome without the assistance of the account provider? [Yes/No/I don't know; please specify]**

#### 3.18.2 Figures

Yes	56
No	17
Yes & No	2
No answer	24

#### 3.18.3 Analysis

- Regarding the need to oblige account providers to facilitate the exercise of rights flowing from the securities, a majority of respondents (56) were in favour

of adding such obligation for account providers. Indeed in many cases, mainly related to corporate actions, general meetings as well as tax-related issues, respondents considered the help of account providers as absolutely required.

- However, whatever their answer, the majority are in favour of letting this issue solved by service level agreements (SLA). Indeed in some cases – as for example for Tax issues (though not directly related to rights stemming from securities) – a compulsory help from the account provider would be impossible to implement. The costs related to such additional tasks are also often indicated in support of the contractual solution.
- The answers do not provide a clear indication that there is a need to add a new legal obligation. In any case such obligation should be softened by the possibility to limit its scope by SLA.

### 3.19 Question 19

#### 3.19.1 Question:

**Do you know other cases where assistance of the account provider is a prerequisite for the exercise of the right by the investor? [Yes/No/I don't know; if yes, please specify]**

#### 3.19.2 Figures:

Yes	57
No	8
I don't know	3
No answer	31

#### 3.19.3 Analysis

- A majority [59] of the answers quote other cases where the assistance of the account provider is needed.

- Most of the reported cases are: Corporate actions (cf. reorganisations); general meetings (cf. nominee in SW&FI) & Tax issues (tax relief). Insolvency proceedings were also quoted.

### 3.20 Question 20

#### 3.20.1 Question

**Do you think that Member States' law should make possible the exercise of rights flowing from securities by an account provider on behalf of the investor where the exercise of the rights by the investor himself is impossible? [Yes/No/I don't know; please specify]**

#### 3.20.2 Figures

Yes	35
No	40
Yes & No	4
No answer	20

#### 3.20.3 Analysis

- As concerns the proposal to make possible the exercise of rights flowing from securities by an account provider on behalf of the investor, half of the respondents (35 + 4 = 39) were in favour of this possibility as it was seen as a way to enhance transparency. However, most of them proposed to limit this to cases where clear instruction/authorisation from the investor had been granted, and preferably through a SLA, rather than subject to the condition of feasibility.
- The other half, (40 opponents to this possibility) consider it as unnecessary as there is an existing proxy system which reaches the same results (reference to rule 452/NYSE for example). In any case, the idea of a general mandate was generally rejected.

### 3.20bis Question 20bis

#### 3.20bis.1 Question

In the affirmative case, do you think that this possibility should be subject

(a) to feasibility on the side of the account provider [Yes/No/ I don't know, please specify, in particular, the exact scope of such feasibility exemption], and/or

(b) to contractually agreed levels of service between the account holder and the account provider? [Yes/No,/ I don't know, please specify].

#### 3.20bis.2 Figures

<b>Yes</b>	<b>34</b>
Without any preference	4
Supporting options a and b	9
Supporting options a only	0
Supporting option b only	21
<b>No to any two options</b>	<b>6</b>
No answer	22

#### 3.20bis.3 Analysis:

- Note that there are more respondents than those who actually responded "yes" to question 21
- A majority of the respondents are in favour of a limitation by contract (option b). Moreover all those who have chosen option a have also chosen option b. There are some questioning the exact scope of the term "feasibility" reason why in some cases this option a has not been chosen (+/-1/3 of the cases).
- Opponent considers there should not be any restriction to this due to the need for rights being exercised.



### 3.21 Question 21

#### 3.21.1 Question

**Do you think that Member States' law should make possible the exercise of rights flowing from securities by an account provider on behalf of the investor, in a scenario where the investor does not want to exercise the rights himself? [Yes/No/I don't know; please specify]**

#### 3.21.2 Figures:

Yes	16
Yes and no	5
No	56
No answer	22

#### 3.21.3 Analysis:

- In the case where the investor has already renounced exercising its rights himself (especially voting rights), the opposition to any automatic representation by the account provider was even stronger (56 "no" to question 21), unless it is backed by a SLA with the Account Holder. The respondents, whether intermediaries or issuers, do not want this to be subject to feasibility (question 21 bis).
- However part of the opponents and most of the supporters do consider this as being acceptable if the investor has allowed so (upon instruction or consent given or contractually agreed).
- Even the supporters consider that this feature cannot obstacle the exercise of the rights by the investor himself.

### 3.21bis Question 21bis

#### 3.21bis.1 Question:

In the affirmative case, do you think that this possibility should be subject:

(a) to feasibility on the side of the account provider [Yes/No/ I don't know, please specify, in particular the exact scope of such feasibility exemption], and/or

(b) to contractually agreed levels of service between the account holder and the account provider? [Yes/No/I don't know; please specify].

#### 3.21bis.2 Figures:

<b>Yes</b>	<b>25</b>
Supporting options a	9
Supporting option b	23
Without no preference expressed	2
<b>Yes and no with no option supported</b>	<b>1</b>
<b>No to any two options</b>	<b>2</b>

#### 3.21bis.3 Analysis:

- Note that there are more respondents than those who actually responded "yes" to question 21
- A majority of the respondents are in favour of a limitation by contract (option b). Moreover all those who have chosen option a have also chosen option (b).
- Some respondents questioned the exact scope of the term "feasibility", which explains why, in some cases, this option (a) has not been chosen.
- Many of those who did not answered question 21bis, mentioned however that there should not be any restriction to the possibility for an account provider to exercise rights flowing from securities on behalf of the investor, on the ground that such rights should be exercised whatever it costs.

- Conclusion : Clear indication among those who favours such a limitation in favour of option b, which converge with the mainstream's view provided under question n°20

### 3.22 Question 22

#### 3.22.1 Question

Do you think that an account provider should be bound to exercise, on behalf of the investor, the following rights flowing from securities:

(a) Rights entailing a change of the relevant security itself (e.g. conversions, reorganisation) [Yes/No/I don't know; please specify];

(b) Collection of dividends or other payments and subscription rights [Yes/No/I don't know; please specify];

(c) Acceptance or refusal of takeover bids and other purchase offers? [Yes/No/I don't know; please specify];

(d) Other rights [please specify which and why]

#### 3.22.2 Figures

<b>Yes</b>	<b>51</b>
Supporting option a	38
Supporting option b	22
Supporting option c	13
Supporting option d	1
Without no preference expressed	8
<b>No to any four options</b>	<b>26</b>
<b>No answer</b>	<b>22</b>

#### 3.22.3 Analysis

- In the case of "pecuniary rights", only 26 answers (mostly French, German and UK intermediaries) rejected any obligation of compulsory exercise by the Account Provider on behalf of its account holder, while 46 answers supported

this obligation, at least for the exercise of conversion or reorganisation rights (option a).

- As concerns "*the collection of dividends or other payment and subscription*" (option b), 30 answers supported such a compulsory exercise, while the support for an obligation to "*accept or refuse take over bids*" dropped to 20 positive answers. One may note however that, among the opponents, as well as among the supporters of such duties, one finds a majority considering that, in the case of pecuniary rights, the account provider should only be obliged to act in the best interest of the investor even without express consent of the latter. The main reason mentioned for this, is the need to preserve the economic value of the securities and the rights attached thereto.

### 3.23 Question 23

#### 3.23.1 Question:

**Do you think that account providers should be bound to pass on information with respect to book-entry securities which is required in order to exercise a right enshrined in the securities which exists against the issuer? [Yes/No/I don't know; please specify];**

#### 3.23.2 Figures:

Yes	73
Yes and no	1
No	7
No answer	18

#### 3.23.3 Analysis

- A vast majority of the respondents (73) was in favour of the account providers' obligation of passing on information with respect to book-entry securities which is required in order to exercise a right enshrined in the securities which exists against the issuer. However, most of them consider this obligation should be limited:

- The limits should result either from a SLA or should be subject to the principle that this new obligation should not impose additional costs to the account providers or to the issuer (2/3 of the answers).
  - Also some consider that this obligation cannot go beyond an obligation of "best effort" and certainly not oblige the account provider to take additional duties like retrieving information (question 23).
  - Another limit also often quoted was that the information to be transmitted should be directly linked to the security held (avoiding general information about the issuer) and that no such obligation should be imposed if the issuer had decided to provide the information by other channels.
- there is a clear indication here. This possibility, if put in place, could be limited by SLA & should be intrinsically related to the security investors consent.

### 3.24 Question 24

#### 3.24.1 Question:

**Do you think that this obligation should be restricted to information :**

**(a) which is received "through the holding chain", (i.e. directly either from the issuer or an account provider which maintains an account for the account provider in question, or from the investor or another account provider for which the account provider in question maintains an account.) [Yes/No/I don't know; please specify];**

**(b) which is directed to all investors in securities of that description [Yes/No/I don't know; please specify]?**

#### 3.24.2 Figures:

<b>Yes</b>	<b>61</b>
Supporting option a	50
Supporting option b	15
Without no preference expressed	11
<b>Yes and no with no option supported</b>	<b>2</b>
<b>No to any two options</b>	<b>4</b>
<b>No answer</b>	<b>22</b>

**3.24.3 Analysis**

- All in all, a majority 50 of the respondents was in favour of limiting passing down to the sole information which is received through the holding chain. Two respondents even limited this to the strict information forwarded by the issuer (or affiliates) and not to additional information that could be put in the chain by upper tier account providers.
- Only a few respondents opposed to this obligation to transmit information, most of them as a matter of principle.
- there is a clear indication in favour of option (a), which is consistent with the answers provided question n°23

**3.25 Question 25**

**Would you advise other/additional restrictions to this duty? [Please specify]**

**3.25.1 Question**

**3.25.2 Figures**

Yes	15
Yes and no	1
No	41
No answer	42

**3.25.3 Analysis**

- A majority of the respondents do not advise any additional restriction.
- Among the few positive answers, a strong link information/security is often quoted. Some would also like limiting this transfer of information to corporate actions (both are also indicated in questions 23 & 24). One respondent proposes a materiality test in which the balance between the costs of the

information for the provider and the relevance for the investor/the security is assessed.

### **Free choice of initial entry of securities**

The purpose of questions 26 to 30 bis is to assess the appropriateness of a legislation tackling Giovannini barrier 9 concerning the (legal) restrictions to the location of initial entry of securities.

#### **3.26 Question 26**

##### **3.26.1 Question:**

**Do you think that the processing of rights flowing from securities is more costly in case where the situation involves a cross-jurisdictional element?  
[Yes/No/I don't know]**

##### **3.26.2 Figures:**

Yes	61
Yes and no	1
No	12
No answer	23

##### **3.26.3 Analysis:**

- A huge majority 61 of the respondents (issuers/investors as well as intermediaries), considered that there are additional costs related to cross-border situations in case of need for information, as well as when trying to exercise the rights enshrined in securities. The reasons provided were the increased complexity – linked to the chosen legal structure -, the language, tax issues and the operational risks incurred. A UK intermediary considered that there are two basic reasons for these additional costs: the non-recognition of the concept of "nominee" and the requirement for paper documentation.

- Among the few negative answers, the reasons for possible increase in costs are seen to be related to the implementation of new obligation related to cross-border situations.

### **3.26bis Question 26bis**

#### **3.26bis.1 Question**

**If yes, could you give your best estimate of the additional cost and specify what types of cost arise?**

#### **3.26bis.2 Figures**

23 answers providing estimates of the over cost in cross-border corporate actions, ranging from:

- "insignificant increase" (an Irish intermediaries association)
- "slightly more costly"
- 30% higher for wholesale trades and 150% higher for retails trades (ICSD)
- "for General Meetings from 200 to 300% more" (18 German issuers)
- "minimum 500% more"
- "dozen times more" (a Polish CSD).

#### **3.26bis.3 Analysis:**

- Only a few respondents provided estimates of these additional costs, usually high level ones; estimates ranged from "slightly more costly" to "a dozen times more. One respondent quoted Clearstream's White Paper of 2002, where it is estimated that the cross-border costs is 30% higher for wholesale trades and 150% higher for retails trades than for domestic trades.
- A UK Intermediary considers that there are two basic reasons for these additional costs: the non-recognition of the concept of "nominee" and the requirement for paper documentation.



### 3.27 Question 27

#### 3.27.1 Question:

**Do you think that an issuer incorporated under the law of an EU Member State should be allowed to arrange for its securities to be initially entered into holding and settlement structures (in particular those maintained by a central securities depository) in, or governed by the law of, another EU Member State? [Yes/No/I don't know; please specify]**

#### 3.27.2 Figures:

Yes	55
Yes and no	14
No	13
No answer	17

#### 3.27.3 Analysis:

- On this question concerning the "exportability" of issuances to a foreign CSD, an overwhelming majority of respondents supports the proposal of having the free choice on initial entries (55 "yes"). This is seen as a major step towards improving both the rationalisation and harmonisation of the European post-trade framework. This is seen as a result of the freedom of movement of capital and a way to facilitate the financial needs of companies.
- Opponents consider this issue is closely related to corporate law and it is thus not feasible to have choice within 2 different legal frames. Moreover this would make the exercise of rights more complicated according to them. Scandinavian respondents have indicated the need to take the specificities of the Nordic CSDs framework (individual access to CSDs).
- Scandinavian answerers have indicated the need to take the specificities of the Nordic CSDs framework (individual access to CSDs).
- One stock exchange proposes to make a clear distinction between holding and settlement (out of scope as competition and free choice already exist). Within holding structure they propose to distinguish between fixed income

securities (free choice exists in IT) and equities. It considers that such new possibility should be accompanied by a level playing field among all actors in all countries and the need to achieve a right balance between this choice and the related costs it triggers.

- One ICSD indicated that for commercial reasons CSDs should be able to refuse/deny to grant access – e.g. no compulsory acceptance in cross-border cases. And lots of detailed questions are indicated (quid in case of multi-location issuances; possibility to pool all securities (new and existing) from an issuer into one single CSD; ...).
- Hence, exportability of issuances is seen as acceptable but many insist on the need for prior harmonisation (corporate law, tax) & there is a strong unanimity of German and French answerers on the need for the prerequisite on "the integrity".

### 3.28 Question 28

#### 3.28.1 Question:

**Do you think that holding and settlement structures for securities, in particular those maintained by a Central Securities Depository, which are governed by the law of an EU Member State, should be open for securities constituted under the law of another EU Member State? [Yes/No/I don't know; please specify]**

#### 3.28.2 Figures

Yes	58
Yes and no	6
No	5
No answer	30

#### 3.28.3 Analysis

- Here again, on this question concerning "importability" of issuances by CSDs, an overwhelming majority is in favour of allowing that holding and settlement

structures for securities which are governed by the law of an EU Member State are open for securities constituted under the law of another EU Member State (58 "yes").

- It is seen as a major step towards improvement of both the rationalization and harmonisation of the European post-trade framework.
- The opponents argue that this will create major issues as different laws will have to be applied and there is no European harmonisation of corporate Law matter to which this is intrinsically linked
- The expected impact on costs is also pointed out regularly: all the answers indicate that this should let some decrease in costs. One of "no" respondents bases his answer on the expectation that cross-border initiatives as T2S will lead to a decrease of costs and be more efficient than the proposed change. Many abstaining answers is also based on the fact that they believe interoperability agreements and T2S initiatives will more easily reach the same results.
- Hence, there is a clear indication that there is a need to allow importability of issuances.

### 3.29 Question 29

#### 3.29.1 Question:

**Are there, in your view, issues stemming from other branches of law, such as corporate law, fiscal law, etc., or regulatory/supervisory concerns that could advise against the establishment of free choice by an issuer, as set out above. [Yes/No/I don't know; if yes, please specify the issues]**

#### 3.29.2 Figures:

Yes	29
No	27
Don't know	3
No answer	40

### 3.29.3 Analysis:

- A small majority (29) of the respondents does consider that there exist other issues which need to be solved previously ;
- These prerequisites can be listed as follows:
  - Most of them quote the need for harmonising corporate and tax law. Within corporate law the mandatory dematerialised regimes are most often quoted. A few respondents added the ISIN requirements, registration and insolvency law. Other respondents indicated that some problems could stem from consumer protection legislation. Others had doubts on the competence and the location of the regulatory body in such cross-border cases.
  - Part of the respondents (mainly German and French) considered that there is a fundamental prerequisite: the need to ascertain the integrity of the issue (split of a same issue between different CSDs should not be allowed).
  - One respondent proposed to make a clear distinction between holding and settlement. Within holding structure, they propose distinguishing between equities and fixed income securities. They consider that such new possibility should be accompanied by a level playing field among all actors in all countries and the need to achieve a right balance between this choice and the related costs it triggers.

### 3.30 Question 30

#### 3. 30.1 Question:

**Do you at present incur additional cost because either or both of the above possibilities of choice do not exist? [Yes/No/I don't know/Not applicable]**

#### 3. 30.2 Figures:

Yes	12
No	30
Don't know	8
Not applicable	4
No answer	45

### **3. 30.3 Analysis:**

- As concerns the additional costs currently incurred because either or These prerequisites can be listed as follows:

#### **3.30bis Question 30 bis**

##### **3. 30 bis.1 Question**

**If yes, could you give your best estimate of the additional cost and specify what types of cost arise?**

##### **3. 30 bis.2 Figures**

Very few answers with figures. However some made their best estimates ranging from :

- (UK intermediaries) "minimum 500% more".
- (Polish CSD) "dozen times more")

##### **3. 30 bis.3 Analysis**

- Besides, the above mentioned figure, an ICSD provides an extensive overview of the costs incurred: they are related to access and interoperability and to the need for IT systems being maintained in a foreign location.
- However the lack of figures renders the answers non conclusive.

## **Duties of account providers**

The purpose of question 31 to 32 bis is to assess the appropriateness of a regulation of the profession of account providers, due to their core role in the dismantling of Giovannini barriers 13, 3 and 9.

### **3.31 Question 31**

#### **3. 31.1 Question**

**Do you think that all providers of securities accounts established in the EU should be subject to authorisation and supervision in relation to their services of maintaining securities accounts? [Yes/No/I don't know; please specify]**

#### **3. 31.2 Figures**

Yes	82
No	2
No answer	15

#### **3. 31.3 Analysis**

- As concerns the kind and level of supervision to which account holders should be subject to, a huge majority of the respondents (82) do consider that it should apply to all account providers without any kind of exemption.
- The two negative answers proposed to let this being regulated by Member States Law, after having completed a costs/benefits analysis.

### **3.31bis Question 31 bis**

#### **3.31bis.1 Question**

**If no, which account providers should not be subject to authorisation and supervision by competent authorities? [Please designate the type of account provider and specify why.]**

### 3.31bis.2 Figures

Only two answers, since there were only two "no" answers under question 31. These answers contain only qualitative information to be provided in the "qualitative report".

### 3.31bis.3 Analysis

- Only two respondents have answered negatively to question 31:
- A European post market infrastructures association does not think that there should be any exemptions to the authorisation and supervisory regime, in line with its belief in functional regulation : *"In addition, any definitions of account providers that are drawn up by the Commission must encompass both direct and indirect holding markets without requiring market structure changes in these markets"*.
- A Czech authority considers that Member State law should stipulate which account providers should not be subject to authorisation and supervision, if Member States consider doing so.

## 3.32 Question 32

### 3. 32.1 Question:

**Do you think that the service of safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash/collateral management (which is a so-called ancillary service under MiFID) should be made an investment service in the sense of MiFID (i.e. inserted in Section A of Annex I of the MiFID and be deleted from Section B)? [Yes/No/I don't know; please specify]**

### 3. 32.2 Figures:

Yes	55
No	22
Yes and no	3
No answer	19

### 3. 32.3 Analysis:

- Regarding the kind of instrument needed to achieve this, a strong majority of respondents (55) favoured a solution amending the MIFID rather than having a separate legal instrument.
- However, within this mainstream, many answers argue that MIFID cannot apply as such to the accounts providers and that the amount of changes it conveys might justify putting it into an "ad hoc" separate Legislative Act. Some respondents also consider that there is a need to exclude direct holding from the application of MIFID.
- As concerns the opponents to amending MIFID, the two most often quoted reasons are (1) the difference in scope of application of the MIFID and (2) the creation of additional costs.. From the negative answers, it appears that a separate act seems more appropriate, due to difference in scope. Others (2 answers) propose inserting this into the banking regulation instead.

### 3.32bis Question 32 bis

#### 3.32bis.1 Question:

**If yes, do you see any specific difficulties in including certain types of account provider in the full or even a limited scope of MiFID? [Yes/No/I don't know; if yes, please specify the difficulties]**

#### 3.32bis.2 Figures:

Yes	4
No	21
No answer	74

#### 3.32bis.3 Analysis:

- Most of the respondents consider there are no difficulties including certain types of account provider in the full or even a limited scope of MiFID.



- The only four positive answers focus on the risk of having different players regulated differently. According to one of them, *"the problem is that there are different classes of operating account providers that may currently, at the EU level, either be separately regulated (e.g., banks), or also not be regulated as such ( e.g. central securities depositories). For them, It is of paramount importance that there should be a uniform set of harmonized regulatory/supervisory conditions for account providers in a pan European market so as to ensure a level playing field as a pre requisite for inclusion of account provision services within the scope of MIFID."*

