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The European Commission
DG Internal Marker
Directorate Financial Services Policy and Financial Markets,
Financial Market Infrastructure Unit

Stockholm 2011-01-21

European Commission (EC) Consultation of November 2010 on legislation on legal certainty of securities holding and dispositions

The Swedish Securities Dealers Association (SSDA, register id 7777147632-40) represents the common interest of banks and investment firms active on the Swedish securities market. The mission of SSDA is the maintaining of a sound, strong and efficient securities market in Sweden. SSDA promotes members' views with regard to regulatory, market and infrastructure related issues. It also provides a neutral forum for discussing and exchanging views on matters which are of common interest to its members.

SSDA has a close cooperation with other trade associations in Sweden, the Nordic area and Europe.

General remarks

Financial markets today are global and all large financial institutions are active in one way or another outside the Union. *The Geneva Securities Convention* will promote legal certainty and economic efficiency with respect to cross-border holdings and dispositions of securities held with an intermediary. In our firm opinion it is extremely important to achieve global compatibility regarding the substantive law of securities dispositions. It must be in the interest of EU as global financial market to implement legislation fully compatible with the Convention.

Furthermore, we have for a long time been very concerned about the lack of progress regarding *the conflict of laws issue*. There is still in the EU no uniform conflict of laws rule that governs issues of crucial practical importance for holdings and dispositions of securities held by an intermediary. Uncertainties in this regard lead to significant expenses for market participants and it adds an unnecessary risk to the global capital market. We therefore support the way forward suggested in the consultation.

A forthcoming proposal must take into account that Central Securities Depositories (*CSDs*) *are account provider in the Swedish book-entry system*

according to the Swedish legislation. In our opinion there should be a special legislation regarding the activity as account provider for CSDs and also for the special function as account operator for the CSD when the CSD is account provider. The MiFID framework is definitely not the right place for regulating CSDs as account operators. This question has been raised several times but is not discussed in the consultation. In our opinion there is a lack of a clear statement from the Commission how this question is going to be solved. We still think "mixed system" are a far better term for the systems in the Nordic region because the systems are a combination of direct and indirect holding. Transparent system gives a false impression that a holding is in one way or another transparent. A book-entry holding of securities is in our view not transparent except for the account provider. A future legislation regarding legal certainty has to be coordinated with rules for CSDs that are properly calibrated to include the core functions of the Swedish book-entry system.

Regarding *corporate actions* investors of course face more difficulties cross-border than in a domestic context. But, there are several good reasons to put further legislative action in this area on hold for time being. Firstly to give time to study the effects of the implementation in Member States of Shareholder´s right Directive. Work is for example taking place on market standards for general meetings in respect of that Directive. Secondly, this section lacks an impact assessment and also an analysis of the needs of different types of investors. Some investors may only want to have the basic rights flowing from securities; others want more or less full service.

Furthermore, to compare securities transactions with payments is to underestimate the complexity of a securities transaction. Before any proposal for legislation is made about the *costs* there must be an impact assessment taking into account that most holdings are national and a proposal to level the costs between domestic and cross-border holdings could have adverse effect on the financial market and increase costs for the small investors.

It should be left to the account holders and account operators to agree on the level of services and thereby the costs for the holding of securities. Furthermore, we believe that the competitive element itself will see to it that such services are offered in the market. An account provider´s right to exercise the rights on behalf of the investor should always be based on the investor´s consent or an agreement between the investor and the account provider.

We are of the opinion that a harmonization of securities law should have effects on company law and especially who the issuer must recognize as securities owner. It is not possible to state or legislate for example that the account provider should ensure that the account holder can exercise his rights without having impact and effect on company law.

Finally, criticism has been raised regarding Geneva Securities Convention that the harmonization achieved in the text of the convention is minimal due to the references to declarations, national insolvency law and "non-convention law". In our view the same criticism can apply to some of the principles in this consultation and we are not convinced that this in some areas is the right way.

Q1

As stated in the general remarks we support objective 2 and 3. Regarding objective 1 we have already mentioned that we have doubts about regulating the account provider function for CSDs in MiFID.

Regarding objective 4, the important question is what is meant by "the full exercise of investor rights must be guaranteed." What is full exercise? We doubt that such exercise can be guaranteed without some harmonization of whom the issuer has to recognize as the legitimated person. Furthermore, how can principles 15 – 17 work if the issuer is not obliged to accept the information from the account providers about the holding the provider represents. See also principle 3.1.2 stating "that the national law should make sure that account holders which act in the capacity of account provider for a third person exercise the rights in accordance with the instructions of that person" and 5.5 5. "Effectiveness in the above sense does not determine whom an issuer has to recognize as legal holder of its securities".

Clearly, an account provider cannot have any obligations or responsibilities towards the holder if the issuer does not accept the account provider.

Q2

The proposal is a step forward and the proposed principles and the notification system are acceptable to us. However, we must emphasize that it is not possible to form a definitive opinion without seeing the detailed drafting of legal rules on shared functions.

Q3

The Commission still calls the system a transparent one which, in our opinion, is not correct. To describe the book-entry system as "transparent" gives the wrong impression and can lead to misunderstandings.

Besides the term transparent we have some doubt about shared functions. Even to describe the system as shared is problematic. It would be better if the words "but not all" were deleted.

Lastly, we are not sure what is meant by saying in section 2.2 that the principle should specify which quality of involvement the other person must have.

Q4

We have experienced some problems when a mixed or indirect holding system has to connect with systems which not allow indirect holding (i.e. nominee holdings).

Q5

It is very important that a forthcoming proposal is in line with The Geneva Securities Convention. Many of our members are involved in transactions with non-EU account holders or account providers. For that reason it is extremely important to achieve global compatibility regarding the substantive law of securities dispositions.

Regarding the principle 1 c we suggest that the right of the investor should be more directly expressed, perhaps in the terms of the right to transfer the holding to another account provider. Furthermore, we are not still convinced about the need of the concept of ultimate account holder. Do we really need it and how is the industry going to separate that holder from the account holder? How does it work in connection with company law?

Q6

See above

Q7

As noted above the compatibility of the planned EU legislation with the Geneva Securities Convention is of fundamental significance. If the international efforts to harmonize substantive law are frustrated through EU-legislation it could damage the EU as a financial centre. Furthermore, such legislation would jeopardize the EU's position as responsible negotiating party in international fora.

Q8

The proposal is a step forward with a little more flexibility. However, we are still of the opinion it goes too far. The concept no credit without debit is not the only solution and also not compatible with all legal systems in the EU. To stay in line with the functional approach it is preferable for a future directive to provide for other specific corrective measures in case of shortfall.

The rule in 2 is a rigid but, if there is a lack of securities, the requirement is that the account provider should act promptly to secure the situation. It seems reasonable enough but the question is still unsolved regarding the legal effects of a shortfall (5.3). Also, this combined with the national discretion about shortfalls can add to the uncertainty for cross-border transactions which is contrary to the aim of the project.

Q9

We have not experienced any real problems regarding excess of securities. It seems to us that this question has got to much attention.

Q10

The proposed principle is not considered appropriate. There are no reasons for letting account providers bear the cost of buy-in in all cases. In particular the account holders should be responsible for the costs if the account holders have caused or contributed to the shortfall.

Q11 and 12

We are of the opinion that the proposed principles give too much room for national discretion. It is very important that sufficient harmonization could be achieved and the European legislation is fully in compliance with the Geneva Securities Convention.

As stated above, there can be a problem regarding the relationship between a securities legislation and company law. Principle 5.1.5 states that the "Effectiveness in the above sense does not determine whom an issuer has to recognize as legal holder of its securities. What will the situation be if the issuer does not accept an account holder or account provider? Who is then going to be responsible for the main principle that the full exercise of investor rights must be guaranteed. An account provider can obviously not be responsible for a decision made by an issuer regarding the account holder's right.

However, we are not entirely clear how to read 5.1.2 compared with 5.1.6. Is 5.1.6 restricted to so-called "conditional credit"?

Furthermore, it is unclear how to understand the principles in 5 compared with the rules in the Settlement Finality Directive (98/26/EC) and, also article 27 in the Geneva Securities Convention.

Q13

Yes.

Q14a

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Q 14 b

It is of course important that erroneous or unauthorized bookings can be reversed and corrected without the account holder´s consent. Such mistakes happen and they should be promptly corrected. Timing is crucial to avoid additional damages. There must always be a possibility to reverse book-entries made by mistake and obviously faulty. However, an explanation of the term erroneous could be beneficial. In addition, we suggest that the case foreseen in section 7.1.1. (b) should be revised so that erroneous crediting may be reversed irrespective of whether the authorized account holder has authorized the crediting, i.e., "which was not authorized…" should be deleted. As we understand it, the current draft means that the account holder will be able to avoid reversal of crediting, for example excess crediting, by having authorized the crediting. We assume that this is not the intention.

The list should of course be added with reference to cases when a courts or judges made decisions.

Q 15

There is no need of any standard documentation as this is a matter that could be left to the discretion of Member States. We have not experienced any problem in this regard.

Q 16

Our starting-point is that the good-faith concept is very problematic to apply on book-entry securities. We have even some doubts about the "test of innocence" but we can't see any grave negative implication of the proposed principle besides the intellectual one.

Q 17

As we have stated before, it is doubtful if any book-entry system is transparent for others than the account provider. For that reason it is problematic to justify the inferior priority for a control agreement on the ground that book-entry systems are transparent. A legislation under which certain interest have priority over other interest based on "visibility" should be rejected. Therefore principle 9, paragraph 1 c) must be deleted. Instead, to promote international harmonization, it would be desirable to add the same provision as in the Geneva Securities Convention that certain interests created in a certain manner should always have priority over other interests.

Furthermore, it must be ensured that the priority rules of the future SLD do not conflict with the Financial Collateral Directive. In addition, we welcome that an agreement between parties now are fully accepted. To promote further harmonization it could be stated that the entry on the account is the benchmark for chronological order.

Q18

No

Q19

Not applicable

Q20

No, not necessarily and we would support a more ambitious approach to further harmonize the legal framework for client securities. In a financial crisis all involved (supervisors, counterparties, investors) have a specific need to quickly determine the positions towards an insolvent institution. Consequently, there is a

need for robust and clear rules to be able to establish a potential shortfall and the consequences thereof.

Q21

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Q22

We do not agree with the proposed principle. For a well-functioning financial market with a high degree of investor protection and legal certainty it is of utmost importance with a harmonized rulebook in this regard as well as the conflict of law rule. Uncertainty about what law would apply and also what type of rules, tracing, pro rata per asset or asset class, in case of a providers' insolvency will have negative impact on the financial markets in the EU without any harmonized solution. In our opinion a harmonized solution is of great importance for the financial markets in the EU and we would prefer a pro rata solution (see Geneva Securities Convention).

Q 23

We can't see any real problem and we are therefore not sure if this rule is really necessary. In our opinion the writing could be positive instead of negative and also clarify that the account holder can give instruction through a representative with the necessary power of attorney. Furthermore, we suppose it should be the account provider, not the intermediary, in principle 11.1

Q 24

We have some doubt if this rule really is enough to give certainty in a cross-border context, in particular in a chain of accounts holding foreign securities.

Q 25

Not applicable

Q 26

In our opinion it must be clearly stated that the laws of all Member States in this context must recognize the effectiveness of non-segregated accounts. We would advocate that the presumption should be incorporated in the future directive. On the other hand a harmonized rule according to which all accounts opened by an account provider with another account provider are presumed to contain client securities would be too far-fetching.

Q27

As stated in the general remarks we are of the opinion that the conflict-of-laws regime is very important and we support every effort to find a satisfactory solution. The proposed principle is a step in the right direction. The current

fragmentation caused by various directives is not acceptable in this crucial area of law. As stated in the general remarks we can support the proposal.

Q28

We are not convinced about this approach. For the vast majority of account holders this information is of no interest because only domestic offices come into question anyway but the expenses will affect all account holders and account providers. Furthermore, for the transparent (mixed) holding systems a different model must be considered. There are no written agreement between the CSD as an account provider and the account holders in a direct holding. One solution could be that the applicable law is stated in the rules of the CSD (the account provider).

In our opinion the intermediary can't be fully responsible for the correctness of the information. Liability in this regard can only occur if the intermediary has acted negligently!

Q29

Conforming to the Hague Convention is of course better than not but the best solution is still in our opinion to adopt the rules of the Hague Convention.

Q30

Is this really practically useful and is there a need? Furthermore we are no sure what the principle in reality means and what the legal effects of the principle are.

Q31

Not applicable

Q32, 33, 34 and 35

We fully support the answer by EBF.

Q36

Not applicable

Q37

In our opinion a much more important issue to solve is the tax barriers.

We are in favor of a market-oriented approach that allows the market participants to determine the right level of pricing depending on demand and supply. A legislative measure in this regard should be left to a later stage after a review of the now proposed legislation and should be subject to an impact

assessment and a market consultation. Furthermore we are not convinced that investors in general and in particular small investors will benefit from this principle.

As we stated in the general remarks this principle lacks cost and benefit analysis as well as an impact assessment. A comparison between corporate action and payments is not adequate.

The term cross-border is today read in a geographical context but may have content, a different meaning, when barrier 9 is abolished. In our opinion a more general definition of cross-border is needed.

For the few corporate actions with established standards and processes non-discriminatory charges can be discussed but for most of the action there are no such standards and processes. In those cases the costs will be very different in different cross-border situations. Until such standards and process are available those situations are not compatible with domestic actions.

Differences of language, communication through one or more intermediaries, taxes and legislation regarding book-entry system are examples of problems that increases costs in the cross-border context.

Q38

Not applicable

Q39

The principle seems fair but we are not convinced that we need technical standards. However, no legal obligation in this regard could be adopted by the Commission through technical standards. Legal obligation should only be imposed by level 1 legislation.

Q40

We are not convinced that there is a real need for harmonization in this area. The matter should be left to the Member States.

Q41

In an EU context, we are of the opinion that account providers should be subject to specific authorization.

Q42

In general MiFID would be an appropriate instrument to cover authorization and supervision for account providers. But, MiFID is absolutely not the right place for regulation of CSDs as account providers as suggested in the 3rd discussion

paper regarding CSDs. The proposed legislation therefore has to be matched by a legislation regarding CSDs which covers their role as account operator.

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