INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW
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UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS FOR THE PREPARATION OF A DRAFT CONVENTION ON HARMONISED SUBSTANTIVE RULES REGARDING INTERMEDIATED SECURITIES
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COMMENTS BY GOVERNMENTS AND INTERNATIONAL ORGANISATIONS

(Comments by the Government of Malta)

CHAPTER I – ***Definitions, scope of application and interpretation***

Article 1 ***Definitions***

Paragraph (m)

"control agreement":- This type of agreement will invariably involve a collateral taker as one of the parties thereto who is accepting to take collateral provided by the account holder. It is submitted that the Committee should thus consider amending the definition of this term by adding immediately after the words "*means an agreement*" the words "*including a collateral agreement as defined in Article 22(1)*". In this way it is proposed to cater for the legal tradition in a number of jurisdictions where such control provisions in favour of the collateral taker would typically be included within the collateral agreement itself and not necessarily in a separate ad hoc agreement.

Article 4 ***Intermediated securities***

[Paragraphs 5. & 6. - Version A / Version B]

We understand that following the Committee's First Session held in May 2005, two alternative versions were proposed for further consideration.

It is submitted that Version A of Article 4 paragraphs 5 and 6 is in keeping with the general principle that the rights arising from the holding of the intermediated securities are effective and may be enforced against the issuer in all situations. Version B, on the other hand, appears to exclude such rights in the circumstances mentioned in paragraph 5 (a) to (d).

Paragraph 7

This paragraph caters for limits that may be determined by virtue of the domestic non-Convention law on the rights arising from a holding of intermediated securities in the name of an account holder in the capacity of a collateral taker. It is submitted that the law may very well allow freedom of contract in this matter such that the contracting parties (i.e., the collateral taker and the collateral provider) may also vary or derogate from any non-mandatory legal provisions. For instance, it is common practice for

a collateral taker to allow the collateral provider to continue to receive payments of dividend until the latter is in default of its obligations and upon due notice having been given to the collateral provider without avail. It is thus suggested that the Committee should consider introducing an amendment to this paragraph immediately following the words "*the domestic non-Convention law*", by adding the words "*or the terms of the control [i.e. collateral] agreement*".

Article 5 ***Acquisition and Disposition of intermediated securities***

Paragraph 4

It is opportune to clarify the rationale behind the addition effected to this Paragraph of the words "*Without prejudice to any rule of the domestic non-Convention law requiring that no credit or debit be made without a corresponding debit or credit, …*" at the Second Session of the *UNIDROIT* Committee meeting in May 2005. It is understood that the amendment is saving the situation that may prevail under a domestic non-Convention law requiring that a credit or debit to a securities account be effected only if there is a corresponding debit or credit. This position appears to be in conflict with and lead to the diametrically opposite effect to that proposed by the Preliminary Draft Convention that seeks to ensure that a credit or debit to a securities account is "*not ineffective*" even when it is not possible to identify the corresponding debit or credit as the case may be (as laid down in the same Article 5[4]). Ideally the Convention should still insist on the effectiveness of a credit or debit to a securities account, but introduce a saving provision for identified circumstances when there might not be a corresponding debit or credit such as, for instance, upon an issuance or redemption of securities or the exercise of conversion rights arising under the terms of the relevant securities.

CHAPTER VI – ***Relations with Issuers of Securities***

Article 19 ***Position of issuers of securities***

Paragraph 2 (e)

In the context of the general prohibition contained in Article 19 (paragraph 1) against any domestic law preventing the holding of securities with an intermediary (or the effective exercise of rights by an account holder), Paragraph 2 lists "*some examples of possible impediments in this context*" (as explicitly mentioned, in the "Explanatory Notes to the Preliminary Draft *UNIDROIT* Convention", in the *Uniform Law Review – Revue de Droit Uniforme, NS-Vol.X 2005-1/2*, p.104). Paragraph 2 (e) in particular outlaws any rule or provision that "*imposes restrictions on the holding of securities or the exercise of rights attached to securities by reference to the identity, status, residence, nationality, domicile or other characteristics or circumstances of any person acting in the capacity of* [an] *intermediary.*"

As a rule, a general disapplication of such restrictive domestic law appears to be appropriate in order to secure a level playing field in intermediated securities.

However, it is also opportune to introduce specific exceptions for legitimate domestic law restrictions that would give direct effect to established standards and norms obtaining in the international financial and economic sectors and the international comity in the field of anti-

money laundering and anti-terrorist financing measures as well as the application of United Nations Security Council economic sanctions. In this regard, it is expected that the law of a Contracting State would give effect or permit restrictions to the holding of securities or the exercise of rights attached to securities in cases where an intermediary is a resident or a national of or is domiciled in a "*non-cooperative country or territory*" ('*NCCT*') as defined by the Financial Action Task Force ('*FATF*') Recommendations or in a State against whom the UN Security Council has levelled economic sanctions. In such well-defined instances, it is submitted that the Article 19 prohibitions should give way to provisions of the domestic non-Convention law of a Contracting State that would give effect to mandatory legal or court-decreed freezing measures or injunctions requiring temporary suspension of rights.

CHAPTER VII – ***Special Provisions with respect to Collateral Transactions***

Article 22 ***Enforcement***

Paragraph 5

It is submitted that, for the sake of consistency, the words "*financial collateral*" in the second line should be amended to read "*collateral securities*" as already defined in Article 22(1). The suggested amendment would precisely focus on the intermediated securities themselves taken as collateral, as the object of realisation or valuation under this Paragraph.