

INTERMEDIATED SECURITIES

Legal Problems and
Practical Issues

Edited by
Louise Gullifer
and Jennifer Payne



• HART •
PUBLISHING

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OXFORD AND PORTLAND, OREGON
2010

Published in the United Kingdom by Hart Publishing Ltd
16C Worcester Place, Oxford, OX1 2JW
Telephone: +44 (0)1865 517530
Fax: +44 (0)1865 510710
E-mail: mail@hartpub.co.uk
Website: <http://www.hartpub.co.uk>

Published in North America (US and Canada) by
Hart Publishing
c/o International Specialized Book Services
920 NE 58th Avenue, Suite 300
Portland, OR 97213-3786
USA
Tel: +1 503 287 3093 or toll-free: (1) 800 944 6190
Fax: +1 503 280 8832
E-mail: orders@isbs.com
Website: <http://www.isbs.com>

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British Library Cataloguing in Publication Data
Data Available

ISBN: 978-1-84946-013-2

Typeset by Columns Design Ltd, Reading
Printed and bound in Great Britain by
TJ International Ltd, Padstow, Cornwall

INTERMEDIATED SECURITIES

Globally, there has been a shift from securities being held directly by an investor, to a situation in which many securities are held via an intermediary. The existence of one or more intermediaries between the investor and the issuer has a potentially significant impact on the rights of the investor, the role and obligations of the issuer, and on the position and responsibilities of the intermediary. However, different jurisdictions have dealt with the issues arising from intermediation in a variety of ways. In the UK, for example, the concept of a trust is used to explain the different rights and obligations which arise in this scenario, whereas in the US the issues have been addressed by legislation, in the form of UCC Article 8. This variety is problematic, given that it is possible for an investor to hold securities in a number of different jurisdictions. A new UNIDROIT Convention on the issue of Intermediated Securities, the Geneva Securities Convention 2009, aims to create a common framework for dealing with these issues. This collection of essays explores the issues that arise when securities are held via an intermediary, and in particular assesses the solutions put forward by the new Convention on this issue. It will be essential reading for practitioners and academics.

Foreword

The sharp move from direct holdings of investment securities to holdings through an account with a securities intermediary has brought many benefits in its train. Issuers can now, if they wish, issue a single global note instead of having to deal directly with perhaps tens of thousands of investors; first-tier intermediaries can in turn deal with a limited number of account holders, who will themselves hold for a larger number of their own customers, and so down the chain, thus creating a pyramid structure involving a hierarchy of intermediaries; and transfers between customers of the same intermediary can take place across its books without the need to involve the issuer or a higher-tier intermediary. The root of title to securities now becomes a credit to a securities account instead of registration in the issuer's records or possession of a certificate. The pooling of investments in an omnibus account without differentiation between one customer and another also makes for flexibility and costs savings.

However, in most countries the law has yet to catch up with these developments. English law, for example, can accommodate many issues through the well-developed institution of the trust and of sub-trusts under it, but there remain a number of problems to which no clear answers can be given: the nature of the account holder's entitlement; the treatment of shortfalls; the impact of an intermediary's insolvency, particularly as regards cash and securities held for its own account which may have been charged to external creditors but to which the account holders will also wish to make claim; the ordering of priorities and the conditions in which a purchaser will obtain a clear title; the legal significance of the collateral-taker's right of reuse; and the exercise of voting rights in an intermediated system.

It was, once again, the United States which led the way in the common law world with its major revision of Article 8 of the Uniform Commercial Code and its focus on rules which respond to the needs of the market rather than on doctrinal considerations. In England the Financial Markets Law Committee produced a report setting out the principles for an investment securities statute. The project was then referred to the Law Commission, which deferred action pending completion of the Unidroit project. At regional level there are EC directives on settlement finality and financial collateral designed to reduce formalities for the acquisition of interests in financial collateral and to give protection against avoidance under insolvency law. At the international level we have the Hague Convention on the law applicable to rights in respect of

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intermediated securities and, more recently, the Unidroit Convention on substantive rules for intermediated securities. This last was a considerable achievement given the widely differing concepts of an indirect holding, which in some legal systems appear more closely to resemble a direct holding; and necessarily a good deal had to be left to non-Convention law.

This collection of essays by a number of distinguished academic and practising experts in the field from a number of jurisdictions, based on their contributions to a conference held at Harris Manchester College, Oxford, in March 2009, is therefore most timely. The papers by the various contributors range far and wide, covering all the above developments and others besides, and combine keen analytical rigour with a deep understanding of the workings of the securities markets. Skilfully edited by Louise Gullifer and Jennifer Payne, the collected papers cast much-needed light on the complexities of the legal issues arising from intermediation, complexities highlighted by the collapse of the Lehman Brothers Group and the extensive litigation now being pursued around the world concerning the interests, rights and liabilities of the various players. This book is essential reading for anyone having a serious interest or involvement in this field.

Roy Goode
Oxford
26 March 2010.

Preface

The origins of this book lie in a conference at Harris Manchester College, Oxford on 20 March 2009. Some 30 participants, including academics and practitioners from the UK, Europe and the US, gathered to discuss the issue of intermediated securities.

The purpose of the Conference in March 2009 was to consider and comment on issues arising out of the intermediated holding of securities and, in particular, the final draft of the UNIDROIT Convention on Substantive Rules regarding Intermediated Securities. We were delighted that speakers from so many jurisdictions attended in order to consider the difficult questions arising in the context of intermediated securities, and in particular to discuss the likely impact of the UNIDROIT Convention on these issues. At the conference the following speakers produced papers or comments: Mark Evans (of Travers Smith), Roy Goode, Louise Gullifer, Erica Johansson, Herbert Kronke, Ben McFarlane, Eva Micheler, Charles Mooney, Guy Morton, Gabriel Moss, Habib Motani, Maisie Ooi, Jennifer Payne, Ed Rock, Robert Stevens, Teun Struycken, and Karin Wallin-Norman. Happily many of these speakers have been able to contribute papers to this volume based on their papers and thoughts at the conference. We would also like to thank Antony Zacaroli, who attended the conference and who has written an additional paper for this volume, and Hideki Kanda who was not able to attend, but who nevertheless has contributed to this collection. The Convention was finalised in October 2009 at a conference in Geneva, with the agreed short title of the Geneva Securities Convention, and the papers in this volume have been fully updated to take account of all changes agreed.

We would like to thank Travers Smith for sponsoring the conference which began this project. Without its support the conference would not have been possible. We would also like to thank Harris Manchester for hosting the event, and the editors at Hart for their assistance in navigating this book through its various stages. We must thank Roy Goode, Dan Prentice and Hugh Beale who so kindly acted as Chairs at the Conference. Thanks are also due to Bernd Delahaye and Wenwen Liang and Jennet Batten for their assistance on the day of the conference, and to Bernd Delahaye and Victoria Barns-Graham for their invaluable work as research assistants in helping to prepare this volume for publication. Special thanks are due to Roy Goode who provided the original inspiration for this project, and who has written the Foreword for this collection.

Louise Gullifer and Jennifer Payne
Oxford, November 2009

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