

**SCHEDULE 2**

**DENMARK**

**COUNTRY ANALYSIS**

**Draft September 2000**

## 1. General

### 1.1 Pledge – General Characteristics

- In respect of fungible securities a security interest may be created by simple pledge agreement between the pledgor and the pledgee.
- Under the Danish Securities Trading Act s. 59 (2) registered securities are defined as negotiable dematerialised securities, registered with a central securities depository, in accounts belonging to individual owners. The registration comprises not only title but also limited rights such as mortgage rights and attachments. The registration of rights will be made at the securities centre but will be governed by the account-keeping institution. Under s. 66 (1) rights in respect of dematerialised securities must be registered in a Securities Centre to obtain protection against legal proceedings and assignees in contract. The constitutive act for transfers and pledges of dematerialised securities is registration. As regards enforcement, the pledgee can require sale of the pledged securities through a bank or a broker authorised to deal on the Copenhagen Stock Exchange.
- With respect to physical bearer securities s.14 of the Danish Bonds Act provides that deprivation of power of disposal of the bearer security is required to obtain protection against legal proceedings and assignees in contract. As regards enforcement, the type of remedy available will be public auction, although other remedies will be available if stipulated in the pledge.

### 1.2 Transfer of Title – General Characteristics

- Although there is no statutory provision which recognises the validity of the transfer of title for security purposes, there is no statutory provision forbidding it, so the transfer of title for security purposes is possible.
- However, collateral arrangements in Denmark are not based on transfer of title. It is difficult to predict the result if such an arrangement were to be considered under Danish law since Danish courts have not dealt with this specific situation.
- As between the parties a Danish Court would be inclined to recharacterise the arrangement as the creation of a form of security interest on the basis that this was the true intention of the parties. *Vis-a-vis* the creditors of the pledgee, however, it is unlikely that such an arrangement would be enforceable, since the parties would have neglected to perfect the security interest in the manner required under Danish law. Were a Danish court to review arrangements based on the transfer of title under a foreign law it is likely the Danish court would uphold the arrangement since it does not appear to be against Danish “*ordre public*” or contravene any mandatory protective rules of Danish law.
- In order to obtain protection against legal proceedings and assignees in contract a transfer of title on registered securities must be notified to the account-keeping institution (and registered in the Danish Securities Centre). Identification of the securities is required for the registration in the Danish Securities Centre. As regards

physical bearer securities deprivation of power of disposal of the bearer security is required to obtain protection against legal proceedings and assignees in contract.

- There are no consents or approvals that must be followed in order to have a valid transfer of title.
- Close-out netting is enforceable under Section 57 and 58 of the Danish Securities Trading Act which basically state that an agreement between two or more parties to the effect that all proved claims pertaining to the clearing business carried on by a clearing centre or Danmarks Nationalbank or pertaining to a payment system which is settled through accounts with Danmarks Nationalbank, shall be set off against each other, may with legal effect towards the estate and creditors also include a provision to the effect that such claims shall be finally discharged or reversed in full if one of the parties is ordered to be wound up, or an administration order is applied for, or negotiations for a compulsory composition are opened. The Section 58 particularly states that an agreement between two or more parties to the effect that all their claims against one another which result from securities trading under the Act shall be set-off against each other regularly (for more details see subsection 2.2.2)
- Contractual set-off is enforceable in the event of formal insolvency proceedings and is limited by a number of protective provisions in the Danish Bankruptcy Act , Sections 42(3) and 42 (4), as a result of which these contractual rights of set-off may not be exercised (for more details see subsection 2.2.2)
- In relation to mark-to-market collateral arrangements and based on the principle that “new security for old debt” may be avoided, any additional deliveries of collateral might be vulnerable to avoidance if made within 6 months prior to the insolvency of the entity providing the collateral.

### **1.3 Considerations relevant to collateral arrangements**

- Floating charges over claims or securities are unknown in the Danish legal system. However it will be possible to create valid pledge over all securities registered or to be registered in a specific account with an account-keeping institution provided the pledgor has no right nor any possibility to take securities out of the account without permission from the pledgee
- Delays in registration or deprivation of power of disposal may invalidate the security in case of the pledgor’s bankruptcy; failing to comply with the relevant perfection requirements will not make effective the security interest vis-s –vis the pledgor’s creditors (the security interest will still be valid as between the pledgor and the pledgee, although this may not be much help).
- Provided the relevant formalities with regards to creation and perfection of security are complied with in relation to each provision of collateral, no further action needs to be taken to ensure that the security interest continues and remains perfected. It is possible to create a security interest over a fluctuating pool of assets provided that its clear at all times which assets are subject to the security interest. Some problems may arise with respect to future obligations if pledgor creates a secondary pledge or an intervening creditor levies execution on either the pledgor’s right to have the

collateral returned or the pledged assets.

- Enforcement may be delayed by one week.
- The pledgee must take reasonable care of the assets pledged and may be held liable for the losses arising from failure to do so;
- In order to maintain protection against legal proceedings and assignees in contract it is of importance that the pledgor has no possibilities of substitution without permission from the pledgee. Substitution risk will not exist during “suspect period” provided the substitute collateral is of no greater value than the collateral it is replacing and further provided that the substitute collateral is posted either simultaneously with or prior to the release of the old collateral. So if the old collateral is released before receipt of the substitute collateral, this will be considered to be a new pledge and may be set aside under Section 70 of the Bankruptcy Act if it occurs within such suspect period. If the value of the substitute collateral exceeds the value of the collateral being replaced the pledge of the excess collateral may risk being set aside under Section 70 Bankruptcy Act. If a substitution creates additional security in respect of previous indebtedness or if the changed securities are not protected against legal process without undue delay the invalidation rules in the Danish Bankruptcy Act may be applied in bankruptcy and in compulsory composition arrangements as well as in debt rescheduling arrangements.
- Until 1 January 2000 a deed of pledge (1) between two Danish entities or (2) signed in Denmark from a Danish pledgor to a foreign pledgee or (3) signed in Denmark from a foreign pledgor to a Danish pledgee had to be stamped with 0.3% of value of the pledged assets. However a deed of pledge was valid whether the stamp duty was paid or not. According to a new Stamp Duty Act no stamp duty is due to be paid as regard Deeds of Pledge signed on or after 1 January 2000.
- As regards re-use, it is possible to a certain extent to re-pledge any collateral received to a third party. Applicable Danish Law in this respect is not based on any statutory provisions and the circumstances under which such a re-pledge may take place and the conditions which would apply are thus not entirely clear. A broader right of the pledgee to use the collateral, for example to sell or lend it, is not possible.
- The right to use collateral by way of rehypothecation in respect of Danish Government debt securities will depend upon how the security interest has been registered with VP. If securities have been transferred into a separate VP account in the name of the pledgee, then the pledgee will be able to exercise rights. However, if the securities have been transferred into a separate VP account in the name of the pledgor (and the account is pledged to the pledgee) then the pledgee will not be able to exercise this right.

## **2. Private International Law and Domestic Law Aspects of Collateral**

### Validity of the Contract/ Attachment

Danish private international law:

- In general Danish law adheres to the principle of freedom of contract and will permit the parties to choose their own law to govern their contract only subject to Danish Public Order.
- It appears that Danish law would most likely be the governing law for the creation of a security interest in cash or fungible securities.

Danish domestic law:

- Inter partes, the only requirement under Danish law is that the contract clearly stipulates that the parties have agreed to enter into a pledge or a security agreement.
- No formality is required in order to create a valid security interest- it can be done orally or in writing. However for all practical purposes a pledge is created in a deed; the deed will be valid without any formalities.
- To obtain protection against legal proceedings and assignees in contract a pledge on registered securities must be notified to the account-keeping institution (and registered in the Danish Securities Centre). Identification of the securities is required for the registration in the Danish Securities Centre. As regard physical bearer securities deprivation of power of disposal of the bearer security is required to obtain that protection. Delays in registration/deprivation of power of disposal may invalidate the security in case of the pledgors bankruptcy.
- A pledgee must take reasonable care of the assets pledged and may be held liable for losses arising from his failure to do so.

### Perfection:

Danish private international law:

- Conflicts of law rules would apply Danish law to the perfection of a security interest in fungible securities and the *lex loci* of fungible securities held through an account in a clearing system is the place where the account is held.

Danish domestic law:

- Rights in respect of dematerialised securities must be registered in a Securities Centre to obtain protection against legal proceedings and assignees in contract. The registration of rights is made at the securities

centre but will be governed by the account-keeping institution. Thus, application for registration must always be made to an account-keeping institution. In order to make a valid pledge there is no requirement for notarisation nor stamping. (See Section 1.1 – General Characteristics).

Priorities:

Danish private international law:

- It appears that Danish Law would most likely be the governing law

Danish domestic law:

- The priority criteria for the dematerialised securities will be the time of registration and for physical securities will be the time of deprivation of power of disposal (possession).

Enforcement:

Danish private international law:

- It appears that Danish Law would most likely be the governing law

Danish domestic law:

- The general rule is that collateral may be sold by compulsory sale or, in the case of listed securities, through a securities dealer. However, the parties may agree on alternative method of liquidation subject to notification requirements. The pledgee must make a notification and demand for payment giving the pledgor one week's notice, unless immediate sale is required to avoid or limit loss, in which case there is no requirement for one week's notice.
- Enforcement of a pledge will be subject to the provisions of the Danish Administration of Justice Act. The pledgee shall before taking any steps regarding enforcement give formal notice (by recommended letter) to the pledgor that the pledge will be realised in case of unpaid debt. After such notice the pledgor has a one-week waiting period to repay the debt.
- Formal notice to the pledgor is not necessary if (1) his address is unknown to the pledgee or (2) immediate sale is necessary to avoid or limit a loss.
- With respect to the enforcement of a security interest in fungible securities registered with the DSC there are certain statutory provisions contained in S 538 and 557 of the Danish Administration of Justice Act which provide that before any enforcement is effected the debtor shall have the "grace period" of one week to fulfil its obligations, and that a security interest in fungible securities may only be enforced by a sale of such securities through a bank or a member of the Copenhagen Stock Exchange.

Insolvency:

Danish private international law:

- Denmark follows a “universal” approach in the sense that it extends insolvency proceedings to all assets of the insolvent party, even assets located abroad. However in practice the enforcement of Danish insolvency rules against non-Danish assets may be limited.
- The Kingdom of Denmark has entered into a bankruptcy treaty with Finland, Iceland, Norway and Sweden which is currently in force in Denmark and the effect of this treaty is the following:
  - a bankruptcy declared in Denmark on the basis of incorporation of the debtor in Denmark will also comprise assets which the bankrupt company, or its branch office registered in such countries, has in Finland, Iceland, Norway or Sweden;
  - The Danish Bankruptcy Act as *lex concursus* will then in general apply as to disposals of assets of the bankrupt, avoidance rules, priority rules and distribution. So matters as to validity of collateral will generally follow “*lex rei sitae*”.
  - although not specifically dealt with in the treaty, it is possible that the set-off and netting provisions will follow “*lex concursus*” although there is also authority for “*lex contractus*” to apply.
  - under Danish law there are no limitations on the bringing of claims against a Danish bank by creditors, who are not subject to the jurisdiction of the courts of Denmark.

Danish domestic law:

- The types of Insolvency Proceedings available under the Danish Bankruptcy Act and Administration of Justice Act are:
  - an official suspension of payments registered at the local bankruptcy court and under the supervision of a Supervisor appointed by the bankruptcy court;
  - compulsory composition in a bankruptcy. These proceedings are also carried out under the supervision of the bankruptcy court;
  - a full bankruptcy under the supervision and authority of the bankruptcy court.
- Registration of a branch or the existence of assets in Denmark would not be sufficient to create jurisdiction for the purposes of declaring a foreign company bankrupt under the Danish Bankruptcy Act.

- There is no possibility of a stay or freeze in the event that the collateral provider is subjected to formal insolvency proceedings of any type.
- No zero-hour rule. The invalidation rules in Danish Bankruptcy Act may be applied in bankruptcy and in compulsory composition arrangements as well as in debt rescheduling arrangements.

### **3. Miscellaneous**

#### **3.1 Cross-border transactions in multi-tiered holding systems**

- The laws of Denmark do not deal clearly with the nature of a participant's interest in a holding of fungible securities. Whether such an interest would be characterised under these laws or whether it is possible to assert ownership over securities which are held on a co-mingled basis depends on whether the owner is able to identify the relevant securities and prove ownership of them.
- The Danish Securities Trading Act Section 6 (3) provides that a securities dealer is entitled to keep the securities of its clients in an omnibus account or a segregated account. However the same section also provides that the securities dealer shall keep a register clearly identifying the individual client's rights of ownership to securities kept on a co-mingled basis and enable each owner to reclaim any securities held in a mingled account in the event of the securities dealer's bankruptcy.
- The interest created in mingled securities held in a segregated client account would not be a direct right to any individual assets held in the account. Rather the owner would be considered as having an ownership interest in securities equal to his/her part of the total amount of securities registered in the account. Such an interest will include all the normal incidents of ownership in any other respect.

#### **3.2 Implementation of the Settlement Finality Directive**

In November 1998 the Economic Ministry set up a working party, headed by the Financial Supervisory Authority, to deal with the implementation of the legislation. It is understood that a final draft was sent to Parliament before the end of 1999. As mentioned above the PRIMA approach is already the law under existing Danish conflict of laws principles. Although the implementing language is expected to mirror the narrow language of the Directive, the commentary will make it clear that this narrow language in no way restricts the application of the existing Danish law principles.