



INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW
INSTITUT INTERNATIONAL POUR L'UNIFICATION DU DROIT PRIVE

**UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS
FOR THE PREPARATION OF A DRAFT CONVENTION ON
SUBSTANTIVE RULES REGARDING INTERMEDIATED
SECURITIES
Second session
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**PRELIMINARY DRAFT CONVENTION ON SUBSTANTIVE RULES
REGARDING INTERMEDIATED SECURITIES**

*(as adopted by the Committee of Governmental Experts
at its second session, held in Rome, 06-14 March 2006)*

Introductory Remarks
by the UNIDROIT Secretariat

1. - During the second session of the UNIDROIT *Committee of Governmental Experts for the Preparation of a Convention on Substantive Rules regarding Intermediated Securities* (the CGE), the Drafting Committee continued its work under its Chairman Mr Hideki Kanda (Japan), with Mr Guy Morton (United Kingdom) and Mr Michel Deschamps (Canada) acting as Co-Chairmen. Members of the Drafting Committee comprised representatives of the delegations from Belgium, Chile, a “Nordic” country, France, Germany, Luxembourg, Switzerland and the United States of America. The Chairman of the Drafting Committee invited observers from the European Commission, the European Central Bank and the Trading Association for the Emerging Markets to participate in its work.

2. - The task of the Drafting Committee was to review the draft articles of the *Preliminary draft Convention on Harmonised Substantive Rules regarding Intermediated Securities*¹ as approved by the CGE at the occasion of its first session in May 2005². The revision of the text was designed to reflect discussion in the ongoing session of the CGE.

3. - The Drafting Committee held its first meeting on 9 March 2006 and its last meeting on 13 March 2006. On 14 March the text of the preliminary draft Convention³, including amendments proposed by the Drafting Committee, was laid before the CGE meeting in plenary. The Chairman of the Drafting Committee stressed that the Drafting Committee had not had enough time to realise all decisions taken by the CGE and to include all necessary changes. Where this was the case, an explanatory footnote had been included.

4. - As regards the proposed changes to the structure of the draft instrument, the Drafting Committee had decided to follow the sequence brought forward in a joint paper of the French and the US Delegations.⁴ The Chairman of the Drafting Committee asked the Secretariat to bring the necessary changes to the text.

5. - Following detailed explanation of the proposed amendments by the Chairman of the Drafting Committee the CGE decided to take the amended text as a basis for further discussion.⁵

6. - The preliminary draft instrument was renamed the *Preliminary draft Convention on Substantive Rules regarding Intermediated Securities*.

7. - After the meeting, the UNIDROIT Secretariat reviewed the text from an editorial perspective and changed the structure and the numbering of the preliminary draft Convention following the indications given by the Chairman of the Drafting Committee.

8. - The revised official text is set out in a marked up version (as against UNIDROIT 2005 Study LXXXVIII Doc. 24) in APPENDIX 1 *infra* and in a clean version in APPENDIX 2 *infra*. A table of concordance is included as APPENDIX 3 *infra*.

¹ UNIDROIT 2005, Study LXXVIII Doc. 24 (Preliminary draft Convention).

² Cf. UNIDROIT 2005, Study LXXVIII Doc. 23 (Report on the first session), Para 193.

³ UNIDROIT 2006, C.G.E./Securities/2/DC/W.P. 3.

⁴ UNIDROIT 2006, C.G.E./Securities/2/W.P. 9.

⁵ UNIDROIT 2006, C.G.E./Securities/2/W.P.17.

APPENDIX 1

PRELIMINARY DRAFT CONVENTION ON ~~HARMONISED~~ SUBSTANTIVE RULES REGARDING INTERMEDIATED SECURITIES

CHAPTER I - DEFINITIONS, SCOPE OF APPLICATION AND INTERPRETATION

Article 1 *[Definitions]*

In this Convention:

(a) “*securities*” means any shares, bonds or other ~~transferable~~ financial instruments or financial assets (other than cash) or any interest therein, which are capable of being credited to a securities account;

(b) “*securities account*” means an account maintained by an intermediary to which securities may be credited or debited;

(c) “*intermediary*” means a person that in the course of a business or other regular activity maintains securities accounts for others or both for others and for its own account and is acting in that capacity;

(d) “*account holder*” means a person in whose name an intermediary maintains a securities account, whether that person is acting for its own account or for others (including in the capacity of intermediary);

(e) “*account agreement*” means, in relation to a securities account, the agreement with the relevant intermediary governing that securities account;

(f) “*intermediated securities*” means the rights of an account holder resulting from a credit of securities to a securities account¹;

(g) “*relevant intermediary*” means, with respect to an ~~securities account holder~~, the intermediary that maintains the securities account for the account holder;

(h) “*disposition*” means an act of an account holder disposing of intermediated securities and includes a transfer of title, whether outright or by way of security, and a grant of a security interest;

(i) “*adverse claim*” means, with respect to any securities, a claim that a person has an interest in those securities that is effective against third parties and that it is a violation of the rights of that person for another person to hold or dispose of those securities;

(j) “*insolvency proceeding*” means a collective judicial or administrative proceeding, including an interim proceeding, in which the assets and affairs of the debtor are subject to control or supervision by a court or other competent authority for the purpose of reorganisation or liquidation;

(k) “*insolvency administrator*” means a person (including a debtor in possession where applicable) authorised to administer an insolvency proceeding, including one authorised on an interim basis;

¹ This definition remains under consideration. Questions have been raised, for example, as to the appropriateness of the particular term “intermediated securities”, as to whether it should be replaced by “intermediated rights”, and as to whether the definition should be expanded so as to include terms that currently form part of Article 4.

(l) securities are “*of the same description*” as other securities if they are issued by the same issuer and:

- (i) they are of the same class of shares or stock; or
- (ii) in the case of securities other than shares or stock, they are of the same currency and denomination and form part of the same issue;

(m) “*control agreement*” means an agreement between an account holder, the relevant intermediary and a collateral taker, or, if so permitted by the domestic non-Convention law, an agreement between an account holder and a collateral taker of which notice is given to the relevant intermediary, which relates to intermediated securities and provides that, in such circumstances and as to such matters as may be specified in the agreement or provided by the domestic non-Convention law, the relevant intermediary is not permitted to comply with any instruction given by the account holder without having received the consent of the collateral taker, or is obliged to comply with any instructions given by the collateral taker without any further consent of the account holder~~includes either or both of the following provisions:~~

~~————— (i) ——— that the relevant intermediary is not permitted to comply with any instructions given by the account holder in respect of the intermediated securities to which the agreement applies without having received the consent of the collateral taker;~~

~~————— (ii) ——— that the relevant intermediary is obliged to comply with any instructions given by the collateral taker in respect of the intermediated securities to which the agreement applies in such circumstances and as to such matters as may be provided by the account agreement or the domestic non-Convention law, without any further consent of the account holder;~~

(n) “*designating entry*” means an entry ~~in favour of a collateral taker~~ in a securities account made in favour of a collateral taker in respect of the securities account or in respect of specified securities credited to the securities account, in respect of specified intermediated securities~~which, under the account agreement, a control agreement or the domestic non-Convention law, has the effect that, in specified circumstances and as to specified matters, either or both of the following effects:~~

~~————— (i) ——— that the relevant intermediary is not permitted to comply with any instructions given by the account holder in respect of the intermediated securities in relation to which the entry is made without having received the consent of the collateral taker, or;~~

~~————— (ii) ——— that the relevant intermediary is obliged to comply with any instructions given by the collateral taker in respect of the intermediated securities in relation to which the entry is made in such circumstances and as to such matters as may be provided by the account agreement, a control agreement or the domestic non-Convention law, without any further consent of the account holder;~~

(o) “*domestic non-Convention law*” means the domestic provisions of law of the State whose law is applicable under Article 2, other than those provided in this Convention;~~;~~

(p) “non-consensual security interest” [to be defined]:

(q) “securities settlement [or clearing] system” means [a system] [an entity] which:

————— (i) clears, settles or clears and settles securities transactions;

————— (ii) [has rules and agreements with its participants that are publicly accessible];

————— (iii) is operated by a central bank or conducts operations that are supervised [by a regulator that has oversight over its rules and agreements];

————— (iv) has been notified as a securities settlement [or clearing] system in a declaration by a Contracting State, [or falls within a category of [systems] [entities] that have been notified as securities settlement [or clearing] systems in a declaration by a Contracting State and has been specifically identified as falling within that category in a publicly accessible website of

its regulator which also specifies the date on which it first was designated as falling within that category];

provided that a declaration referred to in this sub-paragraph must be made on the grounds of the reduction of risk to the stability of the financial system:

(r) “collateral taker” means a person to whom a security interest in intermediated securities is granted;

(s) “collateral provider” means an account holder by whom a security interest in intermediated securities is granted;

(t) “collateral agreement” means an agreement between a collateral provider and a collateral taker providing (in whatever terms) for the grant of a security interest in intermediated securities.

Article 2
[Scope of application]

This Convention applies where rules of private international law of the forum state designate the law of a Contracting State.

Article 3
[Principles of interpretation]

1. - In the implementation, interpretation and application of this Convention, regard is to be had to its purposes, to its international character and to the need to promote uniformity and predictability in its application.

2. - Questions concerning matters governed by this Convention which are not expressly settled in the Convention are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the domestic non-Convention law.

CHAPTER II – TRANSFER OF INTERMEDIATED SECURITIES

Article ~~5~~4
[Acquisition and disposition of intermediated securities]

1. - Intermediated securities are acquired by an account holder by the credit of securities to that account holder's securities account.

2. - No further step is necessary, or may be required by the domestic non-Convention law, to render the acquisition of intermediated securities effective against third parties.

3. - Intermediated securities are disposed of by an account holder by the debit of securities to that account holder's securities account.

4. - 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, a debit or credit of securities to a securities account is not ineffective because it is not possible to identify a securities account to which a corresponding credit or debit has been made.

5. - Debits and credits to securities accounts in respect of securities of the same description may be effected on a net basis.

6. - This Article does not preclude any other method provided by the domestic non-Convention law for the acquisition or disposition of intermediated securities, ~~but the priority of an interest created by any such other method is subject to the rules in Article 10.~~

Article 65

[Security interests in intermediated securities]

1. - An account holder may grant to ~~a another person~~ (“the collateral taker”) a security interest in intermediated securities ~~held by that account holder~~ so as to be effective against third parties by:

(a) entering into a collateral ~~n~~-agreement with the collateral taker ~~providing (in whatever terms) for the grant of such a security interest;~~ and

(b) delivering the intermediated securities into the possession or control of the collateral taker ~~in accordance with paragraph 2;~~

and no further step is necessary, or may be required by the domestic non-Convention law, ~~to render a security interest so granted effective against third parties.~~

2. - Intermediated securities shall be treated as delivered into ~~the possession or control of a collateral taker if-~~

~~_____ (a) the relevant securities they are credited to a securities account of the collateral taker, [(in which case the provisions of Article 5 apply)];-~~

3. - Intermediated securities shall also be treated as delivered to a collateral taker –

_____ (a)(b) if the relevant intermediary is itself the collateral taker and the relevant Contracting State has made a declaration under paragraph 4 in respect of this sub-paragraph;

(b)(c) if a designating entry in favour of the collateral taker has been made and in the securities account in respect of the relevant intermediated securities and the making of such a designating entry is specified in a declaration by the relevant the relevant Contracting State has made a declaration under paragraph 4 in respect of this sub-paragraph; as sufficient to result, under the law of that Contracting State, in the intermediated securities being in the possession or control of the collateral taker; or

(c)(d) if a control agreement with the collateral taker applies to the relevant intermediated securities and the application of such a control agreement is specified in a declaration by the relevant Contracting State under paragraph 4 as sufficient to result, under the law of that Contracting State, in the intermediated securities being in the possession or control of the collateral taker and the relevant Contracting State has made a declaration under paragraph 4 in respect of this sub-paragraph.

4. - A Contracting State may ~~by declaration that under its domestic non-Convention law the condition specified in any one or more of sub-paragraphs (a) to (c) of paragraph 3 is sufficient to constitute delivery of intermediated securities to a collateral taker.[-~~

~~_____ (a)] state which of the conditions specified in paragraph 2(c) to (e) is sufficient, under the law of that Contracting State, to result, under the law of that Contracting State, in intermediated securities being in the possession or control of a collateral taker and describe the requirements under the law of that Contracting State for an effective designating entry or an effective control agreement[- and, or alternatively~~

~~_____ (b) describe the manner of holding or designation of securities credited to a securities account which, under the law of that Contracting State, is sufficient to result in the corresponding intermediated securities being in the possession or control of a collateral taker for the purposes of paragraph 2(f)].~~

5. - A Contracting State may declare that under its domestic non-Convention law~~may by declaration elect that~~ this Article shall not apply in relation to security interests in intermediated securities granted by or to parties ~~of such descriptions as may be falling within such categories as may be specified in the declaration.~~

~~63. - If the domestic non-Convention law so permits, A~~ security interest may be granted under this Article ~~_~~

~~_____ (a) in terms such that it extends to~~ in respect of a securities account (and such a security interest extends to all intermediated securities from time to time standing to the credit of the relevant securities account); or,

~~_____ (b) if the domestic non-Convention law so permits, to~~ in respect of a specified category, quantity, proportion or value ~~of such the~~ intermediated securities from time to time standing to the credit of a securities account. ~~Such a security interest is effective without the need for further identification of particular securities.~~

~~76. - The domestic non-Convention law determines:~~

(a) ~~whether and~~ in what circumstances a non-consensual security security interest in intermediated securities may arise ~~by operation of law and become effective against third parties;~~ and

(b) the evidential requirements in respect of whether a collateral agreement such an agreement as is referred to in paragraph 1(a) or and the delivery of intermediated securities into the possession or control of a collateral taker is required to be evidenced in writing or in a legally equivalent manner and whether such evidence must permit the identification of intermediated securities so delivered.

~~87. - This Article does not preclude any other method provided by the domestic non-Convention law for the grant of a security interest in intermediated securities, but the priority of a security interest granted by any such other method is subject to the rules in Article 640.~~

Article 406

[Priority among competing security interests]

1. - This Article determines priority between security interests in the same intermediated securities.

~~_____ 2. - Security interests that become effective against third parties arising under Article 5 and Article 56(3):~~

(a) have priority over any security interest that becomes effective against third parties created by any method permitted by the domestic non-Convention law other than those provided by Article 5(2) or (3)~~Article 5 or Article 6~~; and

(b) rank among themselves according to the time of in the order occurrence of the following events: in which they were created:

~~_____ (i) when the collateral agreement is entered into, if the relevant intermediary is itself the collateral taker;~~

_____ (ii) when a designating entry is made;

_____ (iii) when a control agreement is entered into, or, if applicable, a notice is given to the relevant intermediary.

3. - Where an intermediary enters into a control agreement with a collateral taker or makes a designating entry in favour of a collateral taker, the security interest of the collateral taker has priority over any security interest of the intermediary that is effective against third parties under Article 5(3).

42. - ~~—~~ A non-consensual security interest in intermediated securities arising or recognised by operation of law under any rule of the domestic non-Convention law has such priority as is afforded to it by that law~~the rule in question~~.

53. - Subject to paragraph ~~21~~ and paragraph ~~2~~, the priority of any competing security interests in the same intermediated securities is determined by the domestic non-Convention law.

64. - As between persons entitled to any security interests referred to in ~~this Article~~ paragraph 2, paragraph 3 and, to the extent permitted by the domestic non-Convention law, paragraph 4, the priorities provided by the preceding paragraphs may be varied by agreement between those persons, but any such agreement does not affect third parties.

Article ~~41~~7

[Acquisition by an innocent person of intermediated securities]

1. - ~~Where securities are credited~~ A person who acquires intermediated securities by credit to a securities account under Article ~~45~~, or who acquires a security interest in such securities by an agreement or designation under Article ~~6~~, and who ~~the~~ account holder does not at the time of acquisition ~~the~~ credit have knowledge of an adverse claim with respect to the securities ~~—~~

_____ (a) the account holder is not subject to ~~that~~ adverse claim;

_____ (b) the account holder is not liable to the holder of the adverse claim; and

_____ (c) the credit is not ineffective or reversible on the ground that the adverse claim² affects any previous debit or credit made to another securities account.

2. - Paragraph 1 does not apply in respect of an acquisition of securities, other than the grant of a security interest, made~~[, or the creation of a security interest effected,]~~ by way of gift or otherwise gratuitously.

3. - An intermediary who makes a debit, credit, or designating entry to a securities account is not liable to the holder of an adverse claim with respect to intermediated securities unless at the time of such debit, credit or designating entry the intermediary has knowledge of the adverse claim.

43. - For the purposes of this Article a person acts with knowledge of an adverse claim if that person:

(a) has actual knowledge of the adverse claim; or

² Further consideration to be given to whether to deal specifically with adverse claims of the intermediary (e.g. by amending the definition of adverse claim).

(b) has knowledge of facts sufficient to indicate that there is a significant probability that the adverse claim exists and deliberately avoids information that would establish the existence of the adverse claim;

and knowledge received by an organisation is effective for a particular transaction from the time when it is or ought reasonably to have been brought to the attention of the individual conducting that transaction.

5. - Notwithstanding Article 8[(2)], if:

(a) securities have been credited to a securities account of an account holder, or have been designated in favour of another person in the manner described in Article 5, in circumstances such that the credit or designating entry is not effective or is liable to be reversed; and

(b) before that credit or designating entry has been [cancelled or] reversed, the securities are credited to a securities account of a third party, or are designated in the manner described in Article 5 in favour of a third party (such a third party being in either case referred to in this sub-paragraph as “the acquirer”), under a further disposition,

the fact that the initial credit or designating entry was made in circumstances such that it is not effective or is liable to be reversed does not make the further credit or designating entry ineffective, in favour of the acquirer, against the person making the further disposition, the relevant intermediary or third parties unless:

(i) the further credit or designating entry is made conditionally and the condition has not been satisfied;

(ii) the acquirer has knowledge, at the time when the further credit or designating entry is made, that it is made as a result of the further disposition and that the further disposition is made in the circumstances referred to in this paragraph; or

(iii) the further disposition is made by way of gift or otherwise gratuitously.]³

6. - For the purposes of paragraph 5 the acquirer has knowledge that the further credit or designating entry is made as a result of a purported disposition made in the circumstances referred to in that paragraph if the acquirer has actual knowledge that it is so made, or has knowledge of facts sufficient to indicate that there is a significant probability that it is so made and deliberately avoids information that would establish that that is the case.]

Article 78

[Lack of Authorisation, ineffectiveness, timing, conditionality and reversal of debits, credits etc.]

1. - A debit ~~or credit~~ of securities to a securities account or a designating entry is not effective unless the relevant intermediary is authorised to make that debit, ~~credit~~, or designating entry:

(a) by the account holder and, in the case of a debit or designating entry that relates to intermediated securities which are subject to a security interest ~~arising~~^{granted} under Article ~~56(3)~~, by the collateral taker; or

(b) by the domestic non-Convention law.

³ Further consideration to be given to whether there should be a more general protection against reversal based on reversal etc. of earlier transactions; paragraphs 4 and 5 reproduce Article 7(6) and (7) of Doc.24.

~~2. – Except as otherwise provided by paragraph 4, a debit or credit of securities to a securities account or a designating entry takes effect when it is made.~~

~~3. – The time at which intermediated securities shall be treated as delivered into the possession or control of a collateral taker is as follows:~~

~~(a) in the circumstances specified in Article 6(2)(a), when the relevant securities are credited to a securities account of the collateral taker;~~

~~(b) in the circumstances specified in Article 6(2)(b), when the agreement between the account holder and the relevant intermediary by which the security interest is granted is entered into;~~

~~(c) in the circumstances specified in Article 6(2)(c), (d) or (e), when the relevant condition is fulfilled;~~

~~(d) in the circumstances specified in Article 6(2)(f), when the relevant securities are held or designated in the manner described in the declaration of the relevant Contracting State referred to in Article 6(4)].~~

25. - The domestic non-Convention law and, to the extent permitted by the domestic non-Convention law, an account agreement or the rules and agreements governing the operation of a settlement [or clearing] system, An account agreement, the rules of a clearing or settlement system or the domestic non-Convention law may provide that a debit or credit of securities or a designating entry is not effective or is liable to be reversed. [The domestic non-Convention law determines whether such a debit, credit or designating entry has any effect against third parties during the period before it is reversed and, if so, what that effect is.]

3. – Subject to Article 7, the domestic non-Convention law determines –

(a) where a debit or designating entry is not authorised or a debit, credit or designating entry is otherwise ineffective, the consequences of such ineffectiveness.

(b) where a debit, credit or designating entry is liable to be reversed, its effect (if any) against third parties and the consequences of reversal.

~~4. – A debit or credit of securities which is made conditionally under the terms of an account agreement, the rules of a securities clearing or settlement system or the domestic non-Convention law is effective against third parties when, and only when, the condition is satisfied]; but if the condition is satisfied, the relevant disposition or acquisition of intermediated securities is treated for the purposes of Article 10 as having become effective against third parties when the relevant debit or credit was made conditionally].~~

CHAPTER III – RIGHTS OF THE ACCOUNT HOLDER ~~PROTECTION OF INNOCENT ACQUIRER~~

Article 49 *[Intermediated securities]*

1. - The credit of securities to a securities account confers on the account holder:

(a) ~~subject to paragraph 2,~~ the right to receive and exercise the rights attached to the securities, including in particular dividends, other distributions and voting rights

(i); where the account holder is not an intermediary or is an intermediary acting for its own account; and,

~~_____ (ii) in any other case, if the domestic non-Convention law so provides.~~

~~(b) the right, by instructions to the relevant intermediary, to dispose of ~~cause~~ the securities in accordance with ~~to be debited to the securities account under Articles 45 and 5 and credited to a securities account of another account holder (whether with the relevant intermediary or another intermediary) or to be delivered into the possession or control of a collateral taker under Article 6;~~~~

~~_____ (c) the right, by instructions to the relevant intermediary, to cause the securities to be debited to the securities account under Article 5 and credited to a securities account of the account holder with a different intermediary;~~

~~(d)(c) the right, by instructions to the relevant intermediary, to cause the ~~withdraw~~ the securities ~~so as to be held by the account holder otherwise than through a securities account, to the extent permitted under the law under which the securities are constituted, the terms of the securities and the account agreement;~~~~

~~_____ (e)(d) subject to this Convention, such other rights as may be conferred by the domestic non-Convention law.~~

~~_____ 2. — Where securities are credited to a securities account of an account holder who is acting in the capacity of intermediary with respect to those securities, that account holder has the rights specified in paragraph 1(a) only if that account holder, or another intermediary through which, directly or indirectly, it holds the relevant securities, is entitled to those rights against the issuer under the terms of the relevant securities and the law under which the relevant securities are constituted.~~

~~3. —~~

~~_____ 2. - Unless otherwise provided in this Convention, Without prejudice to Article 15 and Article 19, the rights referred to in paragraph 1:~~

~~(a) the rights referred to in paragraph 1 are effective against ~~the relevant intermediary and third parties;~~ and~~

~~_____ (b) the rights referred to in paragraph 1(a) may be ~~enforced~~ exercised against the relevant intermediary or the issuer of the securities, or both, ~~and, to the extent provided by~~ in accordance with this Convention, the terms of the ~~relevant~~ securities and the law under which the ~~relevant~~ securities are constituted; ~~the issuer of the relevant securities.~~~~

~~_____ (c) the rights referred to in paragraph 1(b) and 1(c) may be exercised only against the relevant intermediary.~~

~~3[7. - Where securities are credited to a securities account of an account holder in the capacity of collateral taker under Article 56, the domestic non-Convention law determines any limits on the rights described in paragraph 1.~~

~~] _____ 4. — Subject to paragraph 5 and paragraph 6, an intermediary must take appropriate measures to enable its account holders to receive and exercise the rights specified in paragraph 1.~~

Article 10
[Measures to enable account
holders to receive and exercise rights]

1. - An intermediary must take appropriate measures to enable its account holders to receive and exercise the rights specified in Article 9(1), but this obligation does not require the relevant intermediary to take any action that is not within its power or to establish a securities account with another intermediary. ~~[Version A:~~

~~5. - Where the enjoyment of any of the rights referred to in paragraph 1 depends on the actions of the relevant intermediary, the scope of those rights is limited to such an extent as is necessary to ensure that the relevant intermediary is not required to take any action that is not within its power. This does not affect any right of the account holder against the issuer of the relevant securities conferred by this Convention, the terms of the relevant securities and the law under which the relevant securities are constituted.~~

~~6. - The manner of performance of any obligations of the relevant intermediary in respect of the rights of an account holder under paragraph 1, and the extent of the liability of the relevant intermediary for any failure to perform such obligations, are governed by the account agreement, the law by which the account agreement is governed and any applicable provision of the domestic non-Convention law.]~~

2. - This Article does not affect any right of the account holder against the issuer of the securities.

~~[Version B:~~

~~5. - To the extent that the rights referred to in paragraph 1 are dependent on the actions of the relevant intermediary, the account holder is not entitled to any such right to the extent that giving effect to the right:~~

~~_____ (a) is not within the power of the relevant intermediary;~~

~~_____ (b) would require the relevant intermediary to act in a manner that is [more burdensome than reasonable commercial standards or that is] not permitted by any applicable law or by the terms of the relevant securities;~~

~~_____ (c) would require the relevant intermediary to establish a securities account with another intermediary; or~~

~~_____ (d) is waived by the account holder in a manner permitted by the domestic non-Convention law.~~

~~6. - Subject to any applicable provision of the domestic non-Convention law, any obligation of the relevant intermediary in respect of the rights of the account holder under paragraph 1 shall be satisfied if the relevant intermediary acts with respect to that obligation:~~

~~_____ (a) in accordance with the account agreement or, if there is no account agreement, in accordance with [reasonable commercial standards];~~

~~_____ (b) in accordance with any other agreement between the account holder and the relevant intermediary; or~~

~~_____ (c) by placing the account holder in a position itself to exercise any relevant right referred to in paragraph 1.]~~

~~— [7. - Where securities are credited to a securities account of an account holder in the capacity of collateral taker under Article 6, the domestic non-Convention law determines any limits on the rights described in paragraph 1.]~~

~~Article 1211~~

~~[Rights of account holders onin case of insolvency of intermediary]~~

The rights of an account holder under Article 9(1)~~constituted by the credit of securities to a securities account, and the rights of a persona security interest that has become effective against third parties holding a security interest created under Article 56(2) or (3), are effective against the insolvency administrator and creditors in any insolvency proceeding in respect of the relevant intermediary.~~

~~Article 1412~~

~~[Effects of insolvency]~~

Subject to Article ~~2243~~ and Article 264, nothing in this Convention affects:

- (a) any rules of law applicable in insolvency proceedings relating to the avoidance of a transaction as a preference or a transfer in fraud of creditors; or
- (b) any rules of procedure relating to the enforcement of rights to property which is under the control or supervision of an insolvency administrator.

~~Article 1913~~

~~[Position of issuers of securities]~~

1. - The law of a Contracting State shall permit the holding through intermediaries of securities that are permitted to be traded on an exchange or regulated market, and the effective exercise of the rights attached to such securities which are so held. This is without prejudice to the terms of issue of the securities.~~— 1. - Any rule of law of a Contracting State, and any provision of the terms of issue of securities constituted under the law of a Contracting State, which would prevent the holding of securities with an intermediary or the effective exercise by an account holder of rights in respect of intermediated securities shall be modified to the extent required to make possible the holding of such securities with an intermediary and the effective exercise of such rights.~~

2. - In particular, the law of a Contracting State shall recognise the holding of securities described in paragraph 1 by a person acting in his own name on behalf of another person (including a nominee) and shall permit such a person to exercise voting or other rights in different ways in respect of different parts of a holding of securities of the same description.

~~— 2. - Without limiting the generality of Paragraph 1, that paragraph applies in particular to any rule or provision:~~

~~— (a) which restricts the ability of a holder of securities to exercise voting or other rights in different ways in respect of different parts of a holding of securities of the same description;~~

~~— (b) [which does not include adequate provision for making available to account holders holding intermediated securities, or to intermediaries for transmission to such account holders;~~

~~_____ (i) copies of notices, accounts, circulars and other materials addressed by the issuer to holders of such intermediated securities; and~~

~~_____ (ii) means of exercising the rights attached to the securities either in person or through a proxy or other representative;]~~

~~_____ (c) which prohibits or fails to recognise the holding of securities by a person acting in the capacity of nominee or intermediary;~~

~~_____ (d) under which recognition of the holding of securities by an intermediary or the exercise of rights by an account holder holding intermediated securities is conditional on the maintenance of records in a particular medium;~~

~~_____ (e) which 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 intermediary.~~

~~_____ [3. Subject to paragraph 1 and paragraph 2, nothing in this Convention makes an issuer of securities bound by, or compels such an issuer to recognise, a right or interest of any person in or in respect of such securities if the issuer is not bound by or compelled to recognise that right or interest under the law under which the securities are constituted and the terms of the securities.]~~

Article 2014

[Set-off]

1. - As between an account holder who holds intermediated securities for its own account and the issuer of those securities, the fact that the account holder holds the securities with an intermediary shall not of itself, in any insolvency proceeding in respect of the issuer, preclude the existence or prevent the exercise of any rights of set-off which would have existed and been exercisable if the account holder had held the securities- otherwise than through an intermediary.

2. - This Article does not affect any express provision of the terms of issue of the relevant securities.

CHAPTER IV ~~==~~

INTEGRITY OF THE INTERMEDIATED HOLDING SYSTEM ~~INSOLVENCY~~

Article 915

[Prohibition of upper-tier attachment]

1. - No attachment of or in respect of intermediated securities of an account holder shall be granted or made against the issuer of the relevant securities or against any intermediary other than the relevant intermediary.

2. - In this Article "*attachment*" means any judicial, administrative or other act or process for enforcing or satisfying a judgment, award or other judicial, arbitral, administrative or other decision against or in respect of the account holder or for freezing, restricting or impounding property of the account holder in order to ensure its availability to enforce or satisfy any future such judgment, award or decision.

CHAPTER V – DUTIES OF INTERMEDIARY*Article ~~15~~¹⁶**[Instructions to the intermediary]*

1. - Subject to paragraph 2 [and Article ~~8~~⁷(1)], an intermediary is neither bound nor entitled to give effect to any instructions with respect to intermediated securities of an account holder given by any person other than that account holder.

2. - Paragraph 1 is subject to:

(a) the provisions of the account agreement, any other agreement between the intermediary and the account holder or any other agreement entered into by the intermediary with the consent of the account holder;

(b) the rights of any person (including the intermediary) who holds a security interest created under Article ~~5~~⁶;

(c) subject to Article ~~15~~⁹, any judgment, award, order or decision of a court, tribunal or other judicial or administrative authority of competent jurisdiction;

(d) any mandatory rule of the domestic non-Convention- law; and

(e) where the intermediary is [the operator of] a securities settlement [or clearing] or settlement system, the rules of that system.

*Article ~~16~~¹⁷**[Requirement to hold sufficient securities ~~Duty of intermediary with respect to holding or credit of securities~~]*

~~[1. - An intermediary may not:~~

~~(a) make any credit of securities to a securities account maintained by it; or~~

~~(b) dispose of securities held by it or credited to a securities account which it holds with another intermediary,~~

~~if upon that credit or disposition becoming effective there would not be sufficient securities of the same description held by it or credited to securities accounts which it holds with another intermediary.]~~

1. - An intermediary must, for each description of securities, hold securities and intermediated securities of an aggregate number and amount at least equal to the aggregate number and amount of securities of that description credited to securities accounts which it maintains [for account holders]⁵.

2. - If at any time an intermediary does not hold sufficient securities and intermediated securities of any description ~~are not held by an intermediary~~ in accordance with paragraph 1 ~~or credited to securities accounts which it maintains with another intermediary~~, it must [immediately]

⁴ Articles 16, 17 and 18 are subject to modification in the light of further discussion of and possible changes to Articles 7, 10 and 11.

⁵ The square brackets in paragraph 1 reflect the need to ensure that the Convention does not relax more stringent requirements under a domestic non-Convention law that might, for example, require the intermediary to maintain with another intermediary securities sufficient to reflect securities that the intermediary carries on its books for its own account. Consideration may be given to addressing this issue more generally in the convention.

[promptly] take such action as is required to ensure that it holds sufficient securities and intermediated securities of that description ~~are so held or credited~~.

~~3. — In the preceding paragraphs “sufficient securities” of any description means securities of an aggregate number or amount at least equal to the aggregate number or amount of securities of that description credited to securities accounts maintained by the intermediary.~~

~~34. - The preceding paragraphs~~ Paragraph 2 does not affect any provision of the domestic non-Convention law, or, subject to the domestic non-Convention law, any provision of the rules of a securities settlement [or clearing] or settlement system or of an account agreement, relating to the allocation of the cost of ensuring compliance with the requirements of those paragraphs.

Article 18

[Application of domestic non-Convention law and account agreement to obligations of intermediary]

The obligations and duties of an intermediary under this Convention and the extent of the liability of an intermediary are subject to any applicable provision of the domestic non-Convention law and, to the extent permitted by that law, the account agreement.

~~5. — The fact that a credit or disposition is made in contravention of paragraph 1 does not render that credit or disposition ineffective, but:~~

~~(a) — the intermediary must comply with paragraph 2; and~~

~~(b) — this paragraph does not affect any liability of the intermediary to compensate an account holder for any loss arising from the contravention.]~~

Article 19

[Allocation of securities to account holders' rights: securities so allocated not property of the intermediary]

{1. - Securities of each description held by an intermediary or credited to securities accounts held by an intermediary with another intermediary shall be allocated to the rights of the account holders of that intermediary to the extent necessary to ensure that the aggregate number or amount of the securities of that description so allocated is equal to the aggregate number or amount of such securities credited to securities accounts maintained by the intermediary.}

{2. - Securities allocated under paragraph 1 shall not form part of the property of the intermediary available for distribution among or realisation for the benefit of its unsecured creditors in the event of an insolvency proceeding in respect of the intermediary or be otherwise subject to claims of unsecured creditors of the intermediary.}

3. - Subject to paragraph 4, the allocation required by paragraph 1 shall be effected by the domestic non-Convention law and, subject to the domestic non-Convention law, by arrangements made by the relevant intermediary.

~~4. — A Contracting State may by declaration elect that the allocation required by paragraph 1 shall be effected by arrangements for the segregation of securities held by the relevant intermediary or credited to securities accounts held by the relevant intermediary with another intermediary sufficient to ensure, under the law of that Contracting State, that the securities so segregated are allocated to the rights of the account holders of the relevant intermediary.~~ 4. - A Contracting State may declare that under its domestic non-Convention law the allocation required by paragraph 1 applies only to securities that are held by the relevant

intermediary with another intermediary under an arrangement for the segregation of securities held by the relevant intermediary for the benefit of its account holders and does not apply to securities held with another intermediary for the relevant intermediary's own account.

Article 1820

[Loss sharing in case of insolvency of the intermediary Effect of insufficiency of securities held in respect of account holders' rights]

1. - In any insolvency proceeding in respect of an intermediary, if the aggregate number or amount of securities and intermediated securities of any description held by an intermediary or credited to a securities account that it holds with another intermediary is less than the aggregate number or amount of securities of that description credited to securities accounts, the shortfall shall be allocated:

~~_____~~ and

~~(a)(b)~~ subject to sub-paragraph ~~(b)(a)~~, shall be allocated among the account holders to whose securities accounts securities of the relevant description are credited, in proportion to the respective numbers or amounts of securities so credited; ~~or~~

~~(b)(a)~~ where the intermediary is [the operator of] a securities settlement [or clearing] or settlement system and the rules or agreements governing the operation of the system make provision for the allocation ~~elimination~~ of the shortfall, ~~shall be allocated~~ in the manner so provided; ~~or~~

2. - [Unless otherwise provided by the domestic non-Convention law,] [I]n any allocation required under paragraph 1 ~~(a)~~ no account shall be taken of:

(a) the origin of, or any past dealings in, any securities held by the intermediary or credited to securities accounts held by the intermediary with another intermediary; or

(b) the order in which or time at which any securities are credited or debited to the respective securities accounts of account holders.

3. - The preceding paragraphs are subject to any conflicting rule applicable in the insolvency proceeding of the intermediary.

{Article 821

[Overriding effect of certain rules of securities settlement [or clearing] clearing or settlement systems]

Any provision of the rules or agreements governing the operation of a securities settlement [or clearing] or settlement system [which is directed to the stability of the system or the finality of ~~dispositions transactions~~ effected through the system] shall, to the extent of any inconsistency, prevail over ~~{any provision of in [Articles 8, X, Y, ...7] [any provision of this Convention].}~~

{Article 1322

[Effectiveness of debits, credits etc. and instructions on insolvency of operator or participant in securities ~~clearing or settlement~~ [or clearing] system]

1. - Any provision of the rules or agreements governing the operation of a securities ~~clearing or settlement [or clearing]~~ system [which is directed to the stability of the system or the finality of ~~acquisitions or dispositions transaction~~ effected through the system] shall have effect notwithstanding the commencement of an insolvency proceeding in respect of [the operator of] the system or any participant in the system to the extent in so far as that that provision:

(a) precludes the invalidation or reversal of ~~any acquisition or disposition effected by~~ a debit or credit of securities to, or a designating entry in, a securities account which forms part of the system after the time at which that ~~acquisition or disposition debit, credit or designating entry~~ is treated as final under the rules of the system;

(b) precludes the revocation of any instruction given by a participant in the system for making a disposition of securities, or for making a payment relating to an acquisition or disposition of securities, after the time at which that instruction is treated under the rules of the system as having been entered irrevocably into the system.

2. - Paragraph 1 applies notwithstanding that any invalidation, reversal or revocation referred to in that paragraph would otherwise occur by mandatory operation of the insolvency law of a Contracting State.}]

~~CHAPTER VI – RELATIONS WITH ISSUERS OF SECURITIES~~

~~CHAPTER VII – SPECIAL PROVISIONS WITH RESPECT TO COLLATERAL TRANSACTIONS⁶~~

~~Article 2123~~

~~[Scope and interpretation of terms used in Chapter VII]~~

~~1. - This Chapter applies to collateral agreements under which a collateral provider delivers intermediated securities to a collateral taker under Article 5(2) or Article 5(3) in order to secure the performance of any existing or future obligation of the collateral provider or a third person.~~

~~2. - In this Chapter –~~

~~(a) “enforcement event” means, in relation to a collateral agreement, an event on the occurrence of which, under the terms of that collateral agreement, the collateral taker is entitled to enforce its security;~~

~~(b) “collateral securities” means intermediated securities delivered under a collateral agreement;~~

~~(c) “secured obligations” means the obligations secured by a collateral agreement.~~

~~In this Chapter:~~

~~(a) “collateral agreement”, “collateral provider”, “collateral taker”, “collateral securities” and “secured obligations” have the meanings respectively given in Article 22(1);~~

~~(b) “enforcement event” means, in relation to a collateral agreement, an event on the occurrence of which, under the terms of that collateral agreement, the collateral taker is entitled to enforce its security;~~

⁶ Further consideration will be given to the terminology of this Chapter and its consistency with that of the remainder of the preliminary draft Convention.

Article 2224
[Enforcement]

~~1. — This Article applies in respect of an agreement (a “collateral agreement”) under which a person [other than a natural person] (the “collateral provider”) creates a security interest in favour of another person (the “collateral taker”) in intermediated securities which are of a kind regularly traded on a financial market (the “collateral securities”) in order to secure the performance of [any existing or future obligations of the collateral provider or a third person] [financial obligations of any kind referred to in paragraph 2] (the “secured obligations”).~~

~~[2. — The secured obligations may consist of or include any obligation of a financial character, including:~~

~~———— (a) present or future, actual or contingent or prospective obligations (including obligations arising under a master agreement, whether under a provision for the acceleration or close-out of obligations or otherwise);~~

~~———— (b) obligations to deliver securities or other property;~~

~~———— (c) obligations owed to the collateral taker by a person other than the collateral provider;~~

~~———— (d) obligations of a specified description arising from time to time.]~~

13. - On the occurrence of an enforcement event, the collateral taker may realise the collateral securities:

(a) by selling them and applying the net proceeds of sale in or towards the discharge of the secured obligations;

(b) by appropriating the collateral securities as the collateral taker’s own property and setting off their value against, or applying their value in or towards the discharge of, the secured obligations, provided that the collateral agreement provides for realisation in this manner and specifies the basis on which collateral securities are to be valued for this purpose.

24. - Collateral securities may be realised under paragraph 13:

(a) subject to any contrary provision of the collateral agreement, without any requirement that:

(i) prior notice of the intention to realise shall have been given;

(ii) the terms of the realisation be approved by any court, public officer or other person; or

(iii) the realisation be conducted by public auction or in any other prescribed manner; and

(b) notwithstanding the commencement or continuation of an insolvency proceeding in respect of the collateral provider or the collateral taker.

3. - A collateral agreement may provide that, if an enforcement event occurs before the secured obligations have been fully discharged, either or both of the following shall occur, or may at the election of the collateral taker occur, whether through the operation of netting or set-off or otherwise:

(a) the respective obligations of the parties are accelerated so as to be immediately due and expressed as an obligation to pay an amount representing their estimated current value or are terminated and replaced by an obligation to pay such an amount;

_____ (b) an account is taken of what is due from each party to the other in respect of such obligations, and a net sum equal to the balance of the account is payable by the party from whom the larger amount is due to the other party.

_____ 45. - This Article Paragraph 3 and paragraph 4 are is without prejudice to any requirement of the domestic non-Convention law to the effect that the realisation or valuation of ~~financial~~ collateral securities ~~and or~~ the calculation of ~~any the relevant financial~~ obligations must be conducted in a commercially reasonable manner.

Article ~~23~~25

[Right to use collateral securities]

1. - If and to the extent that the terms of a collateral agreement so provide (or, where collateral securities are delivered to the collateral taker under Article 5(2), if and to the extent that the terms of the collateral agreement do not provide otherwise), the collateral taker shall have the right to use and dispose of the collateral securities as if it were the owner of them (a “*right of use*”).

2. - Where a collateral taker exercises a right of use, it thereby incurs an obligation to replace the collateral securities originally transferred (the “*original collateral securities*”) by transferring to the collateral provider, not later than the discharge of the secured obligations, securities of the same issuer or debtor, forming part of the same issue or class and of the same nominal amount, currency and description or, where the collateral agreement provides for the transfer of other assets [following the occurrence of any event relating to or affecting any securities provided as collateral], those other assets.

3. - Securities transferred under paragraph 2 before the secured obligations have been fully discharged:

(a) shall, in the same manner as the original collateral securities, be subject to a security interest under the relevant collateral agreement, which shall be treated as having been created at the same time as the security interest in respect of the original collateral securities was created; and

(b) shall in all other respects be subject to the terms of the relevant collateral agreement.

4. - The exercise of a right of use shall not render invalid or unenforceable any right of the collateral taker under the relevant collateral agreement.

~~5. - A collateral agreement may provide that, if an enforcement event occurs before the secured obligations have been fully discharged, either or both of the following shall occur, or may at the election of the collateral taker occur, whether through the operation of netting or set-off or otherwise:~~

~~_____ (a) the respective obligations of the parties are accelerated so as to be immediately due and expressed as an obligation to pay an amount representing their estimated current value or are terminated and replaced by an obligation to pay such an amount;~~

~~_____ (b) an account is taken of what is due from each party to the other in respect of such obligations, and a net sum equal to the balance of the account is payable by the party from whom the larger amount is due to the other party.~~

*Article 2426**[Top-up or substitution of collateral]*

Where a collateral agreement includes:

(a) an obligation to deliver collateral securities or additional collateral securities ~~[in order to take account of changes in the value of the collateral provided under the relevant collateral agreement or in the amount of the secured obligations]~~ [in order to take account of any circumstances giving rise to an increase in the credit risk incurred by the collateral taker] ~~[or, to the extent permitted by the applicable law as determined by the private international law rules of the forum, in any other circumstances specified in the relevant collateral agreement];~~ or

(b) a right to withdraw collateral securities or other assets on providing collateral securities or other assets of substantially the same value,

the provision of securities or other assets as described in paragraph (a) and paragraph (b) shall not be treated as invalid, reversed or declared void solely on the basis that they are provided during a prescribed period before, or on the day of but before, the commencement of an insolvency proceeding in respect of the collateral provider, or after the secured obligations have been incurred.

*Article 2527**[Declarations in respect of Chapter VII]*

1. - A Contracting State may ~~declare by declaration~~ elect that this Chapter shall not apply ~~in respect under its domestic non-Convention law of the law of that Contracting State.~~

2. - A Contracting State may declare that under its domestic non-Convention law ~~by declaration~~ elect that this Chapter shall not apply in ~~in~~ —

(a) in relation to collateral agreements entered into by natural persons or persons falling within such other categories as may be specified in the declaration; ~~security interests in intermediated securities granted by or to parties of such descriptions as may be specified in the declaration;~~

(b) in relation to intermediated securities which are not permitted to be traded on an exchange or regulated market;

(c) in relation to collateral agreements which provide for secured obligations falling within such categories as may be specified in the declaration.

APPENDIX 2

PRELIMINARY DRAFT CONVENTION ON SUBSTANTIVE RULES REGARDING INTERMEDIATED SECURITIES

CHAPTER I - DEFINITIONS, SCOPE OF APPLICATION AND INTERPRETATION

Article 1 *[Definitions]*

In this Convention:

(a) *“securities”* means any shares, bonds or other financial instruments or financial assets (other than cash) or any interest therein, which are capable of being credited to a securities account;

(b) *“securities account”* means an account maintained by an intermediary to which securities may be credited or debited;

(c) *“intermediary”* means a person that in the course of a business or other regular activity maintains securities accounts for others or both for others and for its own account and is acting in that capacity;

(d) *“account holder”* means a person in whose name an intermediary maintains a securities account, whether that person is acting for its own account or for others (including in the capacity of intermediary);

(e) *“account agreement”* means, in relation to a securities account, the agreement with the relevant intermediary governing that securities account;

(f) *“intermediated securities”* means the rights of an account holder resulting from a credit of securities to a securities account¹;

(g) *“relevant intermediary”* means, with respect to a securities account, the intermediary that maintains the securities account for the account holder;

(h) *“disposition”* means an act of an account holder disposing of intermediated securities and includes a transfer of title, whether outright or by way of security, and a grant of a security interest;

(i) *“adverse claim”* means, with respect to any securities, a claim that a person has an interest in those securities that is effective against third parties and that it is a violation of the rights of that person for another person to hold or dispose of those securities;

(j) *“insolvency proceeding”* means a collective judicial or administrative proceeding, including an interim proceeding, in which the assets and affairs of the debtor are subject to control or supervision by a court or other competent authority for the purpose of reorganisation or liquidation;

(k) *“insolvency administrator”* means a person (including a debtor in possession where applicable) authorised to administer an insolvency proceeding, including one authorised on an interim basis;

¹ This definition remains under consideration. Questions have been raised, for example, as to the appropriateness of the particular term “intermediated securities”, as to whether it should be replaced by “intermediated rights”, and as to whether the definition should be expanded so as to include terms that currently form part of Article 4.

(l) securities are “*of the same description*” as other securities if they are issued by the same issuer and:

(i) they are of the same class of shares or stock; or

(ii) in the case of securities other than shares or stock, they are of the same currency and denomination and form part of the same issue;

(m) “*control agreement*” means an agreement between an account holder, the relevant intermediary and a collateral taker, or, if so permitted by the domestic non-Convention law, an agreement between an account holder and a collateral taker of which notice is given to the relevant intermediary, which relates to intermediated securities and provides that, in such circumstances and as to such matters as may be specified in the agreement or provided by the domestic non-Convention law, the relevant intermediary is not permitted to comply with any instruction given by the account holder without having received the consent of the collateral taker, or is obliged to comply with any instructions given by the collateral taker without any further consent of the account holder;

(n) “*designating entry*” means an entry in a securities account made in favour of a collateral taker in respect of the securities account or in respect of specified securities credited to the securities account, which, under the account agreement, a control agreement or the domestic non-Convention law, has the effect that, in specified circumstances and as to specified matters, the relevant intermediary is not permitted to comply with any instructions given by the account holder without having received the consent of the collateral taker, or is obliged to comply with any instructions given by the collateral taker without any further consent of the account holder;

(o) “*domestic non-Convention law*” means the domestic provisions of law of the State whose law is applicable under Article 2, other than those provided in this Convention;

(p) “non-consensual security interest” [to be defined];

(q) “securities settlement [or clearing] system” means [a system] [an entity] which:

(i) clears, settles or clears and settles securities transactions;

(ii) [has rules and agreements with its participants that are publicly accessible];

(iii) is operated by a central bank or conducts operations that are supervised [by a regulator that has oversight over its rules and agreements];

(iv) has been notified as a securities settlement [or clearing] system in a declaration by a Contracting State, [or falls within a category of [systems] [entities] that have been notified as securities settlement [or clearing] systems in a declaration by a Contracting State and has been specifically identified as falling within that category in a publicly accessible website of its regulator which also specifies the date on which it first was designated as falling within that category];

provided that a declaration referred to in this sub-paragraph must be made on the grounds of the reduction of risk to the stability of the financial system;

(r) “collateral taker” means a person to whom a security interest in intermediated securities is granted;

(s) “collateral provider” means an account holder by whom a security interest in intermediated securities is granted;

(t) “collateral agreement” means an agreement between a collateral provider and a collateral taker providing (in whatever terms) for the grant of a security interest in intermediated securities.

Article 2
[Scope of application]

This Convention applies where rules of private international law of the forum state designate the law of a Contracting State.

Article 3
[Principles of interpretation]

1. - In the implementation, interpretation and application of this Convention, regard is to be had to its purposes, to its international character and to the need to promote uniformity and predictability in its application.

2. - Questions concerning matters governed by this Convention which are not expressly settled in the Convention are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the domestic non-Convention law.

CHAPTER II – TRANSFER OF INTERMEDIATED SECURITIES

Article 4
[Acquisition and disposition of intermediated securities]

1. - Intermediated securities are acquired by an account holder by the credit of securities to that account holder's securities account.

2. - No further step is necessary, or may be required by the domestic non-Convention law, to render the acquisition of intermediated securities effective against third parties.

3. - Intermediated securities are disposed of by an account holder by the debit of securities to that account holder's securities account.

4. - 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, a debit or credit of securities to a securities account is not ineffective because it is not possible to identify a securities account to which a corresponding credit or debit has been made.

5. - Debits and credits to securities accounts in respect of securities of the same description may be effected on a net basis.

6. - This Article does not preclude any other method provided by the domestic non-Convention law for the acquisition or disposition of intermediated securities.

Article 5
[Security interests in intermediated securities]

1. - An account holder may grant to a collateral taker a security interest in intermediated securities so as to be effective against third parties by:

- (a) entering into a collateral agreement with the collateral taker; and

- (b) delivering the intermediated securities to the collateral taker;

and no further step is necessary, or may be required by the domestic non-Convention law.

2. - Intermediated securities shall be treated as delivered to a collateral taker if they are credited to a securities account of the collateral taker.

3. – Intermediated securities shall also be treated as delivered to a collateral taker –

- (a) if the relevant intermediary is itself the collateral taker and the relevant Contracting State has made a declaration under paragraph 4 in respect of this sub-paragraph;

- (b) if a designating entry has been made and the relevant Contracting State has made a declaration under paragraph 4 in respect of this sub-paragraph; or

- (c) if a control agreement applies and the relevant Contracting State has made a declaration under paragraph 4 in respect of this sub-paragraph.

4. - A Contracting State may declare that under its domestic non-Convention law the condition specified in any one or more of sub-paragraphs (a) to (c) of paragraph 3 is sufficient, to constitute delivery of intermediated securities to a collateral taker.

5. - A Contracting State may declare that under its domestic non-Convention law this Article shall not apply in relation to security interests in intermediated securities granted by or to parties falling within such categories as may be specified in the declaration.

6. - If the domestic non-Convention law so permits, a security interest may be granted –

- (a) in respect of a securities account (and such a security interest extends to all intermediated securities from time to time standing to the credit of the relevant securities account); or,

- (b) in respect of a specified category, quantity, proportion or value of the intermediated securities from time to time standing to the credit of a securities account.

7. - The domestic non-Convention law determines:

- (a) in what circumstances a non-consensual security interest in intermediated securities may arise and become effective against third parties; and

- (b) the evidential requirements in respect of a collateral agreement and the delivery of intermediated securities to a collateral taker.

8. - This Article does not preclude any other method provided by the domestic non-Convention law for the grant of a security interest in intermediated securities, but the priority of a security interest granted by any such other method is subject to the rules in Article 6.

Article 6

[Priority among competing security interests]

1. - This Article determines priority between security interests in the same intermediated securities.

2. - Security interests that become effective against third parties under Article 5(3):

- (a) have priority over any security interest that becomes effective against third parties by any method permitted by the domestic non-Convention law other than those provided by Article 5(2) or (3); and

(b) rank among themselves according to the time of occurrence of the following events:

(i) when the collateral agreement is entered into, if the relevant intermediary is itself the collateral taker;

(ii) when a designating entry is made;

(iii) when a control agreement is entered into, or, if applicable, a notice is given to the relevant intermediary.

3. - Where an intermediary enters into a control agreement with a collateral taker or makes a designating entry in favour of a collateral taker, the security interest of the collateral taker has priority over any security interest of the intermediary that is effective against third parties under Article 5(3).

4. - A non-consensual security interest in intermediated securities arising or recognised under any rule of the domestic non-Convention law has such priority as is afforded to it by that law.

5. - Subject to paragraph 2, the priority of any competing security interests in the same intermediated securities is determined by the domestic non-Convention law.

6. - As between persons entitled to any security interests referred to in paragraph 2, paragraph 3 and, to the extent permitted by the domestic non-Convention law, paragraph 4, the priorities provided by the preceding paragraphs may be varied by agreement between those persons, but any such agreement does not affect third parties.

Article 7

[Acquisition by an innocent person of intermediated securities]

1. - Where securities are credited to a securities account under Article 4 and the account holder does not at the time of the credit have knowledge of an adverse claim with respect to the securities -

(a) the account holder is not subject to the adverse claim;

(b) the account holder is not liable to the holder of the adverse claim; and

(c) the credit is not ineffective or reversible on the ground that the adverse claim² affects any previous debit or credit made to another securities account.

2. - Paragraph 1 does not apply in respect of an acquisition of securities, other than the grant of a security interest, made by way of gift or otherwise gratuitously.

3. - An intermediary who makes a debit, credit, or designating entry to a securities account is not liable to the holder of an adverse claim with respect to intermediated securities unless at the time of such debit, credit or designating entry the intermediary has knowledge of the adverse claim.

4. - For the purposes of this Article a person acts with knowledge of an adverse claim if that person:

² Further consideration to be given to whether to deal specifically with adverse claims of the intermediary (e.g. by amending the definition of adverse claim).

(a) has actual knowledge of the adverse claim; or

(b) has knowledge of facts sufficient to indicate that there is a significant probability that the adverse claim exists and deliberately avoids information that would establish the existence of the adverse claim;

and knowledge received by an organisation is effective for a particular transaction from the time when it is or ought reasonably to have been brought to the attention of the individual conducting that transaction.

[5. - Notwithstanding Article 8[(2)], if:

(a) securities have been credited to a securities account of an account holder, or have been designated in favour of another person in the manner described in Article 5, in circumstances such that the credit or designating entry is not effective or is liable to be reversed; and

(b) before that credit or designating entry has been [cancelled or] reversed, the securities are credited to a securities account of a third party, or are designated in the manner described in Article 5 in favour of a third party (such a third party being in either case referred to in this sub-paragraph as "*the acquirer*"), under a further disposition,

the fact that the initial credit or designating entry was made in circumstances such that it is not effective or is liable to be reversed does not make the further credit or designating entry ineffective, in favour of the acquirer, against the person making the further disposition, the relevant intermediary or third parties unless:

(i) the further credit or designating entry is made conditionally and the condition has not been satisfied;

(ii) the acquirer has knowledge, at the time when the further credit or designating entry is made, that it is made as a result of the further disposition and that the further disposition is made in the circumstances referred to in this paragraph; or

(iii) the further disposition is made by way of gift or otherwise gratuitously.]³

[6. - For the purposes of paragraph 5 the acquirer has knowledge that the further credit or designating entry is made as a result of a purported disposition made in the circumstances referred to in that paragraph if the acquirer has actual knowledge that it is so made, or has knowledge of facts sufficient to indicate that there is a significant probability that it is so made and deliberately avoids information that would establish that that is the case.]

Article 8

[Lack of authorisation, ineffectiveness and reversal]

1. - A debit of securities to a securities account or a designating entry is not effective unless the relevant intermediary is authorised to make that debit or designating entry:

(a) by the account holder and, in the case of a debit or designating entry that relates to intermediated securities which are subject to a security interest arising under Article 5(3), by the collateral taker; or

(b) by the domestic non-Convention law.

³ Further consideration to be given to whether there should be a more general protection against reversal based on reversal etc. of earlier transactions; paragraphs 4 and 5 reproduce Article 7(6) and (7) of Doc. 24.

2. - The domestic non-Convention law and, to the extent permitted by the domestic non-Convention law, an account agreement or the rules and agreements governing the operation of a settlement [or clearing] system, may provide that a debit or credit of securities or a designating entry is not effective or is liable to be reversed.

3. – Subject to Article 7, the domestic non-Convention law determines –

(a) where a debit or designating entry is not authorised or a debit, credit or designating entry is otherwise ineffective, the consequences of such ineffectiveness;

(b) where a debit, credit or designating entry is liable to be reversed, its effect (if any) against third parties and the consequences of reversal.

CHAPTER III – RIGHTS OF THE ACCOUNT HOLDER

Article 9 *[Intermediated securities]*

1. - The credit of securities to a securities account confers on the account holder:

(a) the right to receive and exercise the rights attached to the securities, including in particular dividends, other distributions and voting rights

(i) where the account holder is not an intermediary or is an intermediary acting for its own account; and,

(ii) in any other case, if the domestic non-Convention law so provides;

(b) the right, by instructions to the relevant intermediary, to dispose of the securities in accordance with Articles 4 and 5;

(c) the right, by instructions to the relevant intermediary, to cause the securities to be held otherwise than through a securities account, to the extent permitted under the law under which the securities are constituted, the terms of the securities and the account agreement;

(d) subject to this Convention, such other rights as may be conferred by the domestic non-Convention law.

2. - Unless otherwise provided in this Convention,

(a) the rights referred to in paragraph 1 are effective against third parties;

(b) the rights referred to in paragraph 1(a) may be exercised against the relevant intermediary or the issuer of the securities, or both, in accordance with this Convention, the terms of the securities and the law under which the securities are constituted;

(c) the rights referred to in paragraph 1(b) and 1(c) may be exercised only against the relevant intermediary.

3. - Where securities are credited to a securities account of an account holder in the capacity of collateral taker under Article 5, the domestic non-Convention law determines any limits on the rights described in paragraph 1.

Article 10
[Measures to enable account
holders to receive and exercise rights]

1. - An intermediary must take appropriate measures to enable its account holders to receive and exercise the rights specified in Article 9(1), but this obligation does not require the relevant intermediary to take any action that is not within its power or to establish a securities account with another intermediary.

2. - This Article does not affect any right of the account holder against the issuer of the securities.

Article 11
[Rights of account holders in case of insolvency of intermediary]

The rights of an account holder under Article 9(1), and a security interest that has become effective against third parties under Article 5(2) or (3), are effective against the insolvency administrator and creditors in any insolvency proceeding in respect of the relevant intermediary.

Article 12
[Effects of insolvency]

Subject to Article 22 and Article 26, nothing in this Convention affects:

- (a) any rules of law applicable in insolvency proceedings relating to the avoidance of a transaction as a preference or a transfer in fraud of creditors; or
- (b) any rules of procedure relating to the enforcement of rights to property which is under the control or supervision of an insolvency administrator.

Article 13
[Position of issuers of securities]

1. - The law of a Contracting State shall permit the holding through intermediaries of securities that are permitted to be traded on an exchange or regulated market, and the effective exercise of the rights attached to such securities which are so held. This is without prejudice to the terms of issue of the securities.

2. - In particular, the law of a Contracting State shall recognise the holding of securities described in paragraph 1 by a person acting in his own name on behalf of another person (including a nominee) and shall permit such a person to exercise voting or other rights in different ways in respect of different parts of a holding of securities of the same description.

Article 14
[Set-off]

1. - As between an account holder who holds intermediated securities for its own account and the issuer of those securities, the fact that the account holder holds the securities with an intermediary shall not of itself, in any insolvency proceeding in respect of the issuer, preclude the existence or prevent the exercise of any rights of set-off which would have existed and been exercisable if the account holder had held the securities otherwise than through an intermediary.

2. - This Article does not affect any express provision of the terms of issue of the securities.

CHAPTER IV – INTEGRITY OF THE INTERMEDIATED HOLDING SYSTEM

Article 15

[Prohibition of upper-tier attachment]

1. - No attachment of or in respect of intermediated securities of an account holder shall be granted or made against the issuer of the relevant securities or against any intermediary other than the relevant intermediary.

2. - In this Article "*attachment*" means any judicial, administrative or other act or process for enforcing or satisfying a judgment, award or other judicial, arbitral, administrative or other decision against or in respect of the account holder or for freezing, restricting or impounding property of the account holder in order to ensure its availability to enforce or satisfy any future such judgment, award or decision.

Article 16

[Instructions to the intermediary]

1. - Subject to paragraph 2 [and Article 8(1)], an intermediary is neither bound nor entitled to give effect to any instructions with respect to intermediated securities of an account holder given by any person other than that account holder.

2. - Paragraph 1 is subject to:

(a) the provisions of the account agreement, any other agreement between the intermediary and the account holder or any other agreement entered into by the intermediary with the consent of the account holder;

(b) the rights of any person (including the intermediary) who holds a security interest created under Article 5;

(c) subject to Article 15, any judgment, award, order or decision of a court, tribunal or other judicial or administrative authority of competent jurisdiction;

(d) any mandatory rule of the domestic non-Convention law; and

(e) where the intermediary is [the operator of] a securities settlement [or clearing] system, the rules of that system.

Article 17

[Requirement to hold sufficient securities]

1. - An intermediary must, for each description of securities, hold securities and intermediated securities of an aggregate number and amount at least equal to the aggregate

number and amount of securities of that description credited to securities accounts which it maintains [for account holders]⁴.

2. - If at any time an intermediary does not hold sufficient securities and intermediated securities of any description in accordance with paragraph 1, it must [immediately] [promptly] take such action as is required to ensure that it holds sufficient securities and intermediated securities of that description.

3. - The preceding paragraphs do not affect any provision of the domestic non-Convention law, or, subject to the domestic non-Convention law, any provision of the rules of a securities settlement [or clearing] system or of an account agreement, relating to the allocation of the cost of ensuring compliance with the requirements of those paragraphs.

Article 18

[Application of domestic non-Convention law and account agreement to obligations of intermediary]

The obligations and duties of an intermediary under this Convention and the extent of the liability of an intermediary are subject to any applicable provision of the domestic non-Convention law and, to the extent permitted by that law, the account agreement.

Article 19

[Allocation of securities to account holders' rights: securities so allocated not property of the intermediary]

1. - Securities of each description held by an intermediary or credited to securities accounts held by an intermediary with another intermediary shall be allocated to the rights of the account holders of that intermediary to the extent necessary to ensure that the aggregate number or amount of the securities of that description so allocated is equal to the aggregate number or amount of such securities credited to securities accounts maintained by the intermediary.

2. - Securities allocated under paragraph 1 shall not form part of the property of the intermediary available for distribution among or realisation for the benefit of its unsecured creditors in the event of an insolvency proceeding in respect of the intermediary or be otherwise subject to claims of unsecured creditors of the intermediary.

3. - Subject to paragraph 4, the allocation required by paragraph 1 shall be effected by the domestic non-Convention law and, subject to the domestic non-Convention law, by arrangements made by the relevant intermediary.

4. - A Contracting State may declare that under its domestic non-Convention law the allocation required by paragraph 1 applies only to securities that are held by the relevant intermediary with another intermediary under an arrangement for the segregation of securities held by the relevant intermediary for the benefit of its account holders and does not apply to securities held with another intermediary for the relevant intermediary's own account.

⁴ The square brackets in paragraph 1 reflect the need to ensure that the Convention does not relax more stringent requirements under a domestic non-Convention law that might, for example, require the intermediary to maintain with another intermediary securities sufficient to reflect securities that the intermediary carries on its books for its own account. Consideration may be given to addressing this issue more generally in the convention.

*Article 20**[Loss sharing in case of insolvency of the intermediary]*

1. - In any insolvency proceeding in respect of an intermediary, if the aggregate number or amount of securities and intermediated securities of any description held by an intermediary is less than the aggregate number or amount of securities of that description credited to securities accounts, the shortfall shall be allocated:

(a) subject to sub-paragraph (b), among the account holders to whose securities accounts securities of the relevant description are credited, in proportion to the respective numbers or amounts of securities so credited; or

(b) where the intermediary is [the operator of] a securities settlement [or clearing] system and the rules or agreements governing the operation of the system make provision for the allocation of the shortfall, in the manner so provided.

2. - [Unless otherwise provided by the domestic non-Convention law,] [I]n any allocation required under paragraph 1(a) no account shall be taken of:

(a) the origin of, or any past dealings in, any securities held by the intermediary or credited to securities accounts held by the intermediary with another intermediary; or

(b) the order in which or time at which any securities are credited or debited to the respective securities accounts of account holders.

3. - The preceding paragraphs are subject to any conflicting rule applicable in the insolvency proceeding of the intermediary.

*Article 21**[Overriding effect of certain rules of securities settlement [or clearing] systems]*

Any provision of the rules or agreements governing the operation of a securities settlement [or clearing] system [which is directed to the stability of the system or the finality of transactions effected through the system] shall, to the extent of any inconsistency, prevail over any provision of [Articles 8,X,Y, ...] [this Convention].

*Article 22**[Effectiveness of debits, credits etc. and instructions on insolvency of operator or participant in securities settlement [or clearing] system]*

1. - Any provision of the rules or agreements governing the operation of a securities settlement [or clearing] system [which is directed to the stability of the system or the finality of transactions] shall have effect notwithstanding the commencement of an insolvency proceeding in respect of [the operator of] the system or any participant in the system in so far as that provision:

(a) precludes the invalidation or reversal of a debit or credit of securities to, or a designating entry in, a securities account which forms part of the system after the time at which that debit, credit or designating entry is treated as final under the rules of the system;

(b) precludes the revocation of any instruction given by a participant in the system for making a disposition of securities, or for making a payment relating to an acquisition or disposition of securities, after the time at which that instruction is treated under the rules of the system as having been entered irrevocably into the system.

2. - Paragraph 1 applies notwithstanding that any invalidation, reversal or revocation referred to in that paragraph would otherwise occur by mandatory operation of the insolvency law of a Contracting State.

CHAPTER V – SPECIAL PROVISIONS WITH RESPECT TO COLLATERAL TRANSACTIONS⁵

Article 23

[Scope and interpretation in Chapter V]

1. - This Chapter applies to collateral agreements under which a collateral provider delivers intermediated securities to a collateral taker under Article 5(2) or Article 5(3) in order to secure the performance of any existing or future obligation of the collateral provider or a third person.

2. - In this Chapter –

(a) “*enforcement event*” means, in relation to a collateral agreement, an event on the occurrence of which, under the terms of that collateral agreement, the collateral taker is entitled to enforce its security;

(b) “*collateral securities*” means intermediated securities delivered under a collateral agreement;

(c) “*secured obligations*” means the obligations secured by a collateral agreement.

Article 24

[Enforcement]

1. - On the occurrence of an enforcement event, the collateral taker may realise the collateral securities:

(a) by selling them and applying the net proceeds of sale in or towards the discharge of the secured obligations;

(b) by appropriating the collateral securities as the collateral taker’s own property and setting off their value against, or applying their value in or towards the discharge of, the secured obligations, provided that the collateral agreement provides for realisation in this manner and specifies the basis on which collateral securities are to be valued for this purpose.

2. - Collateral securities may be realised under paragraph 1:

(a) subject to any contrary provision of the collateral agreement, without any requirement that:

(i) prior notice of the intention to realise shall have been given;

(ii) the terms of the realisation be approved by any court, public officer or other person; or

(iii) the realisation be conducted by public auction or in any other prescribed manner; and

⁵ Further consideration will be given to the terminology of this Chapter and its consistency with that of the remainder of the preliminary draft Convention.

(b) notwithstanding the commencement or continuation of an insolvency proceeding in respect of the collateral provider or the collateral taker.

3. - A collateral agreement may provide that, if an enforcement event occurs before the secured obligations have been fully discharged, either or both of the following shall occur, or may at the election of the collateral taker occur, whether through the operation of netting or set-off or otherwise:

(a) the respective obligations of the parties are accelerated so as to be immediately due and expressed as an obligation to pay an amount representing their estimated current value or are terminated and replaced by an obligation to pay such an amount;

(b) an account is taken of what is due from each party to the other in respect of such obligations, and a net sum equal to the balance of the account is payable by the party from whom the larger amount is due to the other party.

4. - This Article is without prejudice to any requirement of the domestic non-Convention law to the effect that the realisation or valuation of collateral securities or the calculation of any obligations must be conducted in a commercially reasonable manner.

Article 25

[Right to use collateral securities]

1. - If and to the extent that the terms of a collateral agreement so provide (or, where collateral securities are delivered to the collateral taker under Article 5(2), if and to the extent that the terms of the collateral agreement do not provide otherwise), the collateral taker shall have the right to use and dispose of the collateral securities as if it were the owner of them (a "*right of use*").

2. - Where a collateral taker exercises a right of use, it thereby incurs an obligation to replace the collateral securities originally transferred (the "*original collateral securities*") by transferring to the collateral provider, not later than the discharge of the secured obligations, securities of the same issuer or debtor, forming part of the same issue or class and of the same nominal amount, currency and description or, where the collateral agreement provides for the transfer of other assets [following the occurrence of any event relating to or affecting any securities provided as collateral], those other assets.

3. - Securities transferred under paragraph 2 before the secured obligations have been fully discharged:

(a) shall, in the same manner as the original collateral securities, be subject to a security interest under the relevant collateral agreement, which shall be treated as having been created at the same time as the security interest in respect of the original collateral securities was created; and

(b) shall in all other respects be subject to the terms of the relevant collateral agreement.

4. - The exercise of a right of use shall not render invalid or unenforceable any right of the collateral taker under the relevant collateral agreement.

Article 26
[Top-up or substitution of collateral]

Where a collateral agreement includes:

(a) an obligation to deliver collateral securities or additional collateral securities in order to take account of changes in the value of the collateral provided under the collateral agreement or in the amount of the secured obligations [, in order to take account of any circumstances giving rise to an increase in the credit risk incurred by the collateral taker] or, to the extent permitted by the applicable law as determined by the private international law rules of the forum, in any other circumstances specified in the collateral agreement; or

(b) a right to withdraw collateral securities or other assets on providing collateral securities or other assets of substantially the same value,

the provision of securities or other assets as described in paragraph (a) and paragraph (b) shall not be treated as invalid, reversed or declared void solely on the basis that they are provided during a prescribed period before, or on the day of but before, the commencement of an insolvency proceeding in respect of the collateral provider, or after the secured obligations have been incurred.

Article 27
[Declarations in respect of Chapter V]

1. - A Contracting State may declare that this Chapter shall not apply under its domestic non-Convention law .

2. - A Contracting State may declare that under its domestic non-Convention law this Chapter shall not apply –

(a) in relation to collateral agreements entered into by natural persons or persons falling within such other categories as may be specified in the declaration;

(b) in relation to intermediated securities which are not permitted to be traded on an exchange or regulated market;

(c) in relation to collateral agreements which provide for secured obligations falling within such categories as may be specified in the declaration.

APPENDIX 3

UNIDROIT Study LXXVIII Doc. 24 Preliminary Draft Convention on harmonised substantive rules regarding intermediated securities (May/June 2005)	UNIDROIT Study LXXVIII Doc. 42 Preliminary Draft Convention on substantive rules regarding intermediated securities (March 2006)
Chapter I – Definitions, scope of application and interpretation	Chapter I – Definitions, scope of application and interpretation
Article 1	Article 1
Article 2	Article 2
Article 3	Article 3
Chapter II – Intermediated securities	Chapter II – Transfer of intermediated securities
Article 5	Article 4
Article 6	Article 5
Article 10	Article 6
Article 11; 7(6)&7(7)	Article 7
Article 7(1)-(5)	Article 8
Chapter III – Protection of innocent acquirer	Chapter III – Rights of the account holder
Article 4(1)-(4)	Article 9
Article 4(5)&(6)	Article 10
Article 12	Article 11
Article 14	Article 12
Article 19	Article 13
Article 20	Article 14
Chapter IV – Insolvency	Chapter IV – Integrity of the intermediated holding system
Article 9	Article 15
Article 15	Article 16
Article 16	Article 17
	Article 18 (new)
Article 17	Article 19
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Chapter VII – Special provisions with respect to collateral transactions	Chapter V – Special provisions with respect to collateral transactions
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