

LEGISLATION ON LEGAL CERTAINTY OF SECURITIES HOLDING AND DISPOSITIONS

EuropeanIssuers' Comments on the Member States Working Group Discussion Paper of the Services of the Directorate-General Internal Market and Services (MARKT.G.2/(2010)57731)

8 April 2010

I. INTRODUCTION

EuropeanIssuers understands that the Commission is seeking views from experts of the Member States on a possible future "Securities Law Directive" (hereinafter the "SLD"). The SLD should create legal certainty in the area of holding and disposition of securities kept by book-entry. The key principles and selected proposals are contained in a Discussion Paper (hereinafter the "Discussion Paper") prepared by the Commission. The topic is not new for EuropeanIssuers who has been following up on it closely for years now and contributed to the debate with several position papers¹.

II. GENERAL APPROACH AND SCOPE

1. Account provider- account holder

The Commission says to take a functional and neutral approach, built on the functions (and rights and obligations derived there from) of each party intervening in the holding of securities through book entry, essentially the account provider and the account holder.

The functional approach that appears to be based on the UNIDROIT Convention is not fit for the harmonisation needs existing within the EU.

Although we detect substantial progress in some of the proposals for the SLD, we need to reiterate our concern that in general the proposals are too much securities industry oriented and thus threaten to damage some corporate fundamentals inherent to the issuance of securities. We are concerned that the future legislation, by creating rights to account holders,

¹ See EuropeanIssuers' previous position papers of June 2009 at http://www.europeanissuers.eu/_mdb/position/184_COM_Consult_Harmon_Secur_law_April_09_-_EuropeanIssuers_position_final_20090610.pdf and of 13 November 2008 at http://www.europeanissuers.eu/_mdb/position/166_LCG_2nd_Advice_EuropeanIssuers_Comments_20081113_final.pdf

would assign rights to account holders that are normally reserved to investors (see hereinafter).

We fear that the relationship issuer – shareholder, which should be at the forefront, risks to be superseded by the relationship account provider – account holder, which, although an important one, should come second and not first. Indeed let’s remind ourselves that issuers are at the very origin of the subject matter we are dealing with, namely securities. Looking at the basics, there are two essential parties to a security:

- a) the issuer or the entity that issues the security, as an essential source of funding and
- b) the investor who owns and trades the security, as a source of revenues.

From this point of view, the securities industry, with all due respect, has a secondary role, as it acts as a pure services provider to the two above mentioned parties. We do acknowledge that smooth and efficient trading and post-trading are extremely important in a cross-border investment environment. However, the trading and post-trading industry should be at the service of the prime protagonists that the issuer and the investor are, respect their relationship and the corporate rights and obligations attached to it and leave them unaffected. We cannot help but having the impression that this is sometimes forgotten, or even “reversed”, in the current proposals. Indeed the focus seems to lie with the account provider and the account holder, but many account holders in the chain are also account providers and vice versa.

2. Shareholder transparency

We strongly encourage the Commission not to miss this opportunity to address the issue of shareholder transparency. The future SLD offers the perfect context to provide for an EU wide framework for shareholder transparency that would allow for a direct dialogue between the issuer and the investor.

As a consequence of the contemporary book entry system, particularly in a cross-border investment environment, securities are being held through a chain of account providers. Shareholders can be identified with a varying degree of difficulty depending on whether the shares are bearer, registered in the shareholder’s name or registered in a nominee’s name. Unless the shareholder is registered in his own name, the identification can only be done by going through the holding chain. All these additional layers make it very difficult for the securities issuing company to know who its shareholders (actually its owners) are. This is the case even if the national regime governing the issuer and the securities it issued, provides in a positive right thereto. Whereas several EU Member States have a legal framework that gives the issuer the positive right to obtain effective disclosure from those intervening in the holding chain, there is currently no EU wide legal regime. In some Member States, banking secrecy rules or contractual provisions even stand in the way of such disclosure. Still in many other Member States, the law remains silent. As a consequence, requests for identification are being blocked at Member States borders, as a majority of them still fail to have the principle laid down in their own jurisdiction.

From a practical point of view however, shareholder identification could already effectively happen in most Member States of the EU, even in the current legal environment without a harmonised legal regime, provided that all concerned parties would be willing to co-operate. The difficulty to obtain shareholder disclosure is not a technical one, but is simply explained by the number of layers, *i.e.* the number of intervening account providers that one has to wade through in order to obtain the identity of the shareholder. There should be no mistake on this: the information on the identity is always available to the account provider. The difficulty derives entirely from the fact that the account provider does not pass on the information. The account providers' refusal or reluctance to co-operate could have various reasons: data protection; banking secrecy; lack of knowledge of the requirements that should be complied with; confusion because of conflicting legal or regulatory regimes; lack of level playing field with competing account providers; sheer unwillingness ... One thing we know for sure, only in rare cases it's because the shareholder objects to its identity being disclosed.

We understand that the future SLD might not be the best instrument to establish the right of the issuer to shareholder disclosure as this is clearly a matter of corporate law. However the future SLD would be the perfect instrument to establish the duties of the intermediaries who receive a request for identification from an issuer who bases himself on existing law.

Indeed, the Commission rightly considered it necessary that the SLD should include provisions on the duties of intermediaries to make sure that the investors' corporate rights can be effectively exercised. These duties essentially consist of communicating information on corporate actions through the chain of account providers. The communication flows are both upstream and downstream, in other words they should allow for an end-to-end communication. In our view, nothing would be more logic than to take this excellent opportunity to extend the duties of intermediaries to include the disclosure of the shareholder's identity. It would give account providers once and for all clear directions on what, how, when and towards whom they should be dealing with requests from issuing companies to bring transparency in their shareholder base. By doing so, the legislator would help out all these Member States where the right of disclosure already exist independently from the arrival of a EU wide legal regime that would establish the universal right of the company to know its shareholders².

3. Private Sector Market Standards for General Meetings

We are grateful to the Commission services for their efforts to liaise with the private sector initiative to create [Market Standards for General Meetings](#) (hereinafter the "MSGM"). These MSGM relate to some of the topics that could be addressed in the future SLD, namely the passing of information on general meetings via the chain of intermediaries. It is crucial that the legislative measures that the European Commission would propose, support and enable the effective application of the MSGM. However, as we write this comment paper, the major European banking associations have not endorsed the MSGM yet despite the multiple efforts of the working group to accommodate the concerned banking associations' requests and concerns. As a consequence, the future SLD should take care of embedding the key principles laid down in the MSGM into law. In addition, where the MSGM remain silent because parties

² In the assumption that such right could not be taken for granted.

were not able to reach a consensus or lacked the will to commit on a voluntary basis, the SLD should provide for a positive legal obligation.

IV. DISCUSSION PAPER

1. The minimum content of book-entry securities

Minimum content

We understand that the future SLD is proposed to be built around the central concepts of book entry securities, account, account provider and account holder. In that respect it could seem logic to lay down what rights flow from these concepts. However we have strong doubts that the so-called functional approach could be really workable. Is the right of disposal not an essential element of the property right?? We believe that it will be very difficult to draw the line between what are considered to be methods and what are considered to be legal concepts; between what will be harmonised and the consequences thereof and what will be left to Member States. We fear that rather than bringing legal certainty, we could end up with legal confusion.

We are of the opinion that the concept of book-entry securities is misleading in that it conflicts with other EU legal concepts. The notion “book-entry securities” seems to imply that a credit to a securities account creates a separate title from the underlying issued securities. We must not introduce in the EU the US concept whereby a book entry security creates a sui generis ownership right independently from the underlying securities.

In addition, we do not see any necessity for laying down basic rights attached to “book-entry securities” in the proposed future legislation. On the contrary, we see a clear risk of creating confusing rights for parties who should not be entitled to them. In drawing up harmonized legislation a clear distinction should be made between the rights conferred upon the investor, which are determined by the applicable “lex societatis”, and the legal effects of the acquired rights and their enforceability against third parties, which should be the onus of the SLD. Whereas the former relates to the relationship between the issuer and the investor and should be left outside of the proposed directive, the latter covers the relationship between the investor and the relevant intermediary, which should remain the exclusive subject matter of the envisioned legislation.

Central to the issuers’ concern is that the title is evidenced by book entry on a securities account maintained by the relevant intermediary in the name of the investor. The legal attributes flowing from the rights attached to book-entry securities is a separate matter, which does not fall within the ambit of the SLD.

At most (and to the extent this would not be established yet) the EU law could lay down the principle that the issuer law determines which rights, including those attached to the securities, would be conferred upon the holder of securities who is acting for his own account, *i.e.* the end investor.

The preceding principle applies equally to the rights mentioned under (a), (b) and (c). Imagine for instance that the account holder would not have the rights under (a) but would have those

under (b) and (c). The right of disposal proposed under (b) has very far reaching consequences as a disposal could lead to the acquirer obtaining the rights under (a). It would simply not be workable. We also fail to see the relevance of (c). If one would be eligible to do (b), he should necessarily be able to do (c) as well, on the basis of the principle “who can do more, can do less”.

Core duties

Rather than providing for the core-rights conferred upon the account holders, the future SLD should provide for core-duties on account providers, as described hereafter. These core duties are more efficient to make the custody chain work and more neutral for the rights of the final investor. The account providers’ core duties should include at least the following:

- safeguarding book-entry securities including an obligation of restitution
- reporting on securities movements and holdings
- refraining from using the securities otherwise than for the benefit of the investor and upon instruction thereof
- communication to investors of certain corporate events affecting the securities (see the section on the duties of intermediaries hereinafter) and the processing of the impact on the securities accounts of those events
- execution of any instruction given by the investor, to the extent that this does not violate applicable laws (such as holding sufficient securities)
- daily reconciliation of the securities accounts
- swift, timely and cost efficient identification of the account holder/shareholder, at any time upon request of the issuer.

As an additional note to, we wish to point out that not all securities account providers play the same role: the role of the issuer CSD in particular should be distinguished from the role of the securities account providers further in the chain. The issuer CSD should obviously carry out the so-called notary function and preserve the integrity of the issuance by carrying out first level concordance. This guarantees that there are never more or less securities in circulation than are issued by the company.

Conclusion: the proposed Rule has no relevance: there is no need to establish rights linked to “book-entry securities”; the issuer law is to remain/be the unequivocal source of any rights attached to securities. A list of core duties for account providers would be useful.

2. Acquisition and disposition of book-entry securities and their effectiveness

We think that a fix set of methods, consisting preferably only of debiting and crediting, could in principle bring more legal certainty, but this will not be achieved with the current proposal.

1. It is useful to have EU law on this only if there is complete certainty and clarity on the legal position that a so-called acquisition or disposition or limited interest would entail. But that’s

exactly what the proposal wishes to avoid. No underlying national legal concept will be linked with the terms acquisitions and dispositions. What's the point in having a fixed set of methods when there is no uniform understanding on the purpose they serve? 2. According to the proposal, Member States may characterise the legal nature only when such would not contravene other rules of the SLD. This is hardly reconcilable with the idea that the underlying legal concepts would have to be respected.

3. We would like to point out that the proposed Rules are very ambiguous where registered shares are concerned. It is absolutely necessary to leave national requirements for registration in the issuer's register unaffected. However the proposed Rules contain contradictory provisions, namely paragraphs 1 and 2 of Rule 3. Paragraph 2 says that the effectiveness does not determine who an issuer has to recognize as the legal holder of the securities. It is explained in the text that the national law can still lay down that for instance voting rights are reserved to those persons who figure in the register, which is indeed the only right approach. But paragraph 1 says that Member States shall not require further steps to make an acquisition or disposition effective, meaning that a person could have a holding that is considered effective, but he would not have the voting rights. Once considered effectively acquired, these book-entry securities could thus become the subject of successive transactions (acquisitions and dispositions) and start leading a separate life from the securities as registered in the register.

How could this be justified? Moreover, what will happen with corporate actions and general meetings' processing that take place on the basis of the holdings of book entry securities?

4. It would be necessary to know which would be the applicable law for acquisitions or dispositions, for instance the issuer law as opposed to the law governing the shareholder or the intermediary or the relationship between these parties or the buyer or the seller... Now this is an area where the future legislation should bring harmonisation and clarity: it should indeed lay down a provision that Member States shall provide that the issuer law is the law applicable to the acquisitions and dispositions. Depending on the type of legal form the company has been constituted under, the issuer law may indeed impose restrictions to the acquisitions and dispositions. Therefore, only the issuer law could be a trustworthy source of law.

5. In some markets a conditional securities book-entry is made before the settlement of the acquisition transaction. The book-entry and the corresponding acquisition becomes effective only when the purchased securities are also effectively delivered or when the purchase price is paid by debiting the cash account for instance. This should continue to be possible provided there is a clear indication, for instance by earmarking, of the conditional character of the book-entry.

6. Non-book-entry methods (earmarking, control agreements or agreements in favour of the account provider) should not constitute evidence of an acquisition or disposition in themselves. The more so as again, it is not clear to what position the acquisition or disposal effected by non-book-entry would be able to lead to: what rights will be derived from the non-book-entry method? If non-book-entry-methods would result in for instance acquiring the voting rights at general meetings (and we don't mean as a proxy), it would become impossible to determine the entitlement, i.e. the voting position, on the record date, as this is done through the chain of

intermediaries. Non book-entry methods should only be allowed for the creation of limited interests.

Conclusion: we fear that the proposed approach would only create more uncertainty.

3. Reversal of acquisitions and dispositions

Looking at the proposed harmonised list of circumstances that would justify a reversal, we question the rationale for such Rule. It is obvious that transactions that were executed erroneously or without the required authorisations from the parties concerned, should be reversed without discussion. It is not necessary for European law to enact this principle. In addition, by listing the circumstances in which reversal can be done, the proposal appears to be intended to limit reversal to these circumstances only, to the exclusion for instance of reversals imposed by a court order.

Conclusion: the proposed Rule brings no added value.

4. Priority

We wonder whether it makes sense to create a ranking between interests created by earmarking on the one hand and those created by agreements on the other hand. In principle all interests derive from agreements, except for those interests that are derived from the law. In addition, earmarking is in principle as invisible to third parties as agreements. The argument to give earmarking a higher ranking based on the transparency that goes with book-entry does therefore not hold. The chronological order rule should therefore apply to all methods without distinction. We do however recommend to introduce a rule according to which a specific interest, meaning an interest taken on a specific well defined asset, ranks higher than a general interest, meaning an interest taken on a general not further defined class of assets. This is a generally applied principle in many Member States.

Conclusion: only the chronological order rule should apply combined with a rule that gives priority to specific security interests over general security interests.

5. Account holder protection and integrity of the issue

The Commission argues that Article 13 of the Directive 2004/39/EC³ (hereinafter “MiFID”) and Article 16 of the Directive 2006/73/EC⁴ (hereinafter the “Implementing MiFID”) do not offer sufficient safeguards. We definitely subscribe to that view.

³ Art. 13, 7 and 8 of the Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC, *Official Journal L 145*, 30/04/2004 P. 0001 – 0044:

We believe that account holders must never be confronted with extra costs because the type of securities accounts provided by the account provider require the latter to take extra measures (such as registration) to protect the investor or safeguard the integrity of the issuance.

The explanatory text mentions two concerns of a different nature: a) the integrity of the issuance, which can only be evaluated at a global level and b) the protection of the investor, which is in the first place a matter between the account provider and the account holder and to be looked at at the account level. The integrity of the issuance and the position of the individual investor are not necessarily always linked. The investor's position can be at risk without the global issue being threatened.

The Discussion Paper seems to suggest that the proposed Rule intends to cover both concerns: the integrity of the issuance and the protection of the investor. Whereas we agree with the proposals where they wish to achieve the protection of an individual investor, we believe that the proposed Rule does not address the issue of the issuance integrity. The Discussion paper sounds rather alarming where it points to a diversity of rules amongst EU jurisdictions to avoid problems with the integrity of the issuance, saying that this diversity is a problem in itself. Why does the Commission then not address this problem?

The integrity of the issue is of utmost importance for issuers and investors, for obvious reasons. It is the first duty for any book entry security holding system to ensure that there are no more securities circulating than were actually issued by the issuer. When clearing and settlement systems work well, the integrity of the issuance should not be at risk. This implies first level concordance being assured at the level of the issuer CSD and concordance deriving thereof at the "lower" levels with the participants of the issuer CSD and their clients and the clients thereof and so on until the "lowest tier" account holder or investor. Indeed, crediting and debiting must not occur independently: crediting of the securities account of the purchaser's bank cannot take place without debiting the securities account of the seller's bank nor without crediting and debiting the respective accounts of the purchaser and seller accordingly. The obligation for account providers to maintain a number of securities that corresponds to the number credited to the accounts of the investors is in fact nothing more than the application of clear accounting principles. Under a double entry accounting system, each credit to an account corresponds to a debit in another account and there should accordingly not be any shortfall.

The above requires that every account provider in the chain respects a strict reconciliation regime. We strongly insist on a mandatory daily reconciliation. The regular reconciliation as provided for by Art. 16, 1, c, of the Implementing MiFID is not satisfactory in this regard. Daily reconciliation is also required to ensure the accuracy of the determination on the record date of the entitlement, in other words the holdings for which a person is entitled to corporate

"7. An investment firm shall, when holding financial instruments belonging to clients, make adequate arrangements so as to safeguard clients' ownership rights, especially in the event of the investment firm's insolvency, and to prevent the use of a client's instruments on own account except with the client's express consent.

8. An investment firm shall, when holding funds belonging to clients, make adequate arrangements to safeguard the clients' rights and, except in the case of credit institutions, prevent the use of client funds for its own account."

⁴ Directive 2006/73/EC of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive, *Official Journal L 241, 2.9.2006, p. 26–58.*

rights. These corporate rights include i.a. the right to participate to and vote at the general meeting in accordance with Art. 7 of the Directive 2007/36/EC⁵ (hereinafter the “SRD”) and the right to corporate actions like dividend distributions.

A daily reconciliation regime might however not be sufficient as a safeguard against risks threatening the integrity of the securities issuance and we urge the Commission therefore to address this matter.

Conclusion: the proposal does not include a solution to ensure the integrity of the issuance at a global level. A daily reconciliation regime is the least that should be put in place as a safeguard against integrity risks.

6. Conflict-of-laws of holding and disposition of book-entry securities

We need to make strong reservations against the proposed Rule. First of all, the proposal is using an account provider related criterium to determine the competence for the civil and corporate law aspects of the securities, which is fundamentally unacceptable. Secondly, this proposal has the potential to create conflicts rather than resolve them. Thirdly, the proposal does not really succeed in reducing the margin for interpretation of the location of the account.

1. The proposed Rule is intended to solve possible conflicts-of-law for a well defined list of matters, that includes among others the legal nature of the book-entry securities (para 4.a)), of the acquisition and disposition (para 4 b)) and the right to dividends (para 4 c)). We need to recall the Commission’s earlier explanation that the exact legal nature like the property, trust, etc would not be determined by the future SLD. No indeed, because the proposed Rule says that these issues will be addressed by the Member States, with the competent member State being the one where the account is located.

This approach completely ignores that securities are being issued by a company under terms and conditions determined by the national law of the Member State where the company has its registered office. The security is the core item, not the securities account which is merely a vehicle to “store” or keep the security. The rules governing the security determine whether somebody is entitled to a dividend, NOT the rules governing the account. By including these matters in the scope, the proposed Rule is not only entering into the area of civil law and corporate law which is already unacceptable in itself, but it also disregards the relevance of the issuing company by making the security account and the location of the account provider the centre of the universe.

We do not want to be misunderstood: we fully acknowledge that the account agreement between the provider and the holder will not be governed by the issuer law. But this is a separate issue: the account agreement regards only issues pertaining to the services offered for this account and has nothing to do with issues stretching into the sphere of civil and corporate matters. There is no evidence that a conflict-of-law rule would be needed in the area of

⁵ Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies, *Official Journal L 184*, 14.7.2007, p. 17–24.

securities accounts as such (cfr cash accounts). Hence the proposed Rule does not comply with the subsidiarity principle.

2. Our second objection to the proposed Rule lies in the fact that it potentially creates a different applicable law for every layer of the chain (every account provider-account holder relationship) for a given security. The conflict-of-law principles laid down in the Financial Collateral Directive and the other securities Directives cannot be simply transposed to conflicts of law related to “book-entry securities”. This is because the said Directives only apply to the financial industry, i.e. financial institutions in their business with each other. In addition, these Directives are not based on the concept of different layers of account providers and account holders for the same security as used in the future SLD.

For instance, let’s imagine a Bulgarian investor who holds shares of a company situated in Belgium. In principle the Bulgarian investor will hold these shares with a bank located in Bulgaria: under the proposal, Bulgarian law would determine all matters listed in the proposal between those parties, including the rights to dividends (although the company issued the shares under Belgian law). The Bulgarian bank holds these shares with a major French custodian. French law will fully apply to this relationship, including for the rights to dividends. The French bank holds the shares in an account with the Belgian (international) CSD. Belgian law will fully apply to this relationship, including for the rights to dividends. This example shows that for the same legal question, there would be as many laws applicable as there would be “layers” in the chain. And then again we kept it simple, because the criterium “*the branch which services the client/handles the relationship with the account holder*” would have to be assessed separately for every layer in the chain and could still give other results than those we put forward. Clearly this is not a recipe for legal certainty.

3. We do not believe that a new European-wide conflict-of-law rule is needed to replace the one contained in the above mentioned Directives. They already cover a broad scope and their implementation has proven satisfactory, as experience has shown.

If the Commission believes that the connection criteria in the existing Directives need to be refined, then it should do so with another legal instrument, outside the scope of the SLD. In any event, due consideration should be given to carrying out an impact study on the merits and deficiencies of a change of the said Directives. Besides, any additional interpretative rules regarding the location of the account should be based on objective criteria, rather than criteria leaving the parties (read the “dominant” party) with the freedom to choose the applicable law, as it was the case in the The Hague Convention.

4. The above arguments indicate more than enough that the proposed Rule leaves too much scope for further conflicts. As a matter of fact, there is only one element that remains stable with regard to securities, namely the issuer. This element will never change wherever one finds himself in the holding chain. As we already indicated above (see our comments on Rule 1) the issuer law and only the issuer law, i.e. the law of the Member State where the issuer has its registered office, must determine which rights, including those attached to the securities, are conferred upon the holder of book entry securities who is acting for his own account, *i.e.* the end investor.

Making the issuer law the only law applicable has the additional benefit that such rule would also safeguard the principle laid down in Art.1,2 of the SRD in case of a conflict of laws. According to the SRD the issuer law (*i.e.* the law of the Member State where the company has its registered office) is the applicable law for those matters covered by the SRD. The matters covered by the SRD are “certain rights of shareholders in listed companies”, notably the rights related to general meetings. We envisage in particular the situation where these rights might be menaced as a consequence of the direct relationship issuer – shareholder being “interrupted” by a relationship account provider – account holder.

Rights related to corporate actions are not covered by the SRD. Hence the conflict-of-law rule should in the second place include them also explicitly in its subject matter.

Conclusion: the proposed Rule does not bring a solution to possible conflicts-of-law but has the potential to create a multitude of conflicts. The Issuer is the only stable element and the Issuer law should be the only one applicable since the matters listed stretch into the civil and corporate sphere. As regards the Securities Directives that already have a conflicts-of-law regime, any additional criteria regarding the location of the account should be based on objective elements.

7. Exercise of rights flowing from securities

As we said in Section II “General approach and scope” above, we strongly encourage the Commission to provide for a mandatory legal framework that sets out the duties of intermediaries in this area as explained hereinafter. This is exactly what is needed to complement the SRD and if properly handled, it may give a major boost to cross-border voting in the EU. We find the current proposals a major improvement in comparison with the first ideas expressed in the Second Legal Advice and hope that the Commission will carry this proposal forward without any restrictions and subject to the comments hereinafter.

The proposals are based on a model that transmits information through the holding chain, which is also the model followed by the MSGM. Choosing this model makes sense, because it is the only one in theory that allows to reach the entire shareholder base, starting with the global securities issuance at the level of the issuer CSD. However, we do not know how efficient or inefficient this model will turn out to be. The chain could take time and there is no guarantee that the information would reach its destination. At the same time, for the communication with holders of bearer shares and for registered nominees, there is no other option today.

Given the possible weaknesses of communicating through the chain, the Commission should complete the proposals hereinafter with requirements regarding the diligence and timeliness of the passing on of information, the reasonability of the costs, etc.

Last but not least, and as indicated at the beginning of this comment paper, if issuers would be allowed to have their investors identity disclosed by the account providers, the communication of information could be done directly between the issuer and the investor, saving time and costs and allowing a direct dialogue. Then issuers and investors would not depend anymore on

the help of the account providers for passing on information. The current situation is unfortunately forced upon the issuers and the investors.

8. Recognition of holding through securities accounts

We agree that the investor must not be discriminated because of the holding pattern his intermediary offers him.⁶ Member States should oblige intermediaries to provide such holding patterns to their clients as to allow them to invest in securities abroad. Investors should not have to adapt their investment behaviour nor the exercise of rights flowing from their investments to what the service providers have on offer. Rather should service providers, custodians and other financial intermediaries, remove any restrictions in the area of holding patterns and offer holding systems that effectively enable the investors to invest EU wide. Corporate law or the *lex societatis* of the issuer should be the starting point. It is this law that applies to all investors in the same security. The exercise of the rights by investors should not be hindered by the holding model.

We also believe that the current proposals are quite an improvement in comparison with Recommendation 13 made in the Second Advice published in August 2008 by the Legal Certainty Group. That Recommendation could have led to the understanding that there was no reason to look further than the apparent investor, whereas the ultimate investor with the economic right has to be reached. Such requires the possibility to “look through” the various layers of account holders.

9. Facilitation of the exercise

We believe that the proposed Rule is in general beneficial for all parties concerned and would contribute to making cross-border shareholding more attractive and remove the discrimination between domestic and foreign shareholders.

Contractual agreement

However the proposed Rule threatens to miss its purpose because of paragraph 3.(a) which introduces the possibility to make the obligations subject to a contractual agreement. In case this facilitation is “*necessary for the effective receipt or exercise*”, we do not quite understand why account providers should be allowed to contract out of a mandatory delivery of what is a basic requirement for the ultimate investor to exercise a right enshrined in a security. Indeed what good would it do the ultimate investor for instance to receive information that a general

⁶ We should also like to add here for complete clarity that the investor doesn't choose the holding pattern: it's not the investor who chooses to hold through a chain of providers. The average investor (and market participant for that matter) does not know that the securities are held through a chain. It's actually not clear why intermediated holding often results in holding through a chain of intermediaries. Possible reasons could be:

- That an intermediary in country A prefers to open a securities account with another intermediary in country B rather than directly with the issuer CSD in country B or country C, on the basis that the intermediary in country B is familiar with securities practices of country B or C;
- That an intermediary in country A has to go via an intermediary in country B because he has no direct access to the issuer CSD in country B.

meeting will be held, if he doesn't receive from his account provider the required proof that he holds a certain number of securities on the record date? Or when no proxy is given to him in accordance with 2.(b)? It is absolutely crucial to limit contractual waivers to an absolute minimum and only to those situations where facilitation is not necessary but only requested. The facilitation should remain mandatory anytime the exercise of rights would be impossible or cumbersome without the assistance of the account provider.

We wish to make an additional observation in this respect: the current wording of the proposed Rule seems to suggest that the facilitation under 2.(a), namely the certificate confirming the holding, would not always be necessary but could be triggered only at the request of the ultimate account holder. We wish to point out that this certificate would always be necessary in view of voting at the general meeting.

As regards the scope of the facilitation, it should at least include those corporate actions that call for an action from the investor: for instance a general meeting, a distribution of dividends with options, a voluntary reorganisation, etc., in general any elective corporate event as opposed to a distribution of a cash dividend that will be credited to the investor's account without any action on his behalf. The future legal provision should better not be construed with a list of specific corporate actions, but with a list of criteria determining the type of corporate action.

“Receipt” or “exercise”

Finally, we are not sure whether the proposed Rule should use the two separate notions *“receipt or exercise”*. Does *“receipt”* refer to receiving the right or receiving the fruit of the right? We do not think it could be the former and if it is the latter it could only refer to the fruit of corporate actions. If our interpretation is correct, this could never be made subject to contractual arrangements with the ultimate account holder. The account provider who provides the securities account for the ultimate account holder simply must process the corporate action, for this is done through the chain of intermediaries: the account provider himself will receive the fruit of the corporate action in any case, so he has the duty to pass this on.

Certificate confirming the holdings

We very much welcome the provision that the account provider must provide the certificate confirming the holdings. This system however has to be 100% waterproof in view of the acceptance by the issuer.

The certificate can take on a different meaning depending on whether it's an evidence on a) a specific but *“ordinary”* date or b) record date for general meetings or record date for corporate actions (which are not the same). In case of general meetings and in order to ensure the integrity of the voting process and to avoid irregular voting (double voting, loss of votes, etc.), the certificate should be issued on the basis of EU wide criteria, for instance on how to strike positions. The MSGM include specific indications thereto, but they are not binding (as a matter of fact, they are not even endorsed yet by all stakeholders). If account providers do not all use the same criteria, there will be double entitlements.

The certificate should also be uniform throughout the EU. It could possibly take the form of a unique identifier that could only be used once. It could be a unique secure combination of data (code) to identify a holding, on the basis of standards to be defined by the securities industry such as the ISO standards.

There should also be a safeguard to prevent that a certificate, even by inadvertence, would be exercised more than once. The certificate should be the only valid proof required by the Issuer for participating in and voting at the general meeting, irrespective of the means of participation and voting chosen by the Shareholder, without prejudice to the Issuer's right to accept an alternative proof.

As a last observation on paragraph 3.(b) we would like to point out that market participants in general should also recognise the certificate, not only the issuers.

Conclusion: the proposed Rule should be modified such that an account provider could never contract out of the obligation where facilitation is necessary for the effective (receipt or) exercise of the rights.

10. Exercise under instruction by the ultimate account holder

Paragraph 1.(a) covers the situation where the account provider is recognised as the legal shareholder and the ultimate account holder ("economic" shareholder, beneficial owner, end investor) cannot exercise his rights himself. The situation that is being addressed here, is therefore the one in which the dependence of the ultimate account holder (i.e. the end investor, the one who bears the economic risk) on the account provider is at its highest! Indeed, without any action of the account provider, the investor will be *de facto* deprived from its rights.

However paragraph 3.(a) (para 2 is missing) is intended to make this obligation subject to a contractual agreement. We believe that this is unacceptable and refer to what we said on this above as regards the Rule concerning the facilitation of the exercise. An account provider or a third person could be very well considered to be the legal holder simply because of the type of securities accounts in which the account provider offered to maintain the securities. He should therefore never be allowed to contract out of the corporate rights, because this would clearly discriminate all investors who are in this situation.

Paragraph 1.(b) covers the situation where the account holder simply prefers not to exercise the rights himself, but wishes to give a proxy to the account provider. Why does the proposed Rule not refer to Art. 11 of the SRD as in the proposed Rule concerning the facilitation of the exercise?

We also think that certain conditions of transparency must be fulfilled: the intermediary should disclose its client's name as well as the number of shares held on his behalf.

Conclusion: the proposed Rule should be modified such that an account provider could never contract out of the obligation where his action is necessary for the effective (receipt or) exercise of the rights.

11. Passing on information

European Issuers welcomes the proposed Rule.

Issuer originated information

One of the principles set out in the Discussion Paper with regard to the processing of information, is that the information should not come from third parties. The flow should be end-to-end meaning issuer to end investor. However paragraph 1 is not correctly drafted in that respect. First of all, it misses the layer issuer (or its agent) – issuer CSD and it starts with an account holder with the consequence that the information must have been passed on already once. Only issuer originated information is trustworthy and this is the only information that is to be subject to the obligation of transmission. Paragraph 1 should be reworded as follows: *“received from an issuer by an account provider”*. This modification would address both of the two said concerns.

Paragraph 1.(a) uses the word “necessary” and the Discussion paper provides no explanation on how to interpret this criterium which would however determine when the obligation would be triggered. We believe that as far as a general meeting would be concerned, “necessary information” would include the notice to convene a meeting (the key elements, not the full convocation) and the entitled position on the record date (together with the certificate of the holding). Upstream, such “necessary information” should consist of the notification of attendance including the votes or voting instructions, if any. For corporate actions, it should include all elements that are needed to allow the ultimate investor to take action where such possibility to act is embedded in the corporate action, in other words in any elective corporate action.

Cost

According to paragraph 3. the Commission will separately establish rules regarding the sharing of the cost burden. We take the liberty to formulate a few thoughts in this respect that might help the Commission with its future task.

1. The cost factor is influenced by the length of the chain and the current lack of a harmonised legal framework and harmonised best practices (as currently being laid down in market standards on corporate actions and the MSGM). The more parties intervene, the more costly the processing and the passing down and up again of information will likely become.
2. It should be also reminded that Investors are obliged to keep their securities in a securities account, for the keeping of which they pay a fee.
3. Account providers on the other hand will benefit from the data provided by the issuers (“golden copy”) and seized in a format that allows straight-through-processing. They will make

a profit out of this by reselling the “golden copy” that they will receive from the issuers, whereas today they buy such information from data vendors and have to double-check it and compare it against a number of sources before using it.

4. Then many costs should be able to be reduced significantly as a consequence of the implementation of the said market standards, in particular on corporate actions. However at this stage, there is no indication as to where in the value chain these cost savings would take place or how they would flow back to the users. As a general principle, the end users, the issuers and investors, should be the ultimate beneficiary of the removal of the Giovannini barriers, in particular in terms of efficiency and cost benefits. The infrastructures and intermediaries involved will benefit from the straight-through processing of corporate actions, as it won't be necessary anymore to double-check information and enter the data manually into the IT systems again. Such should lead to significant cost saving and much more efficiency at their level. In a competitive environment, this should bring down the fees for all infrastructures and intermediaries who should in turn be able to reduce fees for services rendered to issuers as well as to investors.

The question is how these expected cost savings and fee reductions will be ventilated. Will there be any transparency on the price setting for both issuers and investors? We understand that in some Member States both the issuer and the investor pay the intermediaries for their involvement in corporate actions' processing. How will this be avoided in the future? Will there be any transparency as to the costs exposed and the savings made at the various levels?

With the Code of Conduct in the area of clearing and settlement, the European Commission succeeded in making huge progress on the transparency of pricing between infrastructures and professional users (intermediaries). Now it is time to take measures to establish transparency in post trading services also for the end users at either end of the chain, namely the issuers and the investors. A monitoring tool or an observatory should be set up to show where the cost savings are and who will benefit from them.

Conclusion: the proposed Rule should be modified so that an account provider could never contract out of the obligation where his action is necessary for the effective receipt or exercise of the rights. The proposed Rule should ensure the timeliness of the passing on. The criteria for sharing the cost burden should be set with caution and a cost monitoring tool should be set up to bring transparency on where the costs lie in the chain and cost savings can be made.

12. Access to Central Securities Depositories

Issuers should have a free choice as to the location of the initial (or subsequent, in case of a so-called “move”) book entry of their securities. This choice should also be a real choice in practice, meaning that it should not be more costly than a locally placed issuance simply because of the foreign element.

13. Regulatory framework for account providers

We agree that the issuer CSD has a specific role to play as it takes care of the integrity of the securities issuance. Such can be dealt with in the future market infrastructure related legislation.

Making the service of safekeeping and administration an investment service in the sense of MiFID would be one way to make sure that account providers which provide these ancillary services would be subject to authorisation. However cataloging them as investment services might entail the applicability of other MiFID provisions that are not relevant or would have too far reaching consequences.

We also recommend differentiating between i) the authorisation of the access to the “profession” of securities account providing and ii) the regulation of the activities and services rendered by the account provider. The list of services that safekeeping and administration should include as core duties, or in other words basic custody services, should be explicitly laid down by law. See our comments under “**1.The minimum content of book-entry securities**” above.

Finally we wish to underline that only intermediated securities holdings are in the scope of the proposed legislative measures. The future legislation should therefore explicitly exclude the direct holding by investors with issuers from its scope to avoid that an issuer would qualify as a regulated account provider.

EuropeanIssuers is a pan European organisation set up to promote the interests of issuing companies. Its members are national associations and companies from 14 European countries counting together some 9.200 listed companies with a combined market value of some € 5.000 billion. As such it represents the vast majority of publicly quoted companies in Europe. The members of EuropeanIssuers come from various sectors including automotive, nutrition, energy, health care, construction, financial services and many more. What brings them together in EuropeanIssuers is that they are all owned by the public, making them subject to an impressive set of complex and stringent rules and regulations. Through EuropeanIssuers listed companies can engage in direct discussions with the decision makers at European, trans-Atlantic and global level. Typical areas of interest include shareholder rights, corporate governance, transparency, clearing and settlement as well as financial reporting and auditing. Our ultimate goal is to achieve fully integrated, liquid and well functioning European financial markets combined with good corporate governance and responsible share-ownership. More information can be found on www.europeanissuers.eu.