The Depository Trust Company

IMPORTANT

B#: 1547

DATE: February 27, 2001

TO: All Participants

CATEGORY: International

FROM: DTCC General Counsel's Office

ATTENTION: Legal Department

SUBJECT: Hague Conference; Draft of International Convention Relating to Conflicts of Law Pertaining to the Pledging of Securities Held Through Indirect Holding Systems

The attached relates to an effort that is underway to establish an international harmonized choice-of-law "Hague Convention" relating to the pledging of securities held by intermediaries.

Last month delegations from 29 member countries and 17 international organizations met in The Hague and prepared the first draft of such an international law. Attached is the draft convention, along with some commentary by the U.S. Delegation on the draft.

Please feel free to direct any comments that you may have on the attached to any member of the U.S. Delegation either in writing or by e-mail.

Jack R. Wiener
General Counsel's Office

United States Delegation to the Hague Conference on Private International Law

Project on the Law Applicable to Dispositions of Securities held through Indirect Holding Systems

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To: Persons Notoriously or Potentially Concerned with the Hague Conference Project on the Law Applicable to Dispositions of Securities Held through Indirect Holding Systems

From: Members of the U.S. Delegation to the Hague Conference Project

Re: Report and Request for Comments and Suggestions

As many of you well know, the Hague Conference on Private International Law (the "Hague Conference"), an intergovernmental organization with 47 member states that promulgates multilateral conventions on different aspects of private international law, determined in May 2000 to investigate the feasibility of preparing on an expedited basis an international instrument to determine the law applicable to the taking of securities as collateral.[1]

[1] To be very precise, the Special Commission on General Affairs and Policy of the Hague Conference on Private International Law recommended in May 2000 that the following item be included, with priority, on the agenda of the Conference:

A "meeting of experts" convened at The Hague on January 15-19, 2001, which was attended by 119 legal experts representing 29 member countries and 17 international organizations (a list of countries and entities represented is attached as Attachment 1), to consider relevant issues and the feasability of drafting a convention (or other appropriate instrument) to present an effective and workable conflict of laws rule to govern the "proprietary aspects" of dispositions of securities held through indirect holding systems. In fact, guided by the deliberations of the delegates, a drafting committee, chaired by Sir Roy Goode of the United Kingdom and including Lars Afrell (Sweden), Diego Davos (Belgium), Professor Francisco Garcimartin (Spain), Professor Hideki Kanda (Japan), Professor Karl Kreuzer (Germany), Antoine Maffei (France) and Professor James Steven Rogers of the US, with Richard Potok as legal expert and Dr. Christophe Bernasconi, First Secretary of the Hague Conference, prepared a draft convention by the final session of the meeting.

Enclosed is a brief memorandum prepared by Professor Rogers identifying certain of the most significant issues addressed at the meeting and relevant to the review of the draft convention. Attached to Professor Rogers' memorandum are a copy of the draft convention, another copy of the convention incorporating certain of the changes or alternatives he discusses together with drafts of additional or revised provisions that the US Delegation has been considering.

A meeting was held on January 5, 2001 at The Federal Reserve Bank of New York, in preparation for the experts meeting at The Hague, to solicit the views of interested individuals and groups, including market participants and industry organizations, commercial and investment banks, global custodians, securities depositories and regulators, regarding the issues that were to be discussed, particularly with reference to a preliminary note prepared for the Hague Conference by Dr. Bernasconi (available at http:/www.hcch.net). Each of the persons who attended the January 5, meeting has received a copy of this communication.

Joyce Hansen, Co-Head of Delegation of the US Delegation, will host a second meeting which will be held at The Federal Reserve Bank of New York, 33 Liberty Street (enter on Liberty Street), in the 10th floor board room, on Monday, March 5, 2001, from 10:00 a.m. until approximately 4:00 p.m. Limited capacity for attendance by teleconference will also be available through Joyce's office.

We have a brief window of opportunity to provide comments and suggestions to the drafting committee and the Permanent Bureau of the Hague Conference, which will prepare a further draft of the convention and a report on the convention and the experts meeting. This will be circulated to the delegations and

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"the question of the law applicable to the taking of securities as collateral, it being understood that, without waiting for the Diplomatic Conference, a working group open to all Member States, to experts and associations specializing in the field, should convene to examine, in collaboration with other international organizations, notably UNCITRAL and Unidroit, and the private sector, the feasibility of drawing up a new instrument on this topic."

observers in advance of the June meeting of the Special Commission of the Hague Conference (and can be made available by the US Delegation to interested persons when available), which will determine the future of this project.

The US Delegation sincerely solicits your thoughts and ideas regarding the draft convention and the issues it seeks to address. You may address them to Joyce Hansen or any other member of the delegation in writing or by e-mail. We would warmly welcome your participation in our meeting on March 5th. In all events, please provide your comments by March 8th.

If you express your interest in this matter and provide contact details, we will keep you informed.

Very best regards and, please, express your thoughts, positive or negative, general or specific.

Harold Burman
Joyce Hansen
Richard Kortright
James Stephen Rogers
Harry Sigman
Jack Wiener

JMH/jl:vf

Enclosures

#70584 v1 - Hague Conference Invitation Letter

ATTACHMENT 1

Working Group, Hague Conference Experts Meeting
January 15-19, 2001

Member Countries Represented:

Germany

Argentina

Australia

Austria

Belgium

Canada

China (including Hong Kong SAR)

Korea

Denmark

Egypt

Spain

Estonia

United States

United Kingdom

Finland

France

Greece

Ireland

Italy

Japan

Latvia

Luxembourg

Morocco

Mexico

The Netherlands

Slovakia

Sweden

Organizations and Observers:

UNCITRAL

OAS

UNIDROIT

European Commission

European Parliament

European Bank for Reconstruction and Development

ECB

IMF

EIB

IBA

FMLG

ISDA

Emerging Markets Traders Association

IOSCO

International Council of Securities Associations

Forum of European Securities Commissions

European Central Securities Depositories Association

Memorandum

To: Interested Parties
From: US Delegation to Hague Conference project on Indirect Securities Holding
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Re: Request for Comments on current draft
Date: February 21, 2001

The Hague Conference on Private International Law is working on a proposed international convention on choice of law for indirect securities holding. Christophe Bernasconi of the Hague Conference Permanent Bureau has prepared an excellent background memo on the project (http://www.hcch.net/e/workprog/securities.html).

The proposed Convention will deal with transfer and pledge of securities held through the so-called "indirect holding system," in which investors hold securities through accounts with brokers or banks, which may in turn hold through accounts with upper-tier intermediaries, such as central securities depositories. Traditional lex situs choice of law for securities point either to the location of the certificate or the issuer's jurisdiction. That worked fine when the investor actually had possession of the certificate or was directly recorded on the books of the issuer. But when the investor holds through a securities account, the location of the certificates or issuer is usually irrelevant and often unknowable. So, a consensus has emerged in the past decade that the governing law should be the law of the place of the relevant intermediary. In the Hague discussions, this idea has come to be referred to by the shorthand "PRIMA" for "place of the relevant intermediary approach," as opposed to the "look through approach" that would look to the situs of the underlying security. The point of the proposed Hague convention is to adopt PRIMA.

We seek advice, comments, and suggestions on the current draft of the proposed Convention, attached as Appendix A. (This draft has not been formally adopted or approved by any stage of the Hague Conference process. It is a slight revision of the text produced at the meeting at The Hague in January 2001. The revision was prepared by the Permanent Bureau and the chair of the Drafting Group.) We have attached as Appendix A-I a version of the draft Convention which includes a number of suggested changes for consideration, many of which are addressed in this memorandum, some not.

Here are some particular points that we believe warrant attention.

Article 1

Article 1(1). Following common Hague Conference practice, this Convention has a general scope provision, Article 1(1), a general rule on determination of applicable law, Article 3, and then a detailed rule on the scope of the applicable law, Article 5. We are concerned about the possibility of difference between the general language in Articles 1 & 3 and the specific language in Article 5. We have suggested both an explicit cross-reference in Articles 1 & 3 to Article 5 and an "alignment" of the language in Articles 1 & 3. Do others share this concern?

Article 1(2). This section determines what degree of "internationality" is Needed to make the Convention applicable. The usual sort of "parties in different States" clause won't work here, because the Convention must apply even though all parties are located in the same country but the collateral includes securities issued by companies around the world. One approach would be to have no internationality scope clause, on the theory that the only time it matters that the Convention applies is where there is in fact a choice of law question to be decided. Alternatively, one could have a clause stating specifically which factors trigger application of the Convention.[2] The current draft takes a middle course. (See Article 11 for cases within the scope of the Convention where domestic conflicts rules apply nonetheless.)

Article 2

We believe that some addition is needed to make clear that the Convention's choice of law rules apply to a pledge of an entire securities account, as well as to a pledge of a security entitlement. (The term "account right" used in this draft is roughly the same concept as security entitlement.) We have suggested that the point might be captured by adding to Article 2(2): "References in this Convention to an account right include any interest in an account right or a securities account as a whole."

Article 3 See above under Article 1.

Article 4

The most controversial issue has been the rule determining the location of the relevant intermediary, or where the "account is located." As background, it may be

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[2] For example, "This Convention applies where any of the following are located in different States: (a) the securities account; (b) the issuer [or issuers] of the securities, (c) the account holder; (d) any party to a disposition of the securities [or an account right] or any interest in the securities [or the securities account]; or (e) any intermediary through whom, mediately or immediately, the securities are held."

worthwhile to recall that in the US project on the Revised Article 8 of the UCC, some people thought that it was always easy to tell what office or branch of an intermediary maintained an account, while others though it was often difficult or impossible to tell. Article 8 ended up with a pragmatic resolution, saying that if the agreement between the intermediary and investor contained a choice of law clause, the law selected counts as the intermediary's jurisdiction. That in turn, determines the law applicable not only to the rights and duties of the investor and intermediary *inter s*e, but also the law applicable to transfer and pledge, e.g., perfection and priorities of a security interest. That approach does two things: First, since account agreements invariably do have a choice of law clause, it provides a convenient way of resolving ambiguity in cases where it's hard to say what office maintains the account. Second, it allows the intermediary and investor to select the law of a jurisdiction—even if that jurisdiction is not otherwise related to the arrangement—in case the 'home' jurisdiction does not have a developed law. The US law on the subject is found in UCC revised article 9-305(a)(3) and in UCC article 8-110(e), as refined in conjunction with revised Article 9.

At the "experts meeting" at The Hague January 15-19, it was apparent that the delegations from most other countries would not accept this approach, which they considered—incorrectly in our view —an improper application of party autonomy notions to third party rights. It is unfortunate that the discussion was phrased in terms of "party autonomy." What, in fact, was sought was an efficient, certain and workable choice of law pointer. It is likely that the Convention will probably say that an agreed designation of the intermediary's jurisdiction is effective only if there is some appropriate nexus.

Are the nexus factors in the current draft of Article 4(2) workable? The rule in Article 4(2) allowing designation of intermediary's jurisdiction by agreement is the key to certainty in application of the Convention, so it is essential that all transaction patterns can be fit within it. Do all transactions you are familiar with fit? If not, what steps would you have to take to make them fit?

Article 4(2) uses the word "agreed" rather than referring to any specific form of agreement or requiring a written agreement. This leaves it to local contract law to say what constitutes an agreement. In many cases, it should be possible for current account arrangements to be supplemented to take advantage of Article 4(2), e.g., by rule change in CSDs or by some form of supplemental notice/agreement. Is it feasible for you to take advantage of this clause? Would it present significant problems of reopening agreements produced through delicate negotiations?

The Article 4(2) "nexus" proviso has two components: (1) that the intermediary actually has an office or branch at the designated location and (2) that the intermediary "[treats][records] the securities account as being maintained at that office or branch for

purposes of reporting to its account holders or for regulatory or accounting purposes." The office or branch component doesn't seem to present serious interpretation issues. Though it would preclude selection of an entirely unrelated law, we discuss below a possible "work-around." (See discussion under heading "Opt-out of nexus requirement for agreements designating intermediary's jurisdiction" and Appendix B to this memorandum.) The other component of the nexus proviso presents more serious drafting and interpretation issues.

The bracketed words "[treats][records]" have been suggested by the Permanent Bureau as replacement for the phrase "allocates" which appeared in the working draft produced at the Hague meeting. As we parse this language, there are two prongs. The test would be satisfied if the intermediary treats the account as located at the agreed place either "for purposes of reporting to its account holders," or "for regulatory or accounting purposes." Even if the last prong does not require that there be any specific form of "report" to regulators, one would still have to be able to say that the account is treated as located at the designated place "for regulatory or accounting purposes." Will transactions you know fit within this language?

We understand that some delegations have expressed concern about the "reporting to its account holders" test on the grounds that it could permit the kind of artificial treatment that the nexus limitation is supposed to prevent. We have indicated that we feel this prong is very important, not as an evasion device but because of the possibility that some scenarios may not easily fit within either of the other prongs (regulatory or accounting treatment).

The second major issue in Article 4 is whether there should be, and, if so, how to design, a "fall-back" rule for cases that do not fit within the Article 4(2) agreed location rule. This could happen either because there is no such agreement between the account holder and its securities intermediary or because the agreed location does not satisfy the nexus test. One approach would be to have no specific fall-back rule. Rather, if Article 4(2) doesn't apply, one would apply the general Article 4(1) ("place where the securities account is maintained"), taking no account of the "black-list" factors listed in current Article 4(4). At the Hague meeting, the group seemed to feel that some more specific fall-back rule was needed, but we would be interested in hearing views on that point—particularly in light of the difficulty of drafting a truly effective fall-back rule.

As currently drafted, the fall-back rule in Article 4(3) probably suggests greater consensus than actually exists on the role and relative significance of possible fall-back locating factors. Rather than focussing in detail on the drafting, or limiting your thoughts to the concepts included here, please consider, in general, the possible use of various location factors, such as:

the office or branch where the account is treated/recorded for purposes of reporting tothe account holder

the office or branch where the account is treated/recorded for accounting purposes

the office or branch where the account is treated/recorded for regulatory purposes

the State whose law governs the agreement between the account holder and its
securities intermediary establishing the securities account

the place where the legal entity that is the relevant securities intermediary that has contracted with the account holder to maintain the securities account is legally established

In addition to your reactions to these factors and your view on the sequence in
which they should appear in the cascade, we would be particularly interested in hearing suggestions for other approaches.

Article 5

Does Article 5 properly capture the matters that should be governed by the law of
the intermediary's jurisdiction? The wording differs from customary US terminology to capture other countries' concepts, e.g., the UK device of title transfer for purposes of security. Note that some of the Article 5 clauses deal with matters that US lawyers would probably place in separate categories—creation of a security entitlement and the perfection of a security interest in a security entitlement. That is largely a product of the need to cover both the US concept of security interests and other countries' concepts of security via pledge versus title transfer. We think that the Article 5 works, but careful attention to the definitions in Article 2 is required to translate Article 5 language into US concepts.

Note that Article 5(d) ("priority of any person's title to or interest in the account
right as against any competing title or interest") is intended to include the point stated in UCC 8-110(b)(4) using the "adverse claim" concept.

Article 5 is, of course, the heart of the Convention. Nevertheless, it received the
least attention. A draft was quickly produced, it met with general agreement, and that was it. Accordingly, we would appreciate your careful attention and consideration of

whether there are important points that are missed, or whether any of the items listed in Article 5 might be construed to cover matters that should not be governed by the law of the place of the relevant intermediary.

Article 6

This Article attempts to walk a delicate line. It seems desirable to proscribe application of local insolvency laws that could, in effect, vitiate the effectiveness of a security interest perfected under the law of the place of the relevant intermediary. On the other hand, it would go far beyond the scope of the Convention to completely deal with the effect of insolvency on a perfected security interest. The bracketed phrase "ranking of categories of claim" is intended to cover such matters as insolvency rules that give priority to tax or wage claims even over a perfected security interest.

We would appreciate comments from two perspectives. First, from the standpoint of US institutions as holders of security interests in collateral, does Article 6(1) accomplish something useful in limiting the risk of disregard of security interests in insolvency proceedings under other State's law? Second, from the standpoint of US bankruptcy law, does Article 6(2) adequately preserve the effectiveness of all rules of US bankruptcy law that may affect secured creditors which should be preserved? It seems to us that these two perspectives are probably in tension, so we would appreciate careful attention to the precise wording of this Article, and suggestions for improvements, particularly from commentators with special expertise in bankruptcy law.

Articles 7 & 8

These are standard Hague Convention clauses. We see no problems here, except that the title of Article 8 "(Exclusion of *renvo*i") is too restrictive and probably should be changed to something like "Exclusion of choice of law rules," which is what the Article substantively provides.

Articles 9 & 10

These too are standard clauses in Hague Conventions, though they may be more significant. The concept of "mandatory rules" is not commonly used in US conflicts law, though the same results may be achieved by virtue of other concepts such as public policy. We believe that the provisions of Article 9 have been fairly well limited in this draft, but would appreciate comments. Article 10 requires additional careful amendment to properly circumscribe its scope.

We were quite pleased that the group agreed to include the final clause in

Article 9, which explicitly excludes local rules on perfection and priorities from the mandatory
rules provision. For example, if the law of a debtor's jurisdiction requires local filing for perfection of a security interest—even though the secured party has taken control—Article 9(1) would preclude a court in the debtor's jurisdiction from invalidating the security interest for lack of filing, so long as the interest has been perfected under the law of the place of the relevant intermediary.

Article 11

This article deals with a very important subject for the US. The Convention rules
should not come into play in cases where the only issue is which US law (State or Federal)
applies. This is important for several reasons. First, there will presumably be some points on which the Convention rules differ from the conflicts rules already in force in the US. We can already see that in the Article 4 rules on location of intermediary. We think it very important that the current US rules remain in force for purely domestic conflicts, particularly since people have been engaging in transactions in reliance upon those rules for over five years. Second, even if there were no real differences of substance between the Convention rules and the domestic US conflicts rules, there will inevitably be some difference in expression. We think it would be highly unproductive to end up with a structure in which litigants could seek to take advantage of minor differences in wording or in which opinion practice had to worry about that possibility.

We don't think Article 11 in the current draft is adequate. Included is an alternative to current Article 11, suggesting how it might be changed. We have tried to take account of several different issues.

The standard Hague Convention provisions regarding these issues usually speak
only of different "territorial units" within a State. It should be made clear that this article also applies to the issue of choice between US federal law and the law of a US state. For example, this is particularly important because of the provisions in federal law on Treasury securities (TRADES) and similar provisions for various GSE securities.

The standard Hague Convention provision just says that a "federal state" is
notbound to apply the Convention to conflicts among its units. We think it might be useful to require that any State that regards itself as covered by this provision be required to make a declaration with the Hague Conference so stating. Our suggested redraft Article 11(1) does that. Note that Article 11(1) deals only with cases in which the forum court
Is within the "federal state" in question.

A separate, but related, issue arises if a forum court in another State faces a Choice among the laws of constituent units of a "federal state." Our suggested redraft Article 11(2) deals with that issue. It says that the foreign court must apply the Federal State's internal conflicts rules rather than the Hague Convention rules.

Note that, although our suggested redraft requires that the Federal State make a declaration, it does not require that the declaration itself spell out the content of the internal conflicts rules. We have given some thought to requiring that, but worry that, if the Convention did so, there might be some slippage between the wording in the declaration describing the rules and the wording in the domestic rules themselves.

To illustrate the operation of the "States with more than one legal system" or "federal article:"

Suppose, for example, that a securities intermediary "located" in New Hampshire uses an account agreement that selects Massachusetts as the securities intermediary's jurisdiction, even though the securities intermediary has no other connection to Massachusetts. Under the UCC rules, the selection of Massachusetts in the account agreement is effective, even with respect to third party issues such as perfection and priorities. However, it presumably would not meet the nexus test in HC Article 4. Under HC Article 11(1), a forum court in the United States can apply the UCC rules rather than the HC rules. Under HC Article 11(2), a forum court in another country must also apply the UCC rules to the choice between Massachusetts and New Hampshire law. Article 11, however, would not preserve the UCC rules if the issue were a choice between US law and the law of a foreign country. Suppose that the New Hampshire intermediary selects Ontario as the securities intermediary's jurisdiction. Even if both the US and Canada have made declarations under our proposed Article 11, and even if the domestic conflicts laws of both the US and Canada would give effect to the agreement's selection of Ontario, Article 11 would not apply, because this is not a conflict between the laws of constituent units of a single Federal State.

Matters Not Covered in Current Draft.

Opt-out of nexus requirement for agreements designating intermediary's jurisdiction.

As a consequence of dispute over the role of "party autonomy" in Article 4, it seems likely that the Convention rule will be more restrictive than current US rules on agreements specifying the intermediary's jurisdiction. Insofar as the issue is only a

matter of selection of the laws of one of the States of the United States or between Federal
and State rules, the issue can covered by the "federal state" provision in Article 11.

An example of a case that we felt might call for the possibility of a less restrictive
rule than the Convention's would arise if some developing country, call it "Batavia," wants to establish an indirect holding system, or permit a global bank to set up such a system through a branch in Batavia, but does not have an adequate body of substantive commercial law. Suppose that Batavia wishes to allow the intermediary to specify in the agreements with its account holders that New York law will govern the arrangement. Assume that Batavia wishes to become a party to the Hague Convention, but doesn't like the requirement of a "nexus" for selection of the intermediary's jurisdiction. If the dispute is purely domestic, it is possible that the Hague Convention will never come into play—though this depends on exactly how the territorial scope provision in Article 1(2) is worded. A more problematic situation would arise if the Batavian intermediary selects New York law, but the investor is from another country, say, France. The most likely place of litigation would be the investor's home jurisdiction, e.g. a bankruptcy proceeding in France. If the French court looks to the Hague Convention, including the "nexus" limitation, it would conclude that the matter is governed by Batavian law, because the Batavian intermediary's selection of New York law does not meet the "nexus" requirement. That seems odd, given that by hypothesis Batavia permitted the selection of New York law because it had concluded that Batavian law was inadequate to

the task. (Indeed, note that as the Convention is currently written, even a forum in the US would be required to apply the Convention rules, including the nexus requirement of Article 4.)

It seems to us that, if other countries do not want to permit unlimited designation
of the intermediary's jurisdiction by agreement, so be it, but that should not prevent the US or other similarly minded jurisdictions from allowing this.

At the meeting at The Hague, we quickly drafted language to implement this idea.
(For those present at the Hague meeting or who have seen documents from the meeting, this is the "Working Document 14" issue.) We have worked more on drafting, and attach as Appendix B our current thinking on how the issue might be handled. We would appreciate hearing others' sense of the importance of the matter so that we can design our negotiation strategy appropriately.

Preservation of US rules on perfection by filing and automatic perfection.

Discussions of the issues covered by this Convention typically focus on PRIMA
versus "look through" approach. But there is one issue on which the current US choice

of law rules are not consistent with PRIMA—though they differ in a different direction from the "look through" approach that we are seeking to exclude.

Under 9-103(6)(f) and Rev'd 9-305(c), perfection of a security interest in investment property by filing, and automatic perfection of a security interest granted by a broker or securities intermediary, is governed by the law of the debtor's jurisdiction. The main point of that rule, of course, is that the financing statement should be filed in the debtor's location, not the location of the securities intermediary through which the debtor holds the securities. That is a deviation from PRIMA. Note, however, that all other issues, such as duties of the intermediary to the secured party or priority of the filed security interest against other claims, are still governed by the law of the intermediary's jurisdiction.

In a case where both the debtor and the intermediary are located in the United States, our proposed Article 11 would solve the problem because the choice among states of the United States is governed by domestic conflicts rules. If, however, a US debtor grants a security interest in a securities account maintained with a foreign intermediary, the perfection by filing rule of US law would not apply, because the Hague Convention would point to the foreign jurisdiction (PRIMA) for the law governing perfection.

We have attached as Appendix C a draft article designed to cover this issue. We would appreciate hearing others sense of the importance of the matter so that we can design our negotiation strategy appropriately.

Appendix A

Hague Conference project on the law applicable to dispositions of securities held through indirect holding systems

Suggestion for amendment of the text of Working Document No. 16 submitted by the Permanent Bureau, the Legal Expert to the Permanent Bureau and the Chair of the Drafting Group

Article 1 Scope of the Convention

(1) This Convention determines the law governing proprietary aspects of dealings in securities held indirectly through a securities account.

(2) This Convention applies in all cases involving a choice between the laws of different States.

Article 2 Interpretation

(1) In this Convention:

"securities" means any stocks, shares, bonds or other financial assets or instruments, or any interest therein, that may be credited to a securities account;

"securities intermediary" means a person that maintains for others accounts to which securities are credited and is acting in that capacity or for its own account;

"securities account" means an account with a securities intermediary to which securities are credited;

"account right" means the aggregate of the rights of an account holder derived from a credit of securities to a securities account;

"account holder" means a person to whose securities account securities are credited;

"disposition" means a pledge or outright transfer of title;

"pledge" includes mortgage, charge and any other form of security interest which is not an outright transfer of title;

"perfection" means completion of the steps necessary to render a disposition of an account right effective against persons who are not parties to that disposition;

Appendix A

"insolvency administrator" means a person or body, including one appointed on an interim basis, authorised in an insolvency proceeding to administer the reorganization or liquidation of the debtor's assets or affairs;

"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.

(2) References in this Convention to an account right include any interest in an account right.

(3) References in this Convention to a disposition of an account right include a disposition to or in favour of the account holder's securities intermediary.

Article 3 Determination of the applicable law

Proprietary aspects of dealings in securities credited to a securities account are governed by the law of the place of the relevant securities intermediary.

Article 4 Determination of the place of the relevant securities intermediary

(1) In this Convention, the place of the relevant securities intermediary means the place where the securities account is maintained.

(2) For the purposes of this Convention, the securities account is [deemed to be] maintained at the place agreed between the account holder and its securities intermediary, provided that such place is a place where the securities intermediary has an office or branch and the securities intermediary [treats][records] the securities account as being maintained at that office or branch for purposes of reporting to its account holders or for regulatory or accounting purposes.

(3) If the place where the securities account is [deemed to be] maintained is not determined under paragraph (2), the place where the securities account is maintained is:

(a) the place of the office or branch at which the relevant securities intermediary [treats][records] the securities account as being maintained for purposes of reporting to its account holders;

(b) if the place where the securities account is maintained cannot be determined under sub-paragraph (a), the place of the office or branch at

Appendix A

which the relevant securities intermediary [treats][records] the securities account as being maintained for regulatory purposes;

(c) if the place where the securities account is maintained cannot be determined under sub-paragraphs (a) or (b), the place of the office or branch at which the relevant securities intermediary [treats][records] the securities account as being maintained for accounting purposes;

(d) *Variant* 1:
if the place where the securities account is maintained cannot be determined under any of sub-paragraphs (a) to (c), the place where the securities intermediary which has contracted with the account holder to maintain the securities account is legally established;

Variant 2:
if the place where the securities account is maintained cannot be determined under any of sub-paragraphs (a) to (c), the State whose law governs the agreement establishing the securities account.

(4) In applying the provisions of this Article no account shall be taken of the following:

(a) the place where the technology supporting the bookkeeping or data processing is located;

(b) the place where certificates representing or evidencing securities are located;

(c) the place where any register of holders of securities maintained by or on behalf of the issuer of the securities is located;

(d) the place where the issuer of the securities is organised or incorporated or has its statutory seat or registered office;

(e) the place where any intermediary other than the securities intermediary that has contracted with the account holder to maintain the securities account is located; or

(f) the place where the account holder is located.

Appendix A

Article 5 Scope of the applicable law

The applicable law determines:

(a) the legal nature of the rights constituting an account right;

(b) the proprietary aspects of any [acquisition,] variation, disposition or extinction of an account right;

(c) any requirements for perfection of a disposition of an account right;

(d) the priority of any person's title to or interest in the account right as against any competing title or interest and the duties, if any, of a securities intermediary to a person who asserts an adverse claim to the account holder's interest; and

(e) any steps required for the realisation of an account right subject to a pledge.

Article 6 Insolvency

(1) The opening of an insolvency proceeding shall not affect the effectiveness of an acquisition or disposition of an account right, constituted and perfected in accordance with the law of the place of the relevant securities intermediary.

(2) Nothing in this Article affects the application of:

(a) any rules of insolvency law relating to the [ranking of categories of claim or to the] avoidance of a transaction as a preference or a transfer in fraud of creditors; or

(b) any rules of insolvency procedure relating to the enforcement of rights to property which is under the control or supervision of an insolvency administrator.

Article 7 General applicability

This Convention applies even if the applicable law is that of a non-Contracting State.

Article 8 Exclusion of *renvoi*

In this Convention, the term "law" means the law in force in a State other than its choice of law rules.

Appendix A

Article 9 International mandatory rules

This Convention does not prevent the application of those provisions of the law of the forum which, irrespective of rules of conflict of laws, must be applied even to international situations, other than any provision imposing requirements with respect to perfection or relating to priorities.

Article 10 Public policy

The provisions of any law determined by this Convention may be disregarded when their application would be manifestly incompatible with public policy.

Article 11 States with more than one legal system

(1) A State within which different territorial units have their own rules of law in respect of any matter dealt with in this Convention shall not be bound to apply this Convention to conflicts solely between the laws of such units.

(2) In relation to a State in which two or more sets of rules of law with regard to any matter dealt with in this Convention apply in different territorial units, any reference to the place of the relevant securities intermediary shall be construed as referring to the territorial unit of the relevant securities intermediary.

Appendix B

US Delegation Suggestion for Article allowing "non-nexus" location selection

Article XX Determination by another State of applicable law with respect to States having made certain declaration.

(1) Any State may, at the time of signature, ratification, acceptance, approval or accession make a declaration that in determining the place of the law of the relevant intermediary, an agreement between a securities intermediary and account holder specifying what shall be deemed to be the place of the relevant intermediary [or what law governs proprietary aspects of dealings in securities credited to the securities account] is effective even though the conditions stated in the proviso to Article 4, paragraph 2 are not satisfied. Any such declaration shall be submitted to the depositary and may be modified submitting another declaration at any time.

(2) In applying this Convention, if a court in another State determines that the place of the relevant securities intermediary is in a State making a declaration provided for in Paragraph 1(a), it shall [be bound to] apply the rule specified in such declaration to determine the law applicable to the issues governed by this Convention.

(possibly add limiting factors, such as)

(3) Any such declaration pursuant to Paragraph 1(a) must

- identify specifically the States within which the place of the relevant intermediary may be deemed to be [or whose law may be selected to govern proprietary aspects of dealings in securities credited to the securities account] or specifying the rule of law applicable to the selection of such States;

- provide that such an agreement is effective only if the place designated as the place of the relevant intermediary [or State whose law is designated to govern proprietary aspects of dealings in securities credited to the securities account] is a place where:

(a) the securities intermediary has an office, branch or a controlled subsidiary;
(b) an account holder, including another securities intermediary, is located;
(c) the securities intermediary or account holder is incorporated; or
(d) another securities intermediary through whom the first mentioned securities intermediary holds securities is located

- provide that such an agreement is effective only if the designation of the place of the relevant intermediary [or State whose law is designated to govern proprietary aspects of dealings in securities credited to the securities account] has been designated for a legitimate and explicit business purpose and has not been made for fraudulent or other illicit purposes or primarily to avoid the effect of international mandatory rules of law of another State that would otherwise be applicable under this Convention.

US Delegation Memo on Proposed Draft Hague Convention
Appendix C
On Indirect Securities Holding

US Delegation Suggestion for Article on perfection by filing

Article XXX

This Convention does not preclude the application of the law of the State where the account holder is located to the perfection of a pledge of an account right if that law permits perfection by means, such as local filing, that do not involve any entry on the books of or agreement with the securities intermediary, provided that the law of the relevant securities intermediary does apply to questions of the duties, if any, of the securities intermediary to the pledgee and to the priority of such pledge against any other pledge or interest in the account right.

PRELIMINARY SUGGESTIONS FOR DISCUSSION BY US DELEGATION

Hague Conference project on the law applicable to dispositions of securities held through indirect holding systems

Suggestion for amendment of the text of Working Document No. 16 submitted by the Permanent Bureau, the Legal Expert to the Permanent Bureau and the Chair of the Drafting Group

Article 1 Scope of the Convention

(1) This Convention determines the law governing the proprietary aspects specified in Article 5 of dealings in securities held indirectly through a securities account.

(2) This Convention applies in all cases involving a choice between the laws of different States.

Article 2 Interpretation

(1) In this Convention:

"securities" means any stocks, shares, bonds or other financial assets or instruments, or any interest therein, that may be credited to a securities account;

"securities intermediary" means a person that maintains for others accounts to which securities are credited and is acting in that capacity or for its own account;

"securities account" means an account with a securities intermediary to which one or more securities are credited;

"account right" means the aggregate of the rights of an account holder derived from a credit of ~~securities~~a security to a securities account;

"account holder" means a person to whose securities account one or more securities are credited;

"disposition" means a pledge or outright transfer of title;

"pledge" includes mortgage, charge and any other form of security interest ~~which is not~~and a transfer of title for security purposes, but excludes an outright transfer of title;

"perfection" means completion of the steps necessary to render a disposition of an account right effective against persons who are not parties to that disposition;

"insolvency administrator" means a person or body, including one appointed on an interim basis, authorised in an insolvency proceeding to administer the reorganization or liquidation of the debtor's assets or affairs;

"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.

(2) References in this Convention to an account right include any interest in an account right or a securities account as a whole.

(3) References in this Convention to a disposition of an account right include a disposition to or in favour of the ~~account holder's~~relevant securities intermediary.

[The scope of the Convention should include the creation and priority of a lien, including a statutory lien, in favour of a securities intermediary. This could, for example, be covered by extension of Article 2(3) or by addition to Article 5(d).]

Article 3 Determination of the applicable law

~~Proprietary~~The proprietary aspects specified in Article 5 of dealings in securities ~~credited to~~held indirectly through a securities account are governed by the law of the place of the relevant securities intermediary.

Article 4 Determination of the place of the relevant securities intermediary

(1) In this Convention, the place of the relevant securities intermediary means the place where the securities account is maintained.

(2) For the purposes of this Convention, the securities account is [deemed to be] maintained at the place agreed between the account holder and its securities intermediary, provided that such place is a place where the securities intermediary has an office or branch and the securities

intermediary [treats][records] the securities account as being maintained at that office or branch for purposes of reporting to its account holders [the purpose of reporting to the account holder] or for regulatory or accounting purposes.

(3) If the place where the securities account is [deemed to be] maintained is not determined under paragraph (2), the place where the securities account is maintained is:

(a) the place of the office or branch at which the relevant securities intermediary [treats][records] the securities account as being maintained for purposes of reporting to its account holders [the purpose of reporting to the account holder];

(b) if the place where the securities account is maintained ~~cannot~~is ~~be~~not determined under sub-paragraph (a), the place of the office or branch at which the relevant securities intermediary [treats][records] the securities account as being maintained for regulatory purposes;

(c) if the place where the securities account is maintained ~~cannot~~is ~~be~~not determined under sub-paragraphs (a) or (b), the place of the office or branch at which the relevant securities intermediary [treats][records] the securities account as being maintained for accounting purposes;

(d) ~~*Variant 1:*~~
if the place where the securities account is maintained ~~cannot be~~is not determined under any of sub-paragraphs (a) to (c), the State whose law governs the agreement establishing the securities account; or

(e) if the place where the securities account is maintained is not determined under any of sub-paragraphs (a) to (~~c~~d), the place where the legal entity that is the relevant securities intermediary which has contracted with the account holder to maintain the securities account is legally established~~;~~ [or incorporated or has its statutory seat, registered or principal place of business or chief executive office];

~~*Variant 2:*~~
~~if the place where the securities account is maintained cannot be determined under any of sub-paragraphs (a) to (c), the State whose law governs the agreement establishing the securities account.~~

(4) In applying the provisions of this Article no account shall be taken of the following:

(a) the place where the technology supporting the bookkeeping or data processing is located;

(b) the place where certificates representing or evidencing securities are located;

(c) the place where any register of holders of securities maintained by or on behalf of the issuer of the securities is located;

(d) the place where the issuer of the securities is organised or incorporated or has its statutory seat or registered office;

(e) the place where any intermediary other than the legal entity that is the relevant securities intermediary that has contracted with the account holder to maintain the securities account is located; or

(f) the place where the account holder is located.

Article 5 Scope of the applicable law

The applicable law determines:

(a) the legal nature of the rights constituting an account right;

(b) the proprietary aspects of any [acquisition,] variation, disposition or extinction of an account right;

(c) any requirements for perfection of a disposition of an account right;

(d) the priority of any person's title to or interest in the account right as against any competing title or interest and the duties, if any, of a securities intermediary to a person who asserts an adverse claim to the account holder's interest; and

(e) any steps required for the realisation of an account right subject to a pledge.

Article 6 Insolvency

(1) The opening of an insolvency proceeding shall not affect the effectiveness of an acquisition or disposition of an account right, [constituted and]

perfected in accordance with the law of the place of the relevant securities intermediary.

(2) Nothing in this Article ~~affects~~shall [affect/change/alter] the effect of such [constituted and] perfected disposition in the insolvency proceeding, including the application of:

(a) any rules of insolvency law relating to the ~~[~~ranking of categories of claim or to the~~]~~ avoidance of a transaction [transfer] [disposition] as a preference or a transfer in fraud of creditors; or

(b) any rules of insolvency ~~procedure~~law relating to the effect and enforcement of rights [constituted and] perfected under otherwise applicable law] to property which is under the control or supervision of an insolvency administrator.

Article 7 General applicability

This Convention applies even if the applicable law is that of a non-Contracting State.

Article 8 Exclusion of ~~*renvoi*~~choice of law rules

In this Convention, the term "law" means the law in force in a State other than its choice of law rules.

Article 9 International mandatory rules

This Convention does not prevent the application of those provisions of the law of the forum which, irrespective of rules of conflict of laws, must be applied even to international situations, other than any provision imposing requirements with respect to the [constitution or] perfection of dispositions or relating to priorities.

Article 10 Public policy

The provisions of any law determined by this Convention may be disregarded ~~when~~to the extent their application would be manifestly incompatible with fundamental public policy of the forum.

Article 11 States with more than one legal system

(1) A State within which different territorial units have their own rules of law in respect of any matter dealt with in this Convention shall not be bound to apply this Convention to conflicts solely between the laws of such units.

(2) In relation to a State in which two or more sets of rules of law with regard to any matter dealt with in this Convention apply in different territorial units, any reference to the place of the relevant securities intermediary shall be construed as referring to the territorial unit of the relevant securities intermediary.

Preliminary US Delegation ~~Suggestions~~suggestion for ~~Revision~~discussion of revision of Article 11

(1) A State within which the State and one or more of its territorial or other units have their own substantive rules of law or choice of law rules in respect of any matter dealt with in this Convention may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention shall not apply to conflicts solely among the laws of such State and units. Any such declaration shall be submitted to the depositary and may be modified by submitting another declaration at any time.

(2) In applying this Convention, if a court in another State determines that the place of the relevant securities intermediary is in such a declaring State, the court shall apply the rules in force in ~~such~~the declaring State for determining which of the laws of the State and one or more of its territorial or other units is applicable.

(3) If ~~there is no declaration referred to in paragraph (1), or~~a State has made no declaration under paragraph (1), or there are no rules referred to in paragraph (2), the rules of this Convention shall apply to determine which of the laws of the State and one or more of its territorial or other units is applicable~~.~~