RESPONSE OF THE INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INC. to the European Commission Consultation Document on conflict of laws rules for third party effects of transactions in securities and claims

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General Note:

The International Swaps and Derivatives Association, Inc. (ISDA). ISDA is the principal international trade association for the derivatives industry. Further information about ISDA can be found on our website at: http://www.isda.org.

The Consultation Document specified that responses must be submitted on-line. The following document sets out the text of those responses as submitted on-line.

QUESTIONS

Question 1

Do you observe in practice that legal opinions on cross-border transactions in securities and claims contain an analysis of which law is applicable (conflict of laws)? Please elaborate on your reply if you have further information.

- Yes, always where relevant
- In general yes, but not in all relevant situations
- In rare cases yes, but often not
- No, in general legal opinions do not include an analysis of which law applies
- I don't know / I am not familiar with legal opinions

In general yes, but not in all relevant situations.

Our members seek legal opinions on cross-border transactions for various purposes and in various contexts. Some are transaction-specific opinions and some are generic opinions, applicable to any transaction that falls within the scope of the opinion.

Whether or not a legal opinion includes an analysis of the conflict of laws position depends entirely on the context, including the legal risk management needs of the party or parties commissioning the opinion. As far as we are aware, however, it is commonplace for our members to request that a legal opinion on a cross-border transaction involving the transfer of securities or claims, in particular in the context of the giving of financial collateral, should also deal with the relevant conflict of laws rules that apply.

For example, we request such an analysis in the opinions that we have commissioned from local counsel in relation to the enforceability of financial collateral taken under standard form credit support documents that we have published. Currently, we have such opinions from local counsel in fifty-five jurisdictions globally (with opinions from additional jurisdictions currently commissioned and in preparation), including 19 Member States of the European Union.

Question 2

Do you think that default of a large participant in the financial market who holds assets in various Member States could possibly create difficult conflict of laws questions, putting in doubt who owns (or has entitlement to) which assets?

- Yes
- No
- I don't know

If no, please explain why.

If yes, please provide concrete examples or specify in which legal context this problem might arise, pointing also to relevant national provisions where possible.

If yes, please give an estimate of the magnitude of the issue (e.g. number or value of transactions that might be concerned).

If yes, please explain how market participants deal with such legal uncertainty.

No.

See our answer to Question 3. The uncertainties that we highlight in our response to that question are capable of creating difficulties for financial market participants in planning and structuring a cross-border financial transaction because of potential uncertainty as to which law applies to govern the proprietary effect (that is, the effect on the rights of third parties) of a holding or transfer of intermediated securities, and therefore potential uncertainty as to how to manage some of the legal risks of the transaction, where to perform the necessary legal due diligence and so on. In practice, these are for the most part manageable risks, but the current situation is less than ideal, and any material legal uncertainty adds potential cost.

In the event of the default of a large financial market participant, the principal proceedings governing its insolvency will, for the most part, determine questions relating to entitlement to assets, including its own entitlement to assets and, where it is holding assets as a custodian, on trust or as security, the entitlement of others to assets it is holding.

Question 3

Are you aware of actual or theoretical situations where it is not clear how to apply EU conflict of laws rules, or their application leads to outcomes that are inconsistent?

- Yes
- No
- I don't know.

If yes, which rules, what is their interpretation and in which Member State(s)? What is the impact of such ambiguity? How does the market deal with this ambiguity?

If no, please explain how you interpret and apply the Place of the Relevant Intermediary Approach (PRIMA), in which types of transactions and in which Member State(s)?

Yes.

There are broadly three categories of problem with the current state of EU conflict of laws rules in relation to intermediated securities:

1. *Inconsistency*: The rules that apply to the proprietary effect of a transfer of intermediated securities are formulated differently under different EU instruments, such as the Settlement Finality Directive (SFD), the Financial Collateral Arrangements Directive (FCAD) and the Winding Up Directive for Credit Institutions (WUDCI);

2. *Large gaps in coverage*: The current sectoral conflict of laws rules that apply under various EU instruments do not, between them, cover all holdings and transfers of intermediated securities; and

3. *Lack of ex ante certainty*: the current sectoral conflict of laws rules that apply under various EU instruments are all based on ascribing a location to an account, which is an inadequate conceptual basis that does not provide *ex ante* certainty under current market conditions and is likely to prove even more problematic as market practices and market technology continue to evolve.

In relation to the first category, there appears to be no justification in principle for the differences in wording of the rule that applies, under Article 9(2) of the SFD, Article 9 of the FCAD and Article 24 of the WUDCI, to give just three examples. The explanation, of course, for the differences in drafting is simply that each of these instruments was drafted at a different time and for a different purpose, apparently without consideration having been given to ensuring consistency of approach. The rules are broadly similar, but the differences in scope and drafting between them leads to uncertainty, particularly where there is a potential overlap of the application of different instruments to the same transaction.

In relation to the second category, there are many transactions, for example, a sale of intermediated securities from a market participant in one country to a market participant in another country, that are not covered by any uniform EU rule, meaning that a national conflict of laws rule will apply. Many EU Member States have not yet properly modernised their private international law rules to deal with intermediated securities outside the context of the sectoral instruments referred to above. This creates a possible impediment to or, at least, drag on further integration of the EU single market in financial services.

In relation to the third category, the "location" of an account is an inadequate conceptual basis for a conflict of laws rule dealing with the proprietary effect of a transfer of intermediated securities for the reason that an account is, strictly speaking, intangible and therefore has no physical location. A securities account is the acknowledgement by a party, the account provider, of a state of affairs existing between itself and another person, the account holder, as to their mutual rights and obligations in relation to intermediated securities.

An account, however, has a number of potential physical associations, which may be located in different countries. For example: the possible physical associations of an account maintained by a financial intermediary might include: (i) where the account is administered by employees of the financial intermediary; (ii) where account entries are recorded (for example, physically entered into a recording system by employees of the intermediary); (iii) where relevant systems infrastructure such as servers are located; (iv) where customer queries relating to the account may be dealt with by the customer in person; (v) where a customer call centre is located, staffed by employees of the intermediary; (vi) where the branch of the financial intermediary with which the customer ordinarily deals is located; (vii) where the financial intermediary is incorporated; (viii) where the financial intermediary is centrally administered and/or has its principal place of business; and (ix)

where the relevant financial intermediary is principally subject to prudential supervision and/or regulated for conduct of business purposes.

This list is not necessarily exhaustive. Which of these physical associations of an account should be privileged for the purposes of determining where an account is "located"?

The full list of choices will vary in relation to the each financial intermediary. Some of these locations are likely to be overlapping (for example, place of incorporation and principal place of business), but not necessarily in the same way for each financial intermediary. Some will clearly be less suitable than others as a "connecting factor" to link an account with a specific country. For example, the location of servers or similar systems infrastructure may seem to be a less compelling physical association of an account than, say, the location of an intermediary branch. Of course, in relation to this latter example, if the location of the relevant branch is to be the privileged physical association determining the "location" of the account, it must be unambiguously identified. Yet it might be the case, for example, that a customer of a financial intermediary regularly deals with both the London and Dublin branches of the intermediary for various purposes. The customer may assume that its account is in London, while the intermediary may consider that it maintains the account in Dublin, for example, for regulatory or other purposes.

It is sometimes said that although the "location" of an account is uncertain in theory due to its intangible nature, there is normally no practical uncertainty as to where an account is located. That may be true currently in many, if not most, cases, but even that practical certainty is likely to be based on a combination of factors that varies subtly from financial intermediary to financial intermediary. Also the parties may proceed on a confident assumption as to where an account is "located" and then discover under the pressure of litigation, when it is too late to remedy the situation, that the "location" of the account was not, in fact, clear once all relevant factors were considered.

It is also important to bear in mind that the assumed "location" of an account is likely to become increasingly uncertain over time as account relationships are increasingly conducted on a "virtual" basis. The development of financial technology, and in particular, cloud-based services, distributed ledger technology and the like, may make the concept of the "location" of an account more obviously artificial and therefore uncertain than it appears to be today.

Question 4

a) In your Member State, which financial instruments are considered to be covered by the EU conflict of laws rules? Please provide references to relevant [statutory] rules, case law and/or legal doctrine.

b) In particular, are registered shares considered to be covered by the EU conflict of laws rules in your Member State?

- Yes
- No
- I don't know

If no, what could be the appropriate conflict of laws solution for those assets in your opinion?

c) In particular, are exchange-traded derivatives considered to be covered by the EU conflict of laws rules in your Member State?

- Yes
- No

- I don't know

If no, what could be the appropriate conflict of laws solution for those assets in your opinion?

As an international trade association, we defer to institutions and firms in each Member State as to the appropriate answer to this question for their Member State.

Question 5

In your Member State, how do statutory rules, case law and/or legal doctrine answer the question which is the relevant 'record' for conflict of laws purposes? Please provide references.

As an international trade association, we defer to institutions and firms in each Member State as to the appropriate answer to this question for their Member State.

Question 6

a) Please describe how exactly you define and apply in practice the Place of the Relevant Intermediary Approach (PRIMA) in your Member State? If appropriate, please provide references to relevant case law and/or legal doctrine that corroborate your interpretation.

b) In your experience, do different substantive laws in one cross-border holding chain interact smoothly or do they create problems in practice? Please provide examples.

As an international trade association, we defer to institutions and firms in each Member State as to the appropriate answer to this question for their Member State.

Question 7

In your experience, what is the scale of difficulties encountered because of dispersal of conflict of laws rules in EU directives and national laws? Please provide examples.

See our answer to Question 3.

Question 8

Do you see added value in Union action to address issues identified in Section 3.1. of this public consultation?

- Yes
- No
- I don't know

If no, what would be the appropriate action in your view?

Yes.

Question 9

Do you think that targeted amendments to the relevant EU legislation containing conflict of laws rules would solve the identified problems?

- Yes
- No
- I don't know

If yes, do you have specific proposals as to which issues should be addressed and how? What would be the order of priority for addressing these issues?

Yes.

It would be useful to introduce a single uniform conflict of laws rule to determine the proprietary effect of the holding or transfer of intermediated securities, applicable regardless of context.

One way to achieve this would be for the EU to adhere to the Hague Securities Convention, although we acknowledge that there has been debate about this issue within the EU. We believe that the some of the criticisms that have been levelled against the Hague Securities Convention during that debate are misconceived, and we believe that other more legitimate concerns can be addressed by appropriate regulatory rules.

For example, where a financial intermediary maintaining an account is a participant in a clearing or settlement system, the financial intermediary can be required to agree that the law specified in the account agreement, which will determine the applicable law under Article 4 of the Hague Securities Convention, will be the law governing that system. We do not necessarily endorse this specific rule. That is a matter for discussion and debate within the EU. We merely give it as an example of the sort of approach that could be taken in order to address concerns raised and make it politically feasible for the EU and EU Member States to adhere to the Hague Securities Convention.

Adherence to the Hague Securities Convention, whether or not subject to further regulatory restrictions in certain contexts along the lines referred to above, together with the repeal or conforming of the currently sectoral rules to the Hague Securities Convention approach, would address the three categories of issues, namely, inconsistency, large gaps in coverage and lack of *ex ante* certainty, which we discuss in our answer to Question 3.

Adhering to the Hague Securities Convention would have the additional advantage of conforming the EU approach to an international approach, currently followed by the US, Switzerland and Mauritius, that is likely to re-gain momentum internationally if the EU also adheres.

If the Hague Securities Convention approach, either directly by adherence or by fashioning a comparable rule based on the law of the account agreement adapted to achieve a consensus within the EU, is not adopted, then a "location"-based approach comparable to that in the FCAD would be the best approach, but where each securities account is ascribed to a location according to a specific, certain connecting factor that is unambiguous and capable of operating in all cases. That rule should be extended to all holdings and transfers of intermediated securities, and the existing rules in the SFD, the FCAD and the WUDCI should be conformed.

Targeted amendments are, of course, capable of resolving the issues of inconsistency and lack of *ex ante* certainty highlighted in our answer to Question 3, but only if a sensible and consistent approach is taken, ensuring that the relevant rules are substantially conformed in scope of application and in substantive operation. There remains, however, the issue of gaps in the coverage of the current rules. We therefore recommend that an appropriate instrument be developed to extend a single consistent rule providing for *ex ante* certainty to all instances of the holding or transfer of intermediate securities. Whether this is done by amendment to an existing EU Directive or Regulation or by incorporating such a rule into a new instrument is a matter of process on which we express no view.

Whatever rule is formulated, it should apply separately to each relationship between an account holder and its immediate intermediary.

Question 10

If there was a targeted solution clarifying which record is relevant for determining the applicable law, do you expect problems if within one Member State the legal relevance of record(s) for conflict of laws purposes does not coincide with the legal relevance of record(s) under substantive law?

- Yes
- No
- I don't know

If yes, please explain your opinion and indicate the relevant national provisions that could generate problems.

If no, please explain your opinion.

No.

It is not clear from the Consultation Document what problem this question is intended to address or what the word "coincide" in the question is meant to signify. As a general principle, a conflict of laws rule provides an entry point to the substantive law of a specific jurisdiction, and the substantive law then operates as normal. The question of the failure of the "legal relevance" of a record for conflict of laws purposes to coincide with its "legal relevance" for substantive law purposes seems, therefore, unlikely to arise.

Question 11

Do you think that an overarching reform of conflict of laws rules on third party effects of transactions in book-entry securities is needed to provide for legal certainty?

- Yes
- No
- I don't know

Yes. See our answer to Question 3.

Question 12

If you prefer an overarching reform, what would be the appropriate connecting factor in your view?

(1) the law of the Place of the Relevant Intermediary Approach (PRIMA);

(2) the law governing the contract (please select among the following options):

(i) the applicable law is chosen by the parties to the account agreement provided that the intermediary has a 'qualifying office' in the country whose law has been chosen, and in the absence of such a choice, determined by objective rules based on the PRIMA connecting factor (the approach of the Hague Securities Convention);

(ii) the applicable law is chosen by the participants of the securities settlement system designated under the Settlement Finality Directive;

(iii) the applicable law is chosen by the parties to the transaction, and in the absence of such choice, determined by objective rules in accordance with the Rome I Regulation;

(3) the law under which the security is constituted;

(4) other solution(s) – please specify.

You can select more than one option in response to Question 12. When making your choice please also explain:

a) the reasons for your preference,

b) which classes of book-entry securities you think each selected option should cover,

c) in which scenario the selected option should apply in your view.

Sub-question to Question 12 answer (1)

a) Please select how should PRIMA be determined:

(1) separately at each level of the holding chain, or

(2) globally for the whole holding chain (Super-PRIMA).

If you prefer Super-PRIMA, please specify which account should be solely relevant for conflict of laws purposes in your view.

b) Please select how should the place of the relevant intermediary be determined:

(1) the intermediary's registered office; or

(2) the intermediary's central administration; or

(3) the intermediary's branch through which the account agreement is handled:

(i) identified by an account number, code or other objective means of identification (Please specify which means should be used to identify the branch) or

(ii) as contractually stipulated in the account agreement; or

(4) other – please specify.

Sub-question to Question 12 answer (2)(i)

a) If you support option (2)(i), do you think the best way is for the Union to become party to the Hague Securities Convention?

- Yes
- No
- I don't know

If yes, do you have data that could help assessing the benefits of a global solution for the EU?

If no, do you have data that could help assessing the drawbacks of the Hague Securities Convention for the EU?

b) Do you consider the Hague Securities Convention should be supplemented by the adoption of a regulatory framework to address potential problems identified so far in discussions on its signature by the Union?

- Yes (*please explain how*)
- No (*please explain why*)
- I don't know

It will be clear from our response to Question 9 that we favour the adoption of the Hague Securities Convention approach, supplemented by the adoption of a regulatory framework to address concerns identified by some critics of the Hague Securities Convention within the EU. We believe that this provides the necessary *ex ante* certainty and is an approach that can be extended and made applicable to all instances of the holding or transfer of intermediated securities. It has the further benefit of representing an international approach.

If such an approach, however, cannot be agreed within the EU for political or other reasons, we favour a formulation of a conflict of laws rule for intermediated securities that provides for greater *ex ante* certainty than the current location-based rules in the SFD, the FCAD, the WUDCI and so on, for the reasons we have given in our responses to Questions 3 and 8.

As per our response to Question 9, we believe that the relevant rule should apply separately to each level within a multi-tiered securities holding structure, which is the current approach within the various EU sectoral instruments, such as the SFD, FCAD and WUDCI, as well as the approach under the Hague Securities Convention. Any other approach is likely, in our view, to lead to potential uncertainty and anomalies.

For example, we do not believe that the so-called "Super-PRIMA" where the applicable law is determined globally for the whole of a chain of securities holdings, for example, by reference to the location of a central securities depository (CSD) in the chain is workable, for various reasons. First, relevant securities may be held in more than one CSD, and it may be unclear, even to a securities holder's immediate intermediary, which CSD is involved in the relevant chain. For example, a Dutch bank acting as intermediary for a Swedish investor may hold securities through a sub-custodian in Paris that holds some of the same issue through Euroclear and some through Clearstream. Some issues may be held initially in a national CSD, with only part of the issue allocated to one of the international CSDs, Euroclear and Clearstream. We do not believe that the Super-PRIMA approach would lead to greater certainty, but rather the reverse.

The current approach of the EU instruments such as the SFD, the FCAD and the WUDCI of applying the rule separately to each level within a multi-tiered securities holding structure works well and is preferable, subject as already discussed to harmonising those rules and introducing a connecting factor that provides the necessary *ex ante* certainty.

Question 13

For each of the options (1)-(4) in Question 12 above, as you defined these in your answers, please indicate the scale of advantages – disadvantages in terms of:

a) an estimated increase / decrease of the number or value of transactions which you are able to undertake in your business (please quantify if possible)

b) an estimated increase / decrease of your legal due diligence costs (please quantify if possible)

c) an estimated increase / decrease of the profitability of your business (please quantify if possible)

d) a change in your business model and the way in which you operate your business

e) any other advantages (please specify and provide relevant data if possible)

f) any other disadvantages (please specify and provide relevant data if possible)

This question, of course, applies to individual market participants rather than to us as an international trade association.

Question 14

In your view, on which of the following issues would options (1)-(4) in Question 12 above have any positive or negative impact:

a) taxation (please specify and quantify if possible)

b) transfer of risks between central depositaries, banks and depositors (please specify and quantify if possible)

c) the effectiveness of clearing and settlement systems (please specify and quantify if possible)

d) the identification of credit institutions' insolvency risks (please specify and quantify if possible)

e) the exercise of voting rights attached to securities (please specify and quantify if possible)

f) the remuneration of the ultimate owners of securities (please specify and quantify if possible)

g) combating market abuse (please specify and quantify if possible)

h) combating money laundering and terrorist financing (please specify and quantify if possible)

The establishment of a uniform conflict of laws rule within the EU that meets the criterion of providing *ex ante* certainty, applies to all holdings and transfers of intermediated securities and applies separately to each relationship between an account holder and an account provider would enhance legal certainty, reduce the cost of legal due diligence, increase liquidity (because more transactions would be done) and therefore promote further integration and efficiency within the European single market in securities. Subject to this, the impact will be either broadly positive or neutral. We do not foresee any potential negative impact of enhancing legal certainty in this area.

Question 15

Which issues should be covered by the scope of the applicable law determined by such conflict of laws rules on third party effects of transactions in book-entry securities:

- the steps necessary to render rights in book-entry securities effective against third parties
- priority issues
- other (*please specify*)

Article 2 of the Hague Securities Convention provides a useful benchmark for the scope of the applicable law determined by a uniform EU conflict of laws rule for intermediated securities. This is true even if an approach other than the specific approach set out in Article 4 of the Hague Securities Convention is followed.

Question 16

Do you have other suggestions for conflict of laws rules for third party effects of transactions in book-entry securities or opinions on this topic that you have not expressed yet above?

No.

Question 17

a) Do transactions in certificated securities still play an important role in your Member State?

- Yes, very important (please estimate the number or value of transactions concerned per year)
- Yes, important (please estimate the number or value of transactions concerned per year)
- Neutral (please estimate the number or value of transactions concerned per year)
- No
- I don't know

b) How often are certificated securities being used as collateral in practice?

- Very frequently (*please estimate the number or value of transactions concerned per year*)
- Frequently (*please estimate the number or value of transactions concerned per year*)
- Sometimes (*please estimate the number or value of transactions concerned per year*)
- Rarely (*please estimate the number or value of transactions concerned per year*)
- Never
- I don't know

Certificated securities are virtually never used to settle a delivery of securities in the OTC derivatives market either to satisfy a physical settlement obligation under a swap, forward or option transaction or to provide financial collateral. Accordingly, we express no views on the questions raised in relation to this part of the Consultation Document.

We are aware, however, the certificated securities remain an important category for other parts of the financial market, and therefore it would appear, in principle, that a consistent, broad-based approach providing *ex ante* certainty would be beneficial in relation to certificated securities. We leave it to others intending to respond to this part of the Consultation Document to consider whether any such reform is necessary in this area.

Question 18

Are conflict of laws rules on third party effects of transactions in certificated securities easily identified in your Member State?

- Yes, there are statutory rules (*please provide reference and indicate the connecting factor*)
- Yes, there is case law (*please provide reference and indicate the connecting factor*)
- Yes, there is legal doctrine (*please provide reference and indicate the connecting factor*)
- No
- I don't know

See our answer to Question 17.

Question 19

Do you see added value in Union action to address the identified issues with regard to certificated securities?

- Yes (*please explain your answer*)
- No
- I don't know

If no, what would be the appropriate action in your view?

See our answer to Question 17.

Question 20

Do you consider that conflict of laws rules on third party effects of transactions in certificated securities should be harmonised at EU level?

- Yes (*please explain*)
- No (*please explain*)
- I don't know

See our answer to Question 17.

Question 21

If you consider that harmonising conflict of laws rules on third party effects of transactions in certificated securities is the appropriate option:

a) What connecting factor do you recommend for certificated registered shares?

b) What connecting factor do you recommend for certificated bearer securities?

c) Which issues should be covered by the scope of the applicable law determined by such harmonised conflict of laws rules:

- the steps necessary to render rights in certificated securities effective against third parties
- priority issues
- other (*please specify*)

See our answer to Question 17.

Question 22

For each of the options (a)-(b) in Question 21 above, as you defined these in your answers, please indicate the scale of advantages – disadvantages in terms of:

a) an estimated increase / decrease of the number or value of transactions which you are able to undertake in your business (please quantify if possible)

b) an estimated increase / decrease of your legal due diligence costs (please quantify if possible)

c) an estimated increase / decrease of the profitability of your business (please quantify if possible)

d) a change in your business model or the way in which you operate your business

e) any other advantages (please specify and provide relevant data if possible)

f) any other disadvantages (please specify and provide relevant data if possible)

See our answer to Question 17.

Question 23

In the past 5 years, have you encountered problems in practice in securing the effectiveness of assignments against persons other than the assignee and the debtor (e.g. a second assignee, a creditor of the assignor or of the assignee) in transactions with a cross-border element?

- Yes
- No
- I don't know

If yes, please specify:

a) How frequently do these difficulties arise in practice?

- *several times per week*
- *several times per month*
- *several times per year*

b) Which category or categories of third parties (e.g. creditors of the assignor, a second assignee) most commonly give rise to difficulties?

c) Please describe shortly as many situations as possible in which these problems have arisen. Please explain whether you were able to overcome the problems and, if so, how.

d) Approximately what percentage of the total transaction costs (legal and other) would be allocated to the legal due diligence required in connection with the above situations?

This question, of course, applies to individual market participants rather than to us as an international trade association.

Question 24

In a typical transaction with a cross-border element involving an assignment of claims, do you undertake legal due diligence with respect to the underlying claim under the law governing the assigned claim?

- Yes
- No
- I don't know

If yes, please specify:

a) Which elements do you verify under the law governing the assigned claim (e.g., assignability of the claim, effectiveness of the assignment against the debtor, other)?

b) How much of the legal costs of a transaction involving an assignment of claims would be allocated to legal due diligence regarding e.g. the assignability of the underlying claim, the perfection of the assignment, or the enforceability of the claim by the assignee against the debtor?

c) Approximately what percentage of the total transaction costs (legal and other) would be allocated to the legal due diligence required in connection with the above situations?

If no (i.e. if you do not undertake due diligence with respect to the underlying claims but accept the legal risks relating, e.g., to the assignability of the claim or its enforceability against the debtor), please explain the reasons for this:

- costs of due diligence
- impossibility to undertake individual verification of the law applicable to each claim assigned
- other (*please explain*)

This question, of course, applies to individual market participants rather than to us as an international trade association. We understand, however, that our members do detailed due diligence on the law governing the assigned claim in relation to cash collateral provided under ISDA Credit Support Annexes as part of their normal legal and credit risk management processes as well as for the purpose of reducing regulatory capital requirements by compliance with, among other things, the legal opinion requirements of the regulatory capital rules. We commission and

make available to members opinions from 55 jurisdictions currently, including 19 EU Member States, as mentioned in our response to Question 1.

Question 25

Do you see added value in Union action to address the identified issues in the area of assignment of claims involving a cross-border element?

- Yes (*please explain your answer*)
- No
- I don't know

If no, what would be the appropriate action in your view?

We are neutral as to whether it is necessary to introduced a harmonised conflict of laws rule governing third party aspects of the voluntary assignment of claims across all sectors, although we agree that the benefits of doing so would be as summarised in the introductory paragraph to part 5.2 of the Consultation Document.

We believe that the law of the assigned claim (option (3) under Question 26) is the best option. It provides a rule that:(i) is consistent over time, (ii) corresponds to the law governing the effectiveness the assigned claim against the relevant debtor of the claim and (iii) is already in effect in a number of important jurisdictions.

In relation to (i), a rule based on the law of the assignor's habitual residence would change over time if the assignor changes habitual residence, which is particularly relevant to an assignor who is a natural person. Also, a rule based on the law of the assignor's habitual residence would mean that a different law would apply in relation to a successive assignment of a claim where the habitual residence of the relevant successive assignor is different. In other words, where C assigns to A and then A assigns to B, where C and A are habitually resident in different countries a different law would apply to each assignment, leading to a potential conflict as to the law that applies to govern the rights of a third party in relation to the assigned claim.

In relation to (ii), the advantage is that a single law applies to proprietary questions, including the enforceability of the assignment against the debtor and as against third parties. This is more likely to accord with the expectations of market participants in the OTC derivatives market than a rule based on option (1) or (2) or some other basis. An important benefit of this is that it would reduce the legal due diligence necessary in relation to a transaction involving the cross-border assignment of claims, as it will already have been necessary to do legal due diligence in relation to the law of the assigned claim.

In relation to (iii), we understand that the law of the assigned claim reflects the current position in Germany, Spain and the UK (England), as well as Japan. We also understand that this is the preferred approach of the securitisations industry. We have seen, for example, a draft of the response to this question prepared by the Association for Financial Markets in Europe (AFME), which clearly supports this approach.

See also our responses to Questions 31 and 32 as to our views regarding the importance of introducing a rule based on the law of the assigned claim in relation to OTC derivatives transactions, including the delivery of cash collateral.

Question 26

What conflict of laws rule on third party effects of assignment of claims would you favour? Please indicate your order of preference among the below options ranging from 1 (best solution) to 4 (least preferred solution):

(1) the law applicable to the contract between assignor and assignee

(2) the law of the assignor's habitual residence

(3) the law governing the assigned claim

(4) other solution(s) (please specify and give reasons for your choice)

Option (3), the law governing the assigned claim. See our answer to Question 25.

Question 27

For each of the above options (1)-(4) please indicate the scale of advantages or disadvantages in terms of:

a) an estimated increase / decrease of the number or value of transactions which you are able to undertake in your business (please quantify if possible)

b) an estimated increase / decrease of your legal due diligence costs (please quantify if possible)

c) an estimated increase / decrease of the profitability of your business (please quantify if possible)

d) a change in your business model or the way in which you operate your business

e) any other advantages (please specify and provide relevant data if possible)

f) any other disadvantages (please specify and provide relevant data if possible)

This question, of course, applies to individual market participants rather than to us as an international trade association.

Question 28

Which issues should be covered by the scope of the applicable law determined by the conflict of laws rule:

- the steps necessary to render rights in claims effective against third parties
- priority issues
- other (*please specify*)

All third party effects of a voluntary assignment of a claim, including priority issues, should be covered by the relevant rule.

Question 29

In your experience, how frequently are claims constituting financial instruments other than book-entry securities or other claims traded on financial markets being assigned?

- Very frequently (*please estimate the number or value of transactions concerned per year*)
- Frequently (*please estimate the number or value of transactions concerned per year*)
- Sometimes (*please estimate the number or value of transactions concerned per year*)
- Rarely (*please estimate the number or value of transactions concerned per year*)
- Never
- I don't know

We do not have the empirical data necessary to answer this question.

Question 30

Are conflict of laws rules on third party effects of assignment of claims constituting financial instruments other than book-entry securities and other claims traded on financial markets easily identified in your Member State?

- Yes, there are statutory rules (*please provide reference and indicate connecting factor*)
- Yes, there is case law (*please provide reference and indicate connecting factor*)
- Yes, there is legal doctrine (*please provide reference and indicate connecting factor*)
- No
- I don't know

As an international trade association, we defer to institutions and firms in each Member State as to the appropriate answer to this question for their Member State. We understand that this question was addressed in the report prepared for the Commission by the British Institute of International and Comparative Law (BIICL).

Question 31

*Would it be useful to provide for a **specific** conflict of laws rule on third party effects of assignment of claims constituting financial instruments other than book-entry securities and/or other claims traded on financial markets which is different from your preferred solution for claims **in general**?*

- Yes
- No
- I don't know

If yes, please:

a) indicate precisely which claims should be covered by such a specific rule

b) provide arguments that would justify the departure from the general solution. Would such a solution have any impact on the market, business models, risks, etc?

c) specify what conflict of laws solution you recommend

d) specify which issues should be covered by the scope of the applicable law determined by such a conflict of laws rule:

- *the steps necessary to render rights in claims effective against third parties*
- *priority issues*
- *other (please explain)*

We support the law of the assigned claim in relation to voluntary assignment of a claim in the context of an OTC derivative transaction, for example, to provide security in the form of cash collateral.

We understand that an alternative option, for example, the law of the assignor's habitual residence, may have advantages in other financial and commercial sectors, such as in relation to factoring and invoice discounting, but not, we note, in relation to securitisations, for the reasons given by AFME in its response to the Consultation Document, which we have seen in draft. As noted in our response to Question 25, we understand that the preferred approach of the securitisations industry is the law of the assigned claim.

We note that the United Nations Convention on the Assignment of Receivables in International Trade adopted on 12 December 2001 (the "UN Convention") is referred to in the Consultation Document, along with the UNCITRAL Legislative Guide on Secured Transactions (the "UNCITRAL Legislative Guide") and the UNCITRAL Model Law on Secured Transactions (the "UNCITRAL Model Law"). As noted in the Consultation Document, Article 4(2)(b) of the UN Convention excludes assignments of receivables arising under or from financial contracts governed by netting agreements from the scope of the rules set out in the UN Convention in relation to assignment of receivables, with the exception of a receivable owed on the termination of all outstanding transactions. For understandable reasons of institutional continuity and consistency, the UNCITRAL Legislative Guide and the UNCITRAL Model Law both include a similar exclusion of payment rights arising under financial contracts governed by netting agreements, except a receivable owed on the termination of all outstanding transactions.

Without making any adverse comment on the approach taken in the UN Convention, the UNCITRAL Legislative Guide and the UNCITRAL Model Law of carving out from the general exclusion an exception for amounts owed on the termination of all outstanding transactions (i.e., close-out amounts), we wish to make it clear that we believe that, for the sake of clarity, simplicity and enhanced legal certainty, a single conflict of laws rule that points to the law of the assigned claim should apply to all assignments of a financial claim in the OTC derivatives market, whether or not arising under a netting agreement and whether or not constituting a close-out amount.

Question 32

In your experience, does cash collateral play an important role?

- Very important (*please estimate the number or value of transactions concerned per year*)
- Important (*please estimate the number or value of transactions concerned per year*)
- Neutral (*please estimate the number or value of transactions concerned per year*)
- Not important
- I don't know

Cash collateral has always been important in the OTC derivatives market for both cleared and non-cleared transactions. Its importance has been enhanced by the introduction of mandatory margin requirements under EMIR as a result of the WGMR margin requirements agreed at the international level by the BCBS and IOSCO. We understand that the vast majority of financial collateral provided to satisfy variation margin requirements is in the form of cash collateral, and that for various reasons this trend is increasing.

Question 33

Are conflict of laws rules on third party effects of assignment of cash held in accounts easily identified in your Member State?

- Yes, there are statutory rules (*please provide reference and indicate connecting factor*)
- Yes, there is case law (*please provide reference and indicate connecting factor*)
- Yes, there is legal doctrine (*please provide reference and indicate connecting factor*)
- No
- I don't know

As an international trade association, we defer to institutions and firms in each Member State as to the appropriate answer to this question for their Member State.

Question 34

*Would it be useful to provide for a **specific** conflict of laws rule on third party effects of assignment of cash held in accounts which is different from your preferred solution for claims **in general**?*

- Yes
- No
- I don't know

If yes, please:

a) provide arguments that would justify the departure from the general solution. Would such a solution have any impact on the market, business models, risks, etc.?

b) specify what conflict of laws solution you recommend

c) specify which issues should be covered by the scope of the applicable law determined by such a conflict of laws rule:

- *the steps necessary to render rights in claims effective against third parties*
- *priority issues*
- *other: please explain*

See our answer to Question 31.

Question 35

*Do you consider that a specific rule, **different from the above**, is needed for cash collateral being provided:*

a) for the purpose of securing rights and obligations potentially arising in connection with a system designated under the Settlement Finality Directive?

- Yes
- No
- I don't know

b) to central banks of Member States or to the European Central Bank?

- Yes
- No
- I don't know

If yes, please:

a) provide arguments that would justify the departure from the general solution for claims and/or the specific solution for cash held in accounts. Would such a solution have any impact on the market, business models, risks, etc.?

b) specify what conflict of laws rule you recommend

As our principal concern is with the safety and efficiency of the OTC derivatives market, we defer to others in relation to this question.

Question 36

In your experience, are credit claims used as financial collateral outside the Eurosystem credit operations?

- Very frequently (*please estimate the number or value of transactions concerned per year*)

- Frequently (*please estimate the number or value of transactions concerned per year*)
- Sometimes (*please estimate the number or value of transactions concerned per year*)
- Rarely (*please estimate the number or value of transactions concerned per year*)
- Never
- I don't know

We do not have hard empirical data relevant to this question, but anecdotal evidence suggests that credit claims are at least sometimes, if not often, used as financial collateral outside the context of the Eurosystem credit operations.

Question 37

Are conflict of laws rules on third party effects of assignment of credit claims easily identified in your Member State?

- Yes, there are statutory rules (*please provide reference and indicate connecting factor*)
- Yes, there is case law (*please provide reference and indicate connecting factor*)
- Yes, there is legal doctrine (*please provide reference and indicate connecting factor*)
- No
- I don't know

As an international trade association, we defer to institutions and firms in each Member State as to the appropriate answer to this question for their Member State.

Question 38

*Would it be useful to provide for a **specific** conflict of laws rule on third party effects of assignment of credit claims which is different from your preferred solution for claims **in general**?*

- Yes
- No
- I don't know

If yes, please:

a) provide arguments that would justify the departure from the general solution. Would such a solution have any impact on the market, business models, risks, etc.?

b) specify what conflict of laws solution you recommend

c) specify which issues should be covered by the scope of the applicable law determined by such a conflict of laws rule:

- the steps necessary to render rights in claims effective against third parties
- priority issues
- other (*please explain*)

See our answer to Question 31.

Question 39

In your experience, how frequently are claims used as underlying assets in securitisations?

- Very frequently (*please estimate the number or value of transactions concerned per year*)
- Frequently (*please estimate the number or value of transactions concerned per year*)
- Sometimes (*please estimate the number or value of transactions concerned per year*)
- Rarely (*please estimate the number or value of transactions concerned per year*)

- Never
- I don’t know

As this question relates to securitisations, which is not part of our core mission, we defer to market participants active in that area and their respective trade associations. We refer, in particular, to the response prepared by AFME, which we have seen in draft.

Question 40

Are conflict of laws rules on third party effects of assignment of claims used as underlying assets in securitisations easily identified in your Member State?

- Yes, there are statutory rules (*please provide reference and indicate connecting factor*)
- Yes, there is case law (*please provide reference and indicate connecting factor*)
- Yes, there is legal doctrine (*please provide reference and indicate connecting factor*)
- No
- I don't know

See our response to Question 39.

Question 41

*Would it be useful to provide for a **specific** conflict of laws rule on third party effects of assignment of claims used as underlying assets in securitisations which is different from your preferred solution for claims **in general**?*

- - Yes
- - No
- - I don't know

If yes, please:

a) provide arguments that would justify the departure from the general solution. Would such a solution have any impact on the market, business models, risks, etc.?

b) specify what conflict of laws solution you recommend

c) specify which issues should be covered by the scope of the applicable law determined by such a conflict of laws rule:

- *- the steps necessary to render rights in claims effective against third parties*
- *- priority issues*
- *- other (please specify)*

See our response to Question 39.

Question 42

Do you have any other comments on the topic of this public consultation?

No.