



**UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS FOR
THE PREPARATION OF A DRAFT CONVENTION ON
SUBSTANTIVE RULES REGARDING INTERMEDIATED
SECURITIES
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***COMMENTS BY GOVERNMENTS
AND INTERNATIONAL ORGANISATIONS***

(Comments by the Government of Switzerland)

Observations on the scope of application of Articles 5 and 6

In accordance with priority needs of the financial markets as identified by Unidroit in the course of its preparatory work, the Draft Convention deals essentially with the acquisition of and the granting of security interest in intermediated securities.

However, like the Hague Convention on the Law Applicable to Certain Rights in Respect of Securities Held with an Intermediary, the subject-matter of the Draft Unidroit Convention is broader.

- “Securities” are defined in Article 1(a) so as to include “any interest therein”, without limitation to security interests.
- Under Article 1 (h), “disposition... includes a transfer of title... and a grant of a security interest” but does not exclude the creation of another interest in intermediated securities. The non-exclusive nature of this list is underlined in French by the use of the word “notamment”.

In many legal systems, limited interests other than security interests may be created in intermediated securities. It is not a rare occasion in Switzerland that an account holder confers an usufruct upon a beneficiary. An usufruct is a limited interest in some property which entitles the beneficiary to any income deriving from that property. In Swiss practice, an usufruct in intermediated securities is often perfected by way of an agreement between an account holder, an intermediary and a beneficiary. This practice is expressly confirmed by the draft statute on intermediated securities which the Government intends to submit to the Parliament in the near future. On an operational level, such an agreement is similar to a control agreement perfecting a security interest. On a legal level, the interest conferred upon the beneficiary is a limited interest other than a security interest.

Articles 4 and 5 of the Draft Convention provide market participants with internationally recognised methods for making their interests effective against third parties.

Article 4 deals with the acquisition of intermediated securities by way of a credit to a securities account, including the acquisition of any interest in such securities, see Article 1 (a). It can therefore be used to acquire full title, any security interest and any limited interest other than a security interest, including an usufruct.

As now drafted, Article 5 is narrower: it only deals with making security interest in intermediated securities effective against third parties.

Article 6 sets up a system of priority granting any interest made effective in accordance with one of the methods recognised by Article 5 (3) priority over any security interest or other limited interest otherwise perfected in accordance with domestic non-Convention law.

Limiting the application of Article 5 to security interests is neither necessary nor justified. To the extent that the Convention provides several internationally recognised methods to make interests in intermediated securities effective against third parties, there is no reason to restrict its scope to security interests.

In its current drafting, the Convention allows parties to create and perfect an usufruct (or any other limited interest) by way of a credit to a securities account in the name of the beneficiary. However, this is not the most efficient arrangement because it does not allow the grantor of the usufruct (who retains the *nudas proprietas* in the intermediated securities) to exercise any right to substitute intermediated securities of equivalent value.

The Swiss delegation proposes that the scope of Article 5 be extended to limited interests other than security interests so that such limited interests may enjoy the priority rule stated in Article 6.

Such an extension could be achieved through the following amendments:

Article 5

...

4bis. – A Contracting State may declare that under its domestic non-Convention law a limited interest other than a security interest may be created in intermediated securities in accordance with paragraphs 1 to 3.

...

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

...

Article 6

1. – This Article determines priority between security interests and other limited interests in the same intermediated securities.

...

Additionally, the word “interest” should be substituted for “security interest” in paragraphs (2), (3), (5) and (6) of Article 6.