



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

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**Working Group on so called Transparent Systems – Intersessional Work  
Comments of the People's Republic of China representative on the draft Working Paper  
on Transparent Systems**

(submitted by the Government of the People's Republic of China)

1. The Chinese system is quite similar to the Finland system and Colombia systems, and the reports submitted by those two countries basically reflect the current conditions of the China securities holding system. Thus in principle we agree with the proposals of Finland and Colombia. In addition, as an emerging securities market that fully realized dematerialization, China has its own characteristics in terms of holding system and accounts maintenance, etc., which it is suggested that the Convention working group should take into consideration.

**I. Comparison between the China securities holding system and the transparent securities holding system defined by the working group**

**a. Comparison**

2. In accordance with the report and Doc 44, transparent holding systems fall into three categories. In China, SD&C is responsible for clearance, registration, central depository and settlement, and investors are required to open accounts through SD&C or its legal agency. The SD&C directly maintains all investors' accounts according to the results of two-tier settlement (that is, SD&C is entrusted to make entries to the investor specific accounts according to the result of settlement of securities transactions between account operators and investors, which is on the basis of netting procedure between SD&C and participants), so it is clear that the China system generally belong to the first category. Since the SD&C and account operators maintain securities accounts together, the account operators also play an indispensable role in the process of maintaining accounts.

**b. Issue account**

3. Since there is no issue account in China, there is no question relating to issue account at present. However, it is necessary to ensure that the amount of securities originally issued correspond to the amount of securities credited to accounts with SD&C, so it is welcomed if there is improvement in relevant articles of the Convention.

## **2. Comments**

### **a. Intermediary**

4. In Doc57, intermediary is defined as: a person that in the course of a business or other regular activity maintains securities accounts for others or both for others and for its own account and is acting in that capacity.

5. It seems that this provision does not exclude the possibility that the CSD could be regarded as an intermediary.

6. Combining with the relevant provisions of Hague Securities Convention, it will not be inconsistent with the principles of the draft Convention if the CSD is regarded as an intermediary. As the sole securities registration and clearing institution in China, SD&C plays multiple roles in securities transactions in terms of the functions of CSD and CCP. Therefore, SD&C shall be regarded as an intermediary in China.

7. Nevertheless, in China, the SD&C and account operators maintain securities accounts together, and account operators provide services for account holders directly, while the SD&C neither complies with the instructions given by account holders, nor establishes contractual relationship with account holders, so the SD&C is not a contracting party of an account agreement, and there is no direct legal relationship between the SD&C and account holders.

8. Accordingly, as for the circumstance of the SD&C as intermediary, it is suggested that some definitions and relevant articles of the Convention should be amended such as account agreement and designating entry, etc. Moreover, there should be a provision regarding the status and functions of account operators.

9. As to Article 3 which provides the Convention does not apply to the activity of creation, recording or reconciliation of securities conducted by central securities depositories or other persons via the issuer of those securities, this article limits the scope of application of the Convention relating to the CSD. Finland and Colombia suggested that this article should be further improved so as to cover all problems relating to the CSD and clarify that the CSD can be regarded as an intermediary.

10. As both the Finland system and the Colombia system are typical transparent system, their suggestion is representative.

11. Whether the CSD shall be regarded as an intermediary is the key element for countries that adopt transparent holding system to accede to the Convention. Despite of a few differences between the China system and the Finland system and the Colombia system, we agree with the proposals of Finland and Colombia.

### **b. Prohibition of upper-tier attachment**

12. The article 17 provides that attachment shall not be made against the issuer or any intermediary other than the relevant intermediary.

13. In China, since the SD&C is the highest tier, there is little possibility to attach against the issuer or any intermediary other than the relevant intermediary in practice when the SD&C is regarded as an intermediary. So there is no specific problem with respect to this article.

### **c. Shortfall**

14. In China, securities central registration is conducted in the investors' names by the SD&C, so all securities transactions are traceable. The reason of shortfall and those persons who default can be clearly pointed out by means of securities accounts maintained by the SD&C. According to the Property Law, it is impossible to make an investor be liable for others' defaults with his own property, so it is difficult for China to apply the rule of shortfall allocation.

**d. Protection of innocent acquisition**

15. The Article 12 stipulates that a person who does not at the time of acquisition have knowledge of an adverse claim with respect to the intermediated securities is not subject to that adverse claim.

16. In China, it is stipulated that securities accounts are opened in investors' real names, and records held on the register by the SD&C are evidence titles. As a result, the ownership of securities is absolute before transaction and innocent acquisition is seldom in practice, so there is no specific problem with respect to this article.

**e. Enforcement of securities interests**

17. Article 28 says that on the occurrence of an enforcement event, the collateral taker may realize the collateral securities: (a) by selling them and applying the net proceeds of sale; (b) by appropriating the collateral securities as the collateral taker's own property and setting off their value against, or applying their value in or towards the discharge of, the secured obligations, provided that the collateral agreement provides for realization in this manner and specifies the basis on which collateral securities are to be valued for this purpose.

18. In China, in order to protect the pledger, the Guarantee Law stipulates that the pledger and the pledgee may not stipulate in the contract that ownership of the pledged property shall be transferred to the pledgee if the obligation is not discharged at maturity.

19. It becomes more flexible in the draft of the Property Law. However, considering the Property Law is being drafted and has not been passed yet, we suggest that the Convention may allow the contracting countries to reserve the option of the above rules.