



OPINION OF THE EUROPEAN CENTRAL BANK
of 13 November 2014
on book-entry securities
(CON/2014/81)

Introduction and legal basis

On 29 September 2014, the European Central Bank (ECB) received a request from the Slovenian Ministry of Finance for an opinion on a draft law on book-entry securities¹ (hereinafter the ‘draft law’).

The ECB’s competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the fifth indent of Article 2(1) of Council Decision 98/415/EC², as the draft law relates to payment and settlement systems. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the draft law

- 1.1 The draft law is a recast of the current Law on book-entry securities³ and makes certain amendments thereto. It regulates book-entry securities, encumbrances on book-entry securities, transfer of book-entry securities, fulfilment of the obligations arising in respect of book-entry securities, the central register of book-entry securities and access to the data maintained therein⁴.
- 1.2 The draft law has several objectives including the facilitation of a legal framework that will enable the use of TARGET2-Securities (T2S) in Slovenia. The explanatory memorandum outlines that the amendments introduced by the draft law are proposed in the light of the TARGET2-Securities corporate action standards on flows, i.e. pending settlement transactions (hereinafter referred to as the ‘T2S corporate actions standards’)⁵ and the Corporate Actions Joint Working Group⁶ standards for corporate actions on stock, i.e. corporate actions on settled balances (hereinafter referred to as

¹ *Predlog Zakona o nematerializiranih vrednostnih papirjih (ZNVP-1)*.

² Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, 3.7.1998, p. 42).

³ *Zakon o nematerializiranih vrednostnih papirjih (ZNVP)* (Official Journal of the Republic of Slovenia, No. 2/07 – official consolidated text, 67/07 - ZTFI, 58/09 and 78/11).

⁴ See Article 1 of the draft law.

⁵ The T2S corporate actions standards were approved by the T2S Advisory Group. The standards are available on the ECB’s website at www.ecb.europa.eu.

⁶ The CAJWG was set up in summer 2008 as one of the work streams of the ‘CESAME 2’ Group. The CESAME 2 Group followed up on the work of the ‘CESAME Group’ (the European Commission’s Clearing and Settlement Advisory and Monitoring Expert Group) and aimed to achieve the goal of a barrier-free single European market for clearing and settlement of securities transactions. The CAJWG is composed of representatives of the main stakeholders, i.e. issuers, market infrastructures, and intermediaries.

the 'CAJWG standards')⁷. The explanatory memorandum outlines that the Law on book-entry securities currently: (a) governs the execution of a smaller number of corporate actions than are governed by the above standards; (b) does not govern the manner in which obligations arising from a corporate action are fulfilled, as envisaged by the standards; and (c) allows the execution of corporate actions which the standards require to be processed through a central securities depository (CSD), in a manner not laid down by the standards. The draft law aims to address these issues in Articles 38 and 39, as further described below.

- 1.3 A further objective of the draft law is to adapt the Slovenian legal framework to the provisions of Regulation (EU) No 909/2014 of the European Parliament and of the Council⁸ (hereinafter the 'CSDR'). The draft law states that its provisions shall apply to the central register managed by a CSD that has a registered office in Slovenia and to a branch of a CSD of a Member State that is registered in the Slovenian business register. Furthermore, the draft law permits book-entry securities to be entered in the central register where the issuer's obligations are governed by foreign law.

2. General observations

The ECB welcomes the draft law as it contributes to facilitating the Slovenian market's adaptation to T2S and the wider harmonisation of standards in post-trade services.

3. Specific observations

3.1 *Corporate actions*

Pursuant to the draft law, a corporate action on a book-entry security is defined as the fulfilment of the obligations arising from that security⁹. Article 39(1) of the draft law requires corporate actions to be processed through the CSD¹⁰ and through the CSD members that manage book-entry securities holders' accounts (hereinafter the 'CSD members'). Article 39(2) defines particular requirements regarding the fulfilment of the obligations arising from book-entry securities and requires the CSD to further specify and implement the requirements in its rules. Such requirements cover, inter alia, the information flow between the issuer and the CSD, and between the CSD and the CSD members, the key dates relating to a corporate action event, e.g. record date, ex-date, payment date, and other deadlines associated with managing corporate action events. As stated in the explanatory memorandum to the draft law, in defining the requirements in Article 39(2), the draft law takes into account the main principles of the T2S corporate actions standards and the

⁷ As regards the CAJWG standards for corporate actions on stock, see 'Market Standards for Corporate Actions Processing' (Revised version 2012). The report is available on the ECB's website at www.ecb.europa.eu.

⁸ Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (OJ L 257, 28.8.2014, p. 1).

⁹ See Article 38 of the draft law.

¹⁰ The Slovenian CSD is 'KDD - Centralna klirinško depotna družba'.

CAJWG standards¹¹. Moreover, Article 39(2) provides that further specification and implementation by the CSD in its rules of the requirements in Article 39(2), shall be ‘in accordance with internationally accepted standards for processing corporate actions on book-entry securities’. The ECB welcomes the above provisions of the draft law, which will facilitate the implementation of the T2S corporate actions standards and the CAJWG standards in Slovenia, as the explanatory memorandum to the draft law proposes¹².

3.2 *Termination of registry accounts in the central register*

A registry account is defined in the CSD’s rules of operation as a provisional account that is not managed by any member¹³. Historically, the registry accounts held in the central register of book-entry securities were established for the purpose of privatisation. They allowed the distribution of book-entry securities to the shareholders of privatised companies without requiring them to enter into a legal relationship with a member of the CSD. The CSD only maintains the book-entry securities on the registry accounts and does not perform associated services¹⁴. According to the explanatory memorandum to the draft law, this renders registry accounts incompatible with the CAJWG standards and the T2S corporate action standards. To address this issue, the holders of the book-entry securities on registry accounts will have to enter into an appropriate contractual relationship with a member of the CSD. The securities held on registry accounts that are not transferred to other accounts by the deadline laid down in Article 19(2) of the draft law will be transferred in accordance with the CSD’s rules to an account held by a competent court and will be subject to the law governing court deposits. The draft law requires the CSD to lay down in its rules a detailed method for terminating registry accounts.

It follows from the above that the accounts of securities holders who enter into contractual relationships with CSD members to manage their accounts before the deadline are intended to be compatible with the CAJWG standards and the T2S corporate action standards. However, it is not entirely clear how the arrangement regarding the holding of any remaining securities on courts’ accounts will interact with T2S. In particular, it is unclear whether these remaining securities on the courts’ accounts will be tradeable and therefore freely negotiable. An arrangement whereby the courts are holders of book-entry securities accounts in the central register and where such accounts are managed by CSD members as investment service providers suggests, in the light of T2S requirements, that the securities on the courts’ accounts may be considered tradeable. The ECB invites the Slovenian authorities to clarify this arrangement.

11 See Article 39 of the draft law.

12 See, further, the ‘T2S Corporate Actions Standards - 2014 Gap Analysis Report’, which identified that Slovenian law does not recognise the role of the CSD in processing the settlement of corporate actions in accordance with the CAJWG standards and the T2S corporate actions standards. The report is available on the ECB’s website at www.ecb.europa.eu.

13 Article 26(4) of the KDD Operations Rules.

14 See the explanatory memorandum to the draft law.

3.3 *Settlement finality*

- 3.3.1 Article 17 of the draft law provides that the CSD shall define in its rules the moments of entry and of irrevocability of a transfer order.

Article 39 of the CSDR requires that the rules of each securities settlement system that the CSD operates must define those moments in line with Articles 3 and 5 of Directive 98/26/EC of the European parliament and of the Council¹⁵, as amended (hereinafter the ‘SFD Directive’). Furthermore, Article 48(8) of the CSDR requires that interoperable securities settlement systems and CSDs, which use a common settlement infrastructure shall establish identical moments of: (a) entry of transfer orders into the settlement system and (b) irrevocability of transfer orders.

- 3.3.2 Furthermore, the ECB notes that the T2S Advisory Group has undertaken work towards agreement on a common definition of the moment of entry of a transfer order into the settlement system and of the moment at which the transfer order is protected against insolvency in accordance with the SFD Directive (Settlement Finality I), as well as the moment of irrevocability of transfer orders (Settlement Finality II). As part of the intended legal harmonisation of CSD rules within T2S, the CSD rules should also ensure that it is not possible to unilaterally cancel the order after matching has taken place within T2S (Settlement Finality II). Common definitions will need to be applied before migration to T2S in order to ensure compliance with the CSDR and T2S harmonised standards.

3.4 *Foreign law*

The ECB understands that, whilst Slovenian law applies to book-entry securities, to the rights of holders arising from such securities and to the encumbrances on such securities, the draft law permits book-entry securities to be entered in the central register where the issuer’s obligations are governed by a foreign law¹⁶. In situations where the issuer’s obligations are governed by a foreign

¹⁵ Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems (OJ L 166, 11.6.1998, p. 45).

¹⁶ See Article 11 in conjunction with Article 13(2) of the draft law.

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law, the Slovenian law applicable to book-entry securities would apply in other respects, e.g. as regards the rights of holders arising from the securities¹⁷.

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 13 November 2014.

[signed]

The President of the ECB

Mario DRAGHI

¹⁷ Article 13(1) of the draft law.