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## Commentary of Articles 3 & 36

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# **The Federal Intermediated Securities Act (FISA) and the Hague Securities Convention (HSC)**





### Art. 3

#### Intermediated securities

<sup>1</sup> **Intermediated securities within the meaning of this Act are personal or corporate rights of a fungible nature against an issuer which:**

- a. **are credited to a securities account; and**
- b. **may be disposed of by the account holder in accordance with the provisions of this Act.**

<sup>2</sup> **Intermediated securities are effective against the custodian and any third party; they are beyond the reach of other creditors of the custodian.**

#### Bucheffekten

<sup>1</sup> Bucheffekten im Sinne dieses Gesetzes sind vertretbare Forderungs- oder Mitgliedschaftsrechte gegenüber dem Emittenten:

- a. die einem Effektenkonto gutgeschrieben sind; und
- b. über welche die Kontoinhaberinnen und Kontoinhaber nach den Vorschriften dieses Gesetzes verfügen können.

<sup>2</sup> Die Bucheffekte ist der Verwahrungsstelle und jedem Dritten gegenüber wirksam; sie ist dem Zugriff der weiteren Gläubigerinnen und Gläubiger der Verwahrungsstelle entzogen.

#### Titres intermédiés

<sup>1</sup> Les titres intermédiés au sens de la présente loi sont les créances et les droits sociaux fungibles à l'encontre d'un émetteur qui répondent aux conditions suivantes:

- a. ils sont inscrits au crédit d'un compte de titres;
- b. le titulaire du compte peut en disposer selon la présente loi.

<sup>2</sup> Les titres intermédiés sont opposables au dépositaire ainsi qu'à tout tiers; ils sont soustraits à la mainmise des autres créanciers du dépositaire.

#### Titoli contabili

<sup>1</sup> Sono titoli contabili ai sensi della presente legge i diritti fungibili di credito o inerenti alla qualità di membro nei confronti dell'emittente:

- a. accreditati su un conto titoli; e
- b. dei quali i titolari dei conti possono disporre secondo le disposizioni della presente legge.

<sup>2</sup> Il titolo contabile ha effetto nei confronti dell'ente di custodia e di qualsiasi terzo; esso non è accessibile agli altri creditori dell'ente di custodia.

#### Table of contents

	Note	Page
I. Intermediated Securities: The Cornerstone of the FISA .....	1	160
1. A New Legal Category of Assets .....	1	160
2. Terminology and Translation .....	6	162
3. "Intermediated Securities" Distinguished from "Securities" .....	9	162
4. History.....	11	163

II.	Legal Definition of Intermediated Securities Art. 3(1) FISA.....	13	164
1.	Personal or Corporate Rights against an Issuer .....	14	164
2.	Of a Fungible Nature .....	23	166
3.	Credited to a Securities Account .....	27	167
4.	May be Disposed of in Accordance with the Act .....	34	169
5.	No Listing or Trading Required .....	41	170
III.	<i>Erga omnes</i> Effectiveness Art. 3(2) FISA .....	42	171
IV.	Comparison with the Geneva Securities Convention.....	51	173

## I. Intermediated Securities: The Cornerstone of the FISA

### 1. *A New Legal Category of Assets*

<sup>1</sup> As suggested by the title of the Act itself, “intermediated securities” are the core notion of the FISA<sup>1</sup> (see also Prel. Cmts FISA N 30). The choice of a new legal concept and new terms in all three official languages of the Swiss Confederation (*titres intermédies*, *Bucheffekten*, *titoli contabili*) reflects a fundamental policy choice, a “paradigm shift.”<sup>2</sup> Intermediated securities are not merely securities which happen to be held with an intermediary (*intermédies*) and are shown in its ledgers (*Bucheffekten*). Intermediated securities arise out of the immobilization or dematerialization of certain financial assets which from then on are treated as book-entries in special accounts maintained by specialized, regulated financial institutions such as banks and securities dealers.

<sup>2</sup> As a matter of fact and of market practice, intermediated securities are different from the certificated (*papiers-valeurs*, *Wertpapiere*) or uncertificated (*droits-valeurs*, *Wertrechte*) securities out of which they arise in accordance with Art. 6 FISA. Intermediated securities are created when certain financial assets are immobilized in the intermediary system in such a way that they can no longer be held and transferred by investors in accordance with the general provisions of commercial law. Intermediated securities are not held physically by the investor and cannot be physically examined and verified by him. They cannot be delivered by hand from the seller to the buyer. They cannot be pledged by delivering physical possession to the pledgee. They cannot be shown at a general meeting of shareholders as evidence of the right to attend and to vote. There are no coupons which can be detached from intermediated securities to cash in interest or dividend payments. (Whether an investor can opt out of the intermediary system and obtain physical securities in return is dealt with in Arts. 7 and 8 FISA.)

<sup>1</sup> Message, BBl 2006, p. 9344 = FF 2006, p. 8845.

<sup>2</sup> Thévenoz, FS Nobel, *passim*.

Though they are based on a financial instrument which is physically or virtually immobilized and is held through one or more intermediaries, intermediated securities exist only in the form of book-entries in special accounts (securities accounts, see *infra* N 28) maintained by custodians. Holding intermediated securities generally means having them credited to a securities account in the investor's name. Transferring them requires an instruction to the custodian to have them debited from the transferor's account and credited to the transferee's account. They may be pledged in various ways (see Arts. 24–26 FISA), all of which require some action by the custodian. Even physically attending the general meeting of shareholders requires some action by the custodian to provide the shareholder with evidence of his right to vote. In short, the whole intermediary holding system relies on the integrity and efficiency of the custodians. 3

As a matter of law, the drafters of the FISA proposed, and the legislature agreed, that intermediated securities should be legally regulated as a new legal category of assets (*bien juridique, Rechtsgut*), as different from movable property as a copyright or a trademark can be. In Swiss law, as in most other commercial legislation, certificated securities are considered to be movable property, whereas uncertificated securities are mere personal rights. However, neither the existing rules on movable property nor the existing provisions dealing with the assignment of personal rights can properly explain, much less regulate, how intermediated securities are recorded in special accounts, transferred between accounts, or merely charged to the account of the investor. A new form of financial property calls for new rules, which is precisely the purpose and scope of the FISA. 4

Art. 3 FISA defines intermediated securities, Art. 6 FISA regulates their creation, and Art. 8 FISA deals with their extinction. In between, all necessary rules should be provided by the Act itself. When the FISA does not explicitly contain a rule in respect of a particular issue, it must be construed in accordance with general principles of legal interpretation, taking due account of the purposes of the Act and of the market practices which the Act purports to regulate. When legal construction does not provide the answer, filling the gap (*lacune de la loi, Gesetzeslücke*) is the responsibility of the courts in accordance with Art. 1(2) of the Civil Code.<sup>3</sup> No part of the Civil Code or the Code of Obligations should automatically apply to fill in the gap.<sup>4</sup> Any analogy with existing provisions dealing with other types of property, personal or real, including physical or dematerialized securities, calls for the utmost caution, taking into consideration the unique circumstances of the intermediated holding system. 5

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<sup>3</sup> Art. 1(2) CC states: “Where no statutory provision is applicable, the court shall decide according to the existing customary law or, in the absence thereof, according to the rules which it would establish if it had to act as a legislator itself.”

<sup>4</sup> Message, BBl 2006, p. 9342 = FF 2006, p. 8843. See criticisms by *Kunz*, p. 56.

## 2. *Terminology and Translation*

- 6 A new concept requires a new terminology. Any terminological choice is fraught with risks of misunderstanding, false friends, and translation mismatches. It is notable that the French *titres intermédiés* (intermediated securities) does not linguistically match the German *Bucheffekten* (book-entry securities); the Italian *titoli contabili* was a subsequent translation from the German. All are complete neologisms and, interestingly, were not borrowed from any other legal system. Quite the opposite. When in May 2005 the Unidroit project looked for a shorter defined term than the lengthy “securities held with an intermediary” used in the Hague Securities Convention, the Committee of Governmental Experts embraced *titres intermédiés* and “intermediated securities” at the suggestion of the Canadian delegation, that explicitly referred to the 2004 Swiss draft act which had just been published in French and English in the *Uniform Law Review*.<sup>5</sup>
- 7 The French term *titres intermédiés* emphasizes intermediated holding as the proper object of FISA. The German *Bucheffekten* and Italian *titoli contabili* focus on the book (accounting) form in which intermediated securities are created, recorded, and transferred. Though not insignificant, this difference should not be over-emphasized. The working group which produced the 2004 report might have adapted the “intermediated” notion to create the German defined term if *mediatisiert* did not have a variety of connotations (e.g., media, communications) extraneous to the unglamorous world of securities custody and settlement.
- 8 The Swiss constitutional system does not provide for authentic English translations of federal acts. However, because the full title of the 2009 Geneva Securities Convention reads “UNIDROIT Convention on Substantive Rules for Intermediated Securities,” the editors of the present Commentary decided that *intermediated securities* was preferable to *book-entry securities* as the English translation to be used in this commentary.

## 3. *“Intermediated Securities” Distinguished from “Securities”*

- 9 Intermediated securities are distinct from certificated/uncertificated securities, though the former arise from the latter when such securities are immobilized and credits are made into a securities account (see Art. 6 FISA and its commentary *infra*). The Code of Obligations (CO) leans on the German doctrine of *Wertpapiere (papiers-valeurs)* when dealing with certificated securities, which Art. 965 CO defines as “any document in which a right is incorporated in such a way that it cannot be claimed nor transferred to others without the document.”<sup>6</sup>

<sup>5</sup> As an appendix to Thévenoz, *Unif. L. Rev.* 2005, p. 312.

<sup>6</sup> Translated in *Swiss-American Chamber of Commerce*, *Securities law: English translation of the official text*, Zurich 2010, p. 1.

Certificated securities are thus negotiable instruments used to convey personal and corporate rights against their issuers through delivery of the certificate and, where necessary, through endorsement. Uncertificated securities are not movable property: they are merely personal claims and corporate rights which are transferable by way of assignment.<sup>7</sup>

Intermediated securities must be distinguished from securities as defined and used in the Securities Exchange and Securities Trading Act (SESTA) of 24 March 1995.<sup>8</sup> Securities (*valeurs mobilières, Effekten*) are defined in Art. 2(a) SESTA as “standardized certificates which are suitable for mass trading, rights not represented by a certificate with similar functions, and derivatives.” That definition reflects the purpose and sets the scope of the regulation and supervision of exchanges, securities traders, and the securities market. The SESTA definition is broader than the FISA definition,<sup>9</sup> in that the SESTA also applies to non-transferable derivatives created on derivative exchanges such as Eurex. Such derivatives do not qualify as intermediated securities because they are not freely transferable and thus cannot be disposed of in accordance with the provisions of the FISA. There is some dispute as to whether the “suitab[ility] for mass trading” requirement of SESTA is different from the “fungible nature” required by FISA (see N 23 seq. *infra*).<sup>10</sup> Wherever the exact line must be drawn between the SESTA and FISA definitions, they need not and probably cannot be identical. The SESTA definition of “securities” reflects the act’s legal purpose, which is to regulate exchanges, securities dealers, and the securities market in order to ensure the transparency of the market and equal treatment of investors (Art. 1 SESTA); the FISA definition of intermediated securities reflects the custody, clearing, and settlement functions of the same markets.

#### 4. History

The development of the concept of intermediated securities was one the main issues the Technical Working Group appointed by the Department of Finance struggled with. The Draft Securities Deposit Act of 2003 had maintained the traditional distinction between certificated securities held in collective custody, global certificates, and uncertificated securities harmonizing only the method of disposition. Furthermore the Draft Securities Deposit Act was still based on a co-ownership model which was extended to uncertificated securities (see

<sup>7</sup> See however *Brunner*, pp. 215 seq., suggesting that uncertificated securities (*droits-valeurs, Wertrechte*) may be transferred by way of credits to accounts.

<sup>8</sup> *Loi fédérale sur les bourses et le commerce des valeurs mobilières, Bundesgesetz über die Börsen und den Effektenhandel*, RS-SR 954.1.

<sup>9</sup> Message, BBl 2006, p. 9345 = FF 2006, p. 8846.

<sup>10</sup> *Foëx*, Disposition, p. 124; *Hess/Friedrich*, GesKR 2008, p. 105; *Lanz*, p. 195 n. 18; *von der Crone/Bilek*, SZW/RSDA 2008, p. 196.

Art. 7(1), 11(1) WVG). The Working Group decided early on to push further the harmonization.<sup>11</sup> For this purpose a new legal category of asset is superimposed upon these underlyings in order to achieve a full harmonization of the legal framework for all kind of securities held with an intermediary. Furthermore, the Working Group decided not to rely on a co-ownership model as a foundation for the new kind of assets.<sup>12</sup> In the course of the informal consultation process this approach concept found broad support. Comments were submitted inter alia by the Federal Banking Commission (which proposed to delete Art. 4 and move its substance to the provisions dealing with the creation of intermediated securities) and the International Swaps and Derivatives Association.

- 12 In the Working Group's Preliminary Draft, the term “intermediated securities” was defined in Art. 4. Art. 4(1) Draft is largely identical with what is now Art. 3. Art. 4(2) Draft, which dealt with foreign securities serving as an underlying for intermediated securities, was moved to Art. 13(2) FISA. The Federal Council's draft was accepted by the parliament without amendments or changes.

## II. Legal Definition of Intermediated Securities – Art. 3(1) FISA

- 13 Art. 3(1) FISA defines “intermediated securities” as (1) personal or corporate rights against an issuer which (2) are of a fungible nature, (3) have been credited to a securities account, and (4) may be disposed of by the account holder in accordance with the provisions of the Act.

### 1. *Personal or Corporate Rights against an Issuer*

- 14 Unlike the Geneva Securities Convention, the FISA does not define “securities,” which (to use the language of Art. 7(1)) are capable of “serving as a basis for intermediated securities.” Art. 3(1) FISA refers to the rights, personal or corporate, against an issuer which characterize any security in the capital markets and thus any intermediated security.
- 15 “Issuer” (*émetteur, Emittent*) is not a defined term.<sup>13</sup> It must be understood in its usual meaning in the capital markets as the legal entity, of a private or public nature, corporate or otherwise, which issues (i.e., creates) the securities that are subscribed or purchased by investors. The preamble to Art. 3(1) stresses that the substance of intermediated securities does not consist of rights against a custodian, but of rights against an issuer. It must be read alongside Art. 13(1) FISA,

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<sup>11</sup> Report, p. 30.

<sup>12</sup> Report, p. 30.

<sup>13</sup> Likewise in Art. 8(2) SESTA.

which explains that “the creation of intermediated securities does not affect the rights of investors against the issuer.”

Securities, and therefore also intermediated securities, typically comprise a bundle of personal and/or corporate rights against an issuer. A bond issued by a company or a government typically contains a promise to pay interest and to repay the principal amount at maturity; in case of default, it may also include voting rights at a meeting of the bondholders. A share issued by a corporation typically includes a right to payment of declared dividends, anti-dilution rights (such as a preemptive right to subscribe newly issued shares), and voting rights. Securities and intermediated securities are thus complex bundles of rights against an issuer which are determined by the issuer’s articles of association and bylaws as well as by the terms of the issue. 16

Art. 3(1) FISA refers to the rights against issuers contained in intermediated securities, but the FISA does not regulate such rights; they are governed by the applicable corporate law (typically that governing equity instruments) or the applicable contract law (typically that governing debt instruments). 17

One or more personal rights against the issuer – such as a right to receive payment of interests or dividends, a right to the repayment of the principal at maturity, etc. – are almost always contained in intermediated securities. Swiss legal principles define personal rights (*créances, Forderungen*) as rights which an obligor (a creditor in the broadest sense) can enforce only against an obligee (a debtor in the broadest sense). Personal rights are also called relative rights (*droits relatifs, relative Rechte*) because they create mutual obligations among individuals while remaining *res inter alios acta vis-à-vis* third parties. Contractual duties are the epitome of personal rights. Personal rights must be distinguished from property rights (or absolute rights – *droits absolus, absolute Rechte*), i.e., rights (or interests) which are effective against all other parties and can be enforced against any person who infringes upon them without justification. Chattels, real estate and copyright, as well as life and limb, are protected by absolute rights. 18

The reference to personal rights in Art. 3(1) FISA should not be understood as excluding security interests and other rights that may be attached to personal rights against the issuer. Such security interests are ancillary (*accessoires*) to the personal rights which they secure. Legally speaking, therefore, they are transferred and extinguished together with the latter (see Arts. 114(1) and 170(1) CO). While property interests cannot form the core of intermediated securities, there is no reason to exclude from the intermediated holding system bonds and other instruments which are secured or backed by interests in tangible or intangible assets such as mortgage-backed or mortgage-linked securities. This is confirmed by the appendix to the Act modifying Arts. 7 and 8 of the Mortgage Bond Lending Act of 1930 for the specific purpose of facilitating the holding of such interests as intermediated securities. 19

- 20 The personal rights contained in an intermediated security generally are, but do not need to be, monetary claims against an issuer, e.g. for the payment of principal, interest, or dividend. In particular, intermediated securities can include a right of conversion (as in a convertible bond), a preemptive right to subscribe new shares, or a right to the delivery of free shares.
- 21 Corporate rights are typically included in shares and other equity instruments, along with monetary rights (e.g., dividend payment) and other personal rights (e.g., right of preferential subscription of new shares). They include the right to attend in the general meeting of shareholders, to vote, request information, and hold directors to account.
- 22 Intermediated securities may include personal rights, corporate rights, or both. The *oder* of the German version of the Act and the “or” of the English translation are inclusive; the *et* in the French version is not technically correct.

## 2. *Of a Fungible Nature*

- 23 The intermediated holding of investors’ personal and corporate rights against issuers requires the rights in each issue to be fungible (*fongibles, vertretbar*). Only fungible rights can be transferred from one securities account to another in a given quantity (e.g., 100 bearer shares of Swatch Group) or in a given nominal amount (e.g., CHF 250,000 of 3.25% Eidgenossenschaft 07-27). Rights which are not fungible, such as those deriving from a one-customer tailor-made derivative contract, may not be individually assigned unless this is permitted by the relevant contract; they are not suited to the intermediated holding system.
- 24 Fungibility is a concept in the law of obligations that has no statutory definition. It characterizes goods and assets which in normal market practices are referred to in terms of number, measures, or weight.<sup>14</sup> For example, the Code of Obligations refers to fungible goods in respect of loans (Art. 312 CO), bailment (Art. 481 CO), and warehousing contracts (Art. 484 CO), and certificated securities such as warehouse receipts, warrants, and the like (Art. 1152 CO). The key element of fungibility is the reference to market practices: fungible assets are whatever the market treats as such.
- 25 Listed registered shares (and other listed registered securities) are a case in point. Because each share is registered in the name of the shareholder with the issuer itself, or with a registration agent such as SAG SIX Aktienregister AG, and is therefore earmarked as belonging to a particular shareholder, one might question

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<sup>14</sup> *Gomez-Richa/Veuve*, GesKR 1/2010 p. 8.

whether registered shares are fungible.<sup>15</sup> Capital markets nonetheless treat them as such.<sup>16</sup> Most shares listed on SIX Swiss Exchange are registered shares.<sup>17</sup> They are traded in a minimum quantity of one item in anonymous trades where the seller and the buyer do not need to, and in fact cannot, identify each other. While registered shares satisfy the fungibility requirement in Art. 3(1) FISA, their transferability will be further discussed below (see *infra* N 39).

In market parlance, securities which are fungible among themselves are said to be “of the same issue.” Art. 23(1) FISA refers to intermediated securities “of the same kind” but does not further define that notion. Art. 1(j) of the Geneva Securities Convention provides more specifically that

securities are ‘of the same description’ as other securities if they are issued by the same issuer and

(i) they are of the same class of shares or stock; or

(ii) in the case of securities other than shares or stock, they are of the same currency and denomination and are treated as forming part of the same issue.

In this context, “issue,” “kind,” and “description” should be treated as synonyms.

### 3. *Credited to a Securities Account*

As suggested by the German and Italian terms (*Bucheffekten, titoli contabili*), intermediated securities have the form and shape of book-entries in special accounts maintained by custodians. A credit (*bonification, Gutschrift, accredito*) to a securities account is a necessary condition for the creation of intermediated securities, as confirmed in Art. 6(1) FISA. Causing a credit to be entered in a securities account is also one way to dispose of intermediated securities (see Art. 24 FISA).

The term “securities account” (*compte de titres, Effektenkonto*) is not defined in the FISA. Its definition must be inferred from Arts. 3 and 6 FISA (stating that

<sup>15</sup> Registered shares which are not actually registered in the name of the shareholder are labeled as “Dispo” shares. In law, the buyer is not considered as shareholder and has not validly acquired the rights attached to the shares. However, where listed shares are concerned, market practice has ensured that all payments and rights other than voting rights are *de facto* conveyed to “Dispo” shareholders. Only voting rights cannot be exercised while the shares remain “Dispo.” On this issue generally, see *Peter Böckli*, *Schweizer Aktienrecht*, 4<sup>th</sup> ed., Zurich 2009, pp. 617–619 and 698–704; *H.C. von der Crone/M. Isler*, *Dispoaktien*, GesKR 2008 Sondernummer 2008, p. 76. The Swiss parliament is presently considering an amendment to the relevant provisions in the Code of Obligations.

<sup>16</sup> Such market practice does not extend to unlisted registered shares: *Hess/Friedrich*, GesKR 2008, p. 105.

<sup>17</sup> On 22 December 2009, 254 registered shares (domestic and foreign issuers) were listed by SIX Swiss Exchange, as against 82 bearer shares. Source: [www.six-swiss-exchange.com](http://www.six-swiss-exchange.com).

intermediated securities do not exist unless and until they are credited to a securities account); by Arts. 4 and 5(1)(b) FISA (stating that custodians maintain securities accounts in the name of a person or a group of persons); and by Chapter V FISA, which sets out the conditions for the disposal of intermediated securities. Art. 1(c) of the Geneva Securities Convention defines a securities account in obvious terms: “an account maintained by an intermediary [what the FISA calls a custodian] to which securities may be credited or debited.”

- 29 Securities accounts are special accounts maintained for clients, who are referred to as “account holders” (*titulaire de compte, Kontoinhaber*; see Art. 5(b)): these accounts record their holdings of intermediated securities. For each kind of intermediated security (pursuant to Art. 24(1) FISA, see N 26 *supra*), a net balance is shown. Legally speaking, only a credit, i.e., a positive balance (e.g., 100 Nestlé registered shares, CHF 250,000 3.25% Eidgenossenschaft 07-27), can constitute an intermediated security. A negative balance represents an overdraft, i.e., an obligation of the account holder to the custodian to retransfer as many intermediated securities to the custodian as necessary to restore a nil balance. A negative position in respect of one kind of securities is thus not an “intermediated security” as defined in Art. 3 FISA, but a mere obligation in respect of an intermediated security.
- 30 Though they are the only actual record of investors’ property (and of account holders’ holdings), securities accounts are not public registers. They are nonetheless maintained by highly regulated and supervised entities (see Art. 4 FISA) and therefore ought to reliably serve their function of recording credits which are, in law, deemed to be intermediated securities.
- 31 Long before the FISA came into force, Swiss banks were maintaining *comptes de dépôt* and *Depotkonten* to record the financial assets of their clients. As a matter of practice, such accounts also record financial assets other than intermediated securities as defined in the FISA. They may, for example, evidence holdings of gold, precious metals, and commodities, or of tailor-made, non-fungible derivative contracts linked to any kind of assets, including foreign exchange and commodities. The financial industry queried whether the FISA requires custodians to proceed immediately to distinguish securities accounts, recording intermediated securities only, from other accounts recording financial assets which are not and cannot be intermediated securities. Such a distinction would require significant and costly operational and IT changes. The first FAQ submitted by the Swiss Bankers’ Association argues that a securities account pursuant to the FISA need not actually be denominated as a “securities account”; and that it can record other financial assets as well as intermediated securities. The first answer is unobjectionable. The second must be questioned.
- 32 It is correct to say that a securities account need not be formally labeled as *Bucheffektenkonto* or *compte de titres*. It is doubtful, however, that one and the same account may record intermediated securities along with other, entirely different

financial assets. Account holders and custodians need to know which substantive law governs the transfer, disposition, use, lending, borrowing, etc. of particular assets. For example, it is possible to transfer a securitized derivative traded on Scoach in accordance with the FISA; but it is not possible to transfer derivatives created on derivatives exchanges such as Eurex.<sup>18</sup> It is certainly important for the account holder to be able to distinguish what is what. Merging all assets in the same account without any specific identifications is perilous and should be avoided. At the very least, the custodian maintaining the account must be able to tell at any moment whether a particular position in the account represents intermediated securities governed by the FISA, or other assets governed by some other provisions of law.

This question, along with many others, needs to be the subject of prudential regulation by FINMA (the Swiss Financial Markets Supervisory Authority) or the Swiss National Bank in its capacity as regulator of securities settlement systems of systemic importance. It is internationally accepted that the reliability and trustworthiness of intermediated securities, their recording, clearing, and settlement, require regulations in support of commercial law. This is emphasized in the preamble of the Geneva Securities Convention, recognizing that the Convention

does not limit or otherwise affect the powers of Contracting States to regulate, supervise or oversee the holding and disposition of intermediated securities or any other matters expressly covered by the Convention, except in so far as such regulation, supervision or oversight would contravene the provisions of this Convention.

The need to supervise custodians is acknowledged by such private law authorities as *Paul-Henri Steinauer*.<sup>19</sup>

#### 4. *May be Disposed of in Accordance with the Act*

The last requirement for intermediated securities under Art. 3(1)(b) FISA might be confused with a legal consequence of intermediated securities. Both are indeed closely interrelated. No kind of intermediated security can be disposed of in accordance with Arts. 24–26 FISA unless the personal and corporate rights it comprises are freely transferable. It would be unreasonable to expect the intermediated holding system to treat a security as transferable if it was not transferable in the first place.

The transferability requirement is also closely connected with the fungibility requirement discussed above. Something that is not freely transferable can hardly be fungible. Hence many commentators have discussed both requirements to-

<sup>18</sup> See N 9 above and *Gomez-Richa/Veuve*, GesKR 1/2010, p. 20.

<sup>19</sup> *Steinauer*, p. 165.

gether. Art. 1(a) of the Geneva Securities Convention only implies fungibility when it insists that securities must be “capable ... of being acquired and disposed of in accordance with the provisions of this Convention.”

- 36 In general, personal and corporate rights against an issuer cannot be intermediated and disposed of in accordance with the FISA if they are issued on terms that make them unsuitable for such treatment or if they are connected with some obligation of the investor to the issuer.
- 37 Certain personal and corporate rights are not freely transferable under the terms of issue, the articles of association of the issuer, or the applicable law. Such is the case of most shares in partnerships and in certain corporate entities. Likewise, most tailor-made derivatives, and derivatives created on a derivative exchange such as Eurex, are not freely transferable. This may be because e.g. the partner’s position is a highly personal one, or because the investor’s rights under a number of derivatives carry obligations arising, e.g., from margin calls, exercise of options, or maturity of obligations requiring the holder to deliver cash or other assets to the issuer.
- 38 An exception to the general rule is stated in Art. 24(4) FISA, which stipulates that this Article (dealing with disposals by way of a credit) “shall not affect restrictions on the transfer of registered shares. Any other restriction shall be ineffective against the transferee or third parties.” (see also Art. 2(2) FISA).
- 39 As mentioned above (N 25 *supra*), market practices treat listed registered shares as tradable assets although the effects of the sale or other disposal on the acquisition or exercise of certain rights included in the registered shares may be subject to limitations or approval by the board of directors. For that reason, Art. 24(4) FISA may be read as a qualification of the transferability requirement set out in Art. 3(1)(b) FISA, extending the definition of intermediated securities to rights which would not otherwise be deemed capable of being “disposed of in accordance with the Act.”<sup>20</sup>
- 40 For an explanation of the relationships between disposals in accordance with the FISA and restrictions affecting the transfer of registered shares in accordance with Arts. 685 seq. CO; see N 35 seq. to Art. 24.

## 5. *No Listing or Trading Required*

- 41 The definition of intermediated securities in Art. 3 FISA does not require them to be listed on any regulated exchange or traded on any regulated or unregulated market or alternative trading facility.

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<sup>20</sup> *Gomez-Richa/Veuve*, GesKR 1/2010 pp. 9–10.

### III. *Erga omnes* Effectiveness Art. 3(2) FISA

According to Art. 1(2) FISA, the purpose of the FISA is “to ensure the protection of the property rights of investors.” Certificated securities incorporating personal or corporate rights against issuers were created as movable property enabling investors to easily transfer or pledge these rights by transferring or pledging the certificates (see Art. 965 CO). Uncertificated securities, on the other hand, are purely personal rights which are transferred by way of assignment pursuant to Arts. 164 seq. CO, like any other personal right. Over and above the legal implication of Art. 1(2) FISA – that intermediated securities must be some form of investor’s property rights if they are to be protected by the Act – the FISA contains other provisions which give intermediated securities a very different status from mere personal rights. 42

The key provision here is Art. 3(2) FISA, which includes two statements. Intermediated securities are “effective [*opposables, wirksam*] against the custodian and any third party,” i.e., *erga omnes*. Indeed, they are “beyond the reach of other creditors of the custodian, a principle that is implemented by Art. 17 FISA. It should be noted that Art. 3(2) FISA mentions this *erga omnes* effectiveness but not the enforcement of the rights against the issuer. This is the province of Art. 13(2) FISA, which stipulates that “unless otherwise provided by this Act, account holders may exercise their rights only through their custodian.” As already noted, investors must often rely on their custodian to obtain payment of coupons or the principal of intermediated bonds, or to obtain the documents necessary for admittance to the general meeting and access to the votes conferred by their intermediated shares. 43

*Erga omnes* effectiveness – both generally and in the insolvency of a custodian – is a fundamental feature of property rights. That is not as surprising as one might think. Intermediated securities are personal or corporate rights against the issuer, not against the custodian (unless the custodian is the issuer). It is perfectly logical that a custodian’s bankruptcy should not affect the rights of account holders against issuers. 44

A further characteristic of property rights is that their owners have the right and the power to trace and follow them in the hands of any third party (*droit de suite, Folgerecht*) unless the latter acquired them properly or is protected as a *bona fide* purchaser (Art. 29 FISA). Movable and immovable property may be recovered (*revendication, Vindikation*, Arts. 641 and 973 CC) from any unprotected holder. The right to trace and follow movable and immovable property is based on the claim that “this thing is mine”: *ubi rem meam invenio, ibi eam vindico*. The principle hardly applies to fungible property, however. For example, if 10 kg of my apples have been mixed with apples of the same kind belonging to my neighbor, I cannot claim back my apples specifically – only a share in the mixed pool of apples and the delivery of an equivalent quantity. Whether it is a proprietary or a personal claim may depend on a number of things. For apples mixed in a fungible 45

pool, Swiss law grants a proprietary remedy (Art. 727 CC), whereas it only grants a personal remedy if cash belonging to A has been purportedly or inadvertently mixed with B's cash.<sup>21</sup> A cannot claim back her property under Art. 641 CC but must claim payment of an equivalent sum on the basis of unjust enrichment, a personal claim exposed to the risk of B's insolvency.

- 46 For intermediated securities, the Act takes a middle way. If B has acquired intermediated securities improperly from A, or is not a *bona fide* purchaser, Art. 29(2) FISA gives A a claim against B for restitution of the securities "in the same quantity and of the same kind pursuant to the rules of the Code of Obligations on unjust enrichment." Unlike cash, however, Art. 29(3) FISA reinforces that personal claim by providing some degree of protection if B becomes bankrupt or subject to other liquidation proceedings. To the extent that B actually holds intermediated securities of the relevant kind, A can insist that they be excluded from B's estate and delivered to him in preference to other creditors of B.
- 47 As *Denis Piotet* has noted, intermediated securities have two more features that are characteristic of property rights as opposed to personal rights.<sup>22</sup> Art. 29 FISA protects a *bona fide* acquirer for value even if the transferor had no power or authority, or the credit to the transferor's securities account has been subsequently reversed. Art. 30 FISA sets out *prior tempore potior iure* priorities among several dispositions of the same intermediated securities.
- 48 In sum, intermediated securities include very distinctive features which assimilate them to property rights. They are effective against third parties (even though they can only be enforced against the issuer, generally through and with the help and support of the custodian). Intermediated securities remain effective in the insolvency of the custodian: they cannot be accessed by the custodian's other creditors. And if they have gone astray, intermediated securities can be recovered from their current holder by way of a personal claim enhanced by some degree of insolvency protection.
- 49 Legal authors have unequivocally endorsed the notion that intermediated securities form a new legal category of assets subject to their own rules.<sup>23</sup> Insofar as a dispute remains, it touches on the legal characterization of intermediated securities. Piotet doubts that they can be considered as a particular form of property rights.<sup>24</sup> *Steinauer* rightly notes that intermediated securities have mixed features but are generally more akin to proprietary rights than to personal rights.<sup>25</sup> This last observation confirms the distinctiveness of the new legal concept of intermediated securities, which cannot be identified either as personal rights or as

<sup>21</sup> ATF/BGE 47 II 267 (1921), Confédération suisse c. Etat du Valais.

<sup>22</sup> *Piotet*, p. 108.

<sup>23</sup> See e.g. *Föëx*, Gage, p. 144; *Eigenmann*, SZW/RSDA 2006, pp. 107 seq.; *Kuhn*, Bucheffektenmodell, pp. 44–46; *Kunz*, p. 47; *Piotet*, p. 107; *Steinauer*, p. 153; *Thévenoz*, FS Nobel, p. 704.

<sup>24</sup> *Piotet*, pp. 107–113.

<sup>25</sup> *Steinauer*, pp. 155–157.

movable property. Intermediated securities are distinct and their features have been legally defined on the basis of actual market practices.

Whatever the exact nuance, intermediated securities are legally effective against third parties under Art. 3(2) FISA. This implies that any misappropriation or unauthorized infringement constitutes a tort pursuant to Art. 41(1) CO, as in the case of any other unjustified infringement of absolute rights.<sup>26</sup> 50

#### IV. Comparison with the Geneva Securities Convention

Unlike the FISA, Art. 1 of the Geneva Securities Convention has separate definitions for “securities” and “intermediated securities.” Art. 1(a) of the Convention defines securities as 51

any shares, bonds or other financial instruments or financial assets (other than cash) which are capable of being credited to a securities account and of being acquired and disposed of in accordance with the provisions of this Convention.

As explained in section 1–5 of the Draft Official Commentary,<sup>27</sup> the enumeration of shares, bonds, etc., is not limitative. It “allows for the evolution of market practice and the creation of new types of securities capable of being held in the intermediated holding system.” The double test in this definition is essentially similar to Art. 3(1)(a) and (b) FISA. The Convention does not explicitly require securities to be fungible, but that requirement is probably implied.<sup>28</sup>

Art. 3 FISA is, if anything, more restrictive than the definitions in Arts. 1(a) and (b) of the Convention. It follows that intermediated securities within the meaning of in the FISA also qualify as intermediated securities within the meaning of the Convention.<sup>29</sup> 52

First, Art. 1(b) of the Convention defines intermediated securities not only as “securities credited to a securities account” but also as “rights or interests in securities resulting from the credit of securities to a securities account.” In other words, in a pledge transaction executed in accordance with Art. 24 FISA and Art. 11 of the Convention, a credit to the securities account of the pledgee can properly be described as an intermediated security under the Convention even if it merely confers a limited interest on the account holder. While the definition of 53

<sup>26</sup> ATF/BGE 112 II 118, at 5.e): “L’illicéité est [...] réalisée, en tout cas, lorsque l’acte incriminé porte atteinte à un bien protégé par un droit absolu, tel que la vie, l’intégrité corporelle ou la propriété. L’ordre juridique protège directement ces droits, sans qu’il soit nécessaire de rechercher dans chaque cas si l’auteur du dommage a violé une injonction déterminée.”

<sup>27</sup> Draft Official Commentary on the draft Convention on Substantive Rules regarding Intermediated Securities, 3 July 2009, UNIDROIT CONF. 11/2 – Doc. 5.

<sup>28</sup> See the Draft Official Commentary, at 1–16.

<sup>29</sup> On the notion of intermediated securities in the Convention, see *Thévenoz*, 13 *Stanford J. L. Bus. & Fin.*, pp. 420–432.

intermediated securities in Art. 3 FISA does not expressly extend to such a credit, there should be no substantive difference between the treatment of that credit under the FISA and under the Convention. In particular, as with any (other) intermediated securities, the pledge account holder can charge his interest in accordance with Art. 25 FISA, or further transfer it in accordance with Art. 24 FISA.

- 54 Second, Art. 9 of the Convention, “Intermediated securities,” describes the rights that “the credit of securities to a securities account confers on the account holder.” Art. 9(1)(a) refers to “any rights attached to the securities,”<sup>30</sup> which Art. 3(1) FISA describes as “personal or corporate rights against the issuer.” Art. 9(1), however, extends the list of the rights conferred by a credit to include the right to effect a disposition, the right to cause the intermediated securities to be held otherwise than through a securities account, and any such other rights as may be conferred by non-Convention law, i.e., the domestic law designated by the applicable rules of conflict.
- 55 In short, whereas the FISA treats intermediated securities as rights against the issuer only, the Convention extends the notion to some other rights against the custodian. Nevertheless this difference is a matter of legal approach rather than of substance. Neither the FISA nor the Convention purports to regulate or modify the rights against the issuer, i.e., the rights attached to the securities.<sup>31</sup> Both deal with how intermediated securities are created, transferred, charged, realized, and extinguished. They form the substantive law governing the proprietary aspects of intermediated securities, and thus fall within the scope of the applicable law as designated by Art. 2 of the Hague Securities Convention.

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<sup>30</sup> The words “rights attached to the securities” are reminiscent of the traditional distinction in Swiss and German laws relating to *Wertpapiere* (*papiers-valeurs*) between *Rechte aus dem Papier* and *Rechte am Papier*.

<sup>31</sup> *Bahar*, at 1-a-ii, rightly remarks that the distinction has its limitations, with corporate restrictions on share transfer being a borderline case.



## Art. 36

<b>Referendum and effective date</b>	<sup>1</sup> <b>The Act shall be subject to an optional referendum.</b> <sup>2</sup> <b>The Federal Council shall set the effective date.</b>
Referendum und Inkrafttreten	<sup>1</sup> Dieses Gesetz untersteht dem fakultativen Referendum. <sup>2</sup> Der Bundesrat bestimmt das Inkrafttreten.
Référendum et entrée en vigueur	<sup>1</sup> La présente loi est sujette au référendum. <sup>2</sup> Le Conseil fédéral fixe la date de l'entrée en vigueur.
Referendum ed entrata in vigore	<sup>1</sup> La presente legge sottostà a referendum facoltativo. <sup>2</sup> Il Consiglio federale ne determina l'entrata in vigore.

- 1 Art. 36 is modelled after the standard clause concluding most statutes passed by the Parliament.
- 2 The Federal Intermediated Securities Act was enacted by both houses of Parliament on 3 October 2008. Under the Federal Constitution, a petition signed by 50'000 citizens within a period of three months might have called for a referendum to be held in respect of this statute.<sup>1</sup> No such petition was circulated as the Act was politically uncontroversial and its highly technical nature would anyhow have made such a referendum highly unlikely.
- 3 Under Art. 36(2), the Government had the authority to determine the effective date. It deferred to requests by the financial services industry and delayed the implementation of the Act by about one year to allow enough time for the adaptation of contracts and operational arrangements. On 6 May 2009, the Federal Council formally decided to promulgate the Act with effectiveness as of 1 January 2010. The Act was published on 21 July 2009 in the *Official Collection of Federal Legislation*.<sup>2</sup>
- 4 The promulgation of the Act included amendments of existing laws listed in the Annex. The following amendments have become effective as of 1 January 2010:

<sup>1</sup> See *Bundesblatt* (BBl) 2008, p. 8321 = *Feuille fédérale* (FF) 2008, p. 7561.

<sup>2</sup> *Amtliche Sammlung des Bundesrechts* (AS)/*Recueil officiel des lois fédérales* (RO) 2009, pp. 3577 and 3593.

- a) Art. 901(3) of the Civil Code (of 10 December 1907);<sup>3</sup>
- b) Arts. 7 and 8 of the Mortgage Bond Lending Act (of 25 June 1930);<sup>4</sup>
- c) Arts. 622(1) and 627(14) of the Code of Obligations (of 30 March 1911);<sup>5</sup>
- d) Arts. 973a to 973c of the same Code, which are commented in the last part of this commentary;
- e) Art. 287(3) of the Debt Enforcement and Bankruptcy Act (of 11 April 1889);<sup>6</sup>
- f) Art. 17 (deleted) and Art. 37d of the Banking Act (of 8 November 1934).<sup>7</sup>

The Annex also includes the addition of a new paragraph (2<sup>bis</sup>) to Art. 470 of the Code of Obligations. Art. 470(2<sup>bis</sup>) CO entered into force on 1 October 2009, three months before the rest of the FISA.<sup>8</sup> Such anticipated effectiveness was necessary for Switzerland to comply with the EU Payment Services Directive (PSD)<sup>9</sup> as a prerequisite for the participation in the Single European Payment Area. Art. 470(2<sup>bis</sup>) CO implements Art. 66 PSD (see *supra* Cmt. Art. 15 N 39 seq.).

The Federal Intermediated Securities Act may be modified by later legislation. A current, consolidated version in German, French and Italian is available online at any time from the *Systematic Collection of Federal Legislation*.<sup>10</sup>

<sup>3</sup> A current, consolidated version of this statute in German, French and Italian is available in the *Systematic Collection of the Federal Legislation* (RS) at <http://www.admin.ch/ch/d/sr/sr.html> under RS 210.

<sup>4</sup> *Ibid.*, under RS 957.1.

<sup>5</sup> *Ibid.*, under RS 220.

<sup>6</sup> *Ibid.*, under RS 281.1.

<sup>7</sup> *Ibid.*, under RS 957.1.

<sup>8</sup> *Amtliche Sammlung des Bundesrechts/Recueil officiel des lois fédérales* 2009 (RO), pp. 3577 and 3593.

<sup>9</sup> Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market, Official Journal L 319, 05/12/2007 pp. 1–36.

<sup>10</sup> [http://www.admin.ch/ch/f/rs/c957\\_1.html](http://www.admin.ch/ch/f/rs/c957_1.html).