

II

(Preparatory Acts)

ECONOMIC AND SOCIAL COMMITTEE

Opinion of the Economic and Social Committee on the 'Proposal for a European Parliament and Council Directive on Settlement Finality and Collateral Security'

(97/C 56/01)

On 21 June 1996, the Council decided to consult the Economic and Social Committee, under Article 100a of the Treaty establishing the European Community on the above-mentioned proposal.

The Section for Economic, Financial and Monetary Questions, which was responsible for preparing the Committee's work on the subject, adopted its Opinion on 16 October 1996. The Rapporteur was Mr Donovan.

At its 339th Plenary Session (meeting of 31 October 1996), the Economic and Social Committee adopted unanimously the following Opinion.

1. Payments (national and above all international) are increasing steadily, driven by technological innovation. Netting systems have been established. The increase in the amounts exchanged between financial institutions and the rapidity of these exchanges involve increased risk. What is to be done in the event of the insolvency or bankruptcy of one of the participants? When is a payment final? To what extent is collateral security provided in connection with participation, e.g., as guarantee for default/loss-sharing, in payment systems, in particular netting system, affected in the event of insolvency proceedings against the provider of the security?

2. The complexity of these payment systems, the amounts transferred and the lack of transparency in netting systems with regard to the indebtedness of a given participant at a given moment are such that a Report to the Governors of the Central Banks of the Group of Ten Countries (BIS) [the Lamfalussy Report⁽¹⁾] goes so far as to speak of 'systemic risk', a domino effect involving a cascade of insolvency's culminating in

financial market collapse, if obligations had to be converted from net to gross.

3. The purpose of the proposal for a Directive is to reduce these risks to a minimum by harmonizing the laws of the Member States so as to provide for:

- the legal validity of netting agreements and their enforceability against any creditor in the event of insolvency;
- the enforceability of collateral security provided in connection with participation in payment systems;
- the enforceability of collateral provided for monetary policy purposes, and so contribute to developing the necessary legal framework for the monetary policy of the future European Central Bank.

3.1. The Directive is also intended to facilitate the integration of the banking networks of the Member States and prepare for the third stage of EMU. Moreover, the removal of impediments to internal market payments, thus making cross-border payment arrangements more efficient and cost-effective.

⁽¹⁾ Report of the Committee on inter-bank schemes of the Central Banks of the Group of Ten Countries, BIS, Basle, November 1990.

4. It should be pointed out that this is a draft Directive. The Commission is not seeking uniform legislation, but rather the attainment of certain objectives, i.e.:

- the legal validity of payment netting must be recognized in all jurisdictions concerned and its effects must be binding on third parties;
- any payment order made in accordance with the rules of the system must be irrevocable;
- any insolvency proceedings must not have a retroactive effect on the rights and obligations of participants in the netting systems. The insolvency law applicable to the rights and obligations in connection with direct participation in a payment system in the event of insolvency proceedings against a participant in that payment system must be clearly determined;
- collateral security must be insulated from the effects of the insolvency law of the Member State of a failed participant.

5. The Economic and Social Committee welcomes this proposal in view of its importance for the functioning of the internal market, with a view to preparations for the third stage of EMU, but also and above all because of the importance of an EU payments system for economic stability and thus employment.

6. The Committee proposes the following amendments to the text of the proposal for a Directive:

6.1. Given that payment systems and securities settlement systems are often linked it is inadvisable to provide for enforceable netting, avoidance of retroactive effects and finality, in payment systems, and not provide similar protection for securities settlement systems.

The application of the Directive should therefore be amended where necessary to include securities settlement systems, in particular in relation to the zero-hour rule, retroactive provisions and irrevocability/finality.

6.2. In Article 1, amend the text to read 'any currency, the ecu and the euro'.

6.3. In Article 2(a), sub-participants should also be covered, otherwise there will be a 'gap' in the protection against systemic consequences by the non-inclusion of relationships such as those in correspondent banking arrangements and sub-participant, i.e., so-called 'indirect', membership/participation in payment systems.

6.4. Article 2(b) can be deleted as a consequence of the above-proposed change to Article 2(a).

6.5. In Article 2(1), the definition of 'collateral security' should include all the various legal techniques used, in practice in connection with the operation of payment and settlement systems.

6.6. In Articles 3 to 7, delete the words 'direct' and 'directly', which are no longer necessary as a consequence of the above-proposed change to Article 2(a).

6.7. In relation to Articles 5, 6 and 7, a branch, located in the European Union, of a credit institution from a non-EU country is a credit institution within the meaning of Community law. The Commission should take the necessary steps to ensure that Articles 5 and 6 should apply to such branches, having regard to the insolvency law of a non-EU country in which the credit institution is based.

6.7.1. With the increasing internationalization of economies, credit institutions from non-EU countries with no branch in the Community ought to be able to participate in Community payment and securities settlement systems on the basis of conventions governing the application of Articles 5, 6 and 7.

6.8. In Article 7, the text should be revised to reflect the drafting changes proposed above in relation to the definition of collateral security in Article 2(1). The use of terms relating to 'pledging' of securities does not reflect the wide range of legal techniques used in providing collateral security.

7. The Committee would ask the Commission to consider in the framework of international institutions how to avoid systemic risks worldwide.

Brussels, 31 October 1996.

*The President
of the Economic and Social Committee*

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