

Recommendations 2000

ISSA

INTERNATIONAL
SECURITIES
SERVICES
ASSOCIATION

Status Report 2001 Market Key Issues Schedule

The issues are sorted first by recommendation,
then by compliance question (topic addressed),
then by country

Important note:

This is a working and evolving document, forming an integral element of the Recommendations 2000 initiative. This list cannot claim to be complete, and some of the issues raised may be controversial, or may be viewed differently by the respective local markets. It represents, however, the perception of a significant group of cross-border market participants. Additions, clarifications, suggestions or comments are welcome and encouraged and will, where appropriate, be reflected in the document.

April 2002

Recommendation 1: Governance

Securities Systems have a primary responsibility to their users and other stakeholders. They must provide effective low cost processing. Services should be priced equitably.

Questions:

- 1.1 Is the board that governs the depository answerable to its users?
- 1.2 Does any single organisation, or sector (e.g. brokers, custodians, Stock Exchange) have a large voting position at the board of the depository?
- 1.3 Is there cross subsidisation of products (e.g. international services subsidised by local ones or transaction costs subsidised by asset servicing charges)?
- 1.4 What process is in place at the depository to ensure that it meets the needs of all its stakeholders (e.g. institutions, broker dealers, retail investors, issuers)?
- 1.5 What is the communications strategy of the depository to its stakeholders and how is this run?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
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No issues identified.

Recommendation 2: Technology - Core Processing

Securities Systems must allow the option of network access on an interactive basis. They should cope with peak capacity without any service degradation, and have sufficient standby capabilities to recover operations in a reasonably short period within each processing day.

Questions:

- 2.1 How often, over the last twelve months, has the depository been required to:
 - Change its published settlement timetable?
 - Extend the time of opening for settlement input by users?
 - Delay start of day processing?
- 2.2 Does the depository operate real time or multiple batch processing for settlement?
- 2.3 Does the depository allow interactive communication (on line real time) with its users, enabling settlement input and amendment?
- 2.4 Has the depository ever failed to recover an outage within the day or failed to start processing runs for a whole day, and, if so, when did that failure arise and what steps have been taken to prevent a similar event in the future?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
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No issues identified.

Recommendation 3: Technology - Messaging and Standards

The industry worldwide must satisfy the need for efficient, fast settlement by full adherence to the International Securities Numbering process (ISO 6166) and uniform usage of ISO 15022 standards for all securities messages. The industry should seek to introduce a global client and counterpart identification methodology (BIC - ISO 9362) to further facilitate straight through processing. Applications and programmes should be structured in such a way as to facilitate open interaction between all parties.

Questions:

- 3.1 Does the market use ISIN as the primary securities identification code?
- 3.2 Are the major participants in the market linked electronically?
- 3.3 Does the depository communicate using true (i.e. not bilaterally agreed on sub-standards) ISO standards for securities messaging?
- 3.4 Does the market operate standard identification codes for counterparties or client accounts and, if so, how do (or could) these fit into a single global identification methodology?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Canada	<p>Compatible electronic messaging standards</p> <p>The technology in the messaging and processing environment leads to several instances requiring manual intervention as well as processing errors. Currently, it is estimated that over 60% of messages are sent via telephone, fax or mail, and these require manual re-keying by the recipient. In addition, internal systems developed by market participants are usually not compatible in terms of their ability to pass electronic messages from one participant to another, and therefore generates the need for re-keying.</p> <p>Many of the current systems in the industry process messages in batch, rather than in real-time. This processing lag adds to the inefficiencies and lack of timeliness.</p> <p><i>Reference: Rec. 3, Q 2 and 3</i></p>	It is hoped that the introduction of System X at the central depository in 2002 will induce market participants to revamp their systems to achieve real-time functionality and STP.	CSD
Chile	<p>ISIN</p> <p>Chile's securities settlement system does not utilise ISIN coding.</p> <p><i>Reference: Rec. 3, Q 1</i></p>	ISIN's are expected to be introduced by the end of 2002.	CSD

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Colombia	<p>ISIN</p> <p>The adoption of ISIN codes would be beneficial to facilitate the identification of Colombian securities.</p> <p><i>Reference: Rec. 3, Q 1</i></p>	Adopt and promote use of ISIN.	Exchange, CSD
Denmark	<p>Use of BIC codes for counterparty identification</p> <p>The market operates with local standard identification codes for counterparty information: BIC codes are not accepted. The majority of foreign clients use standard SWIFT formatting which includes BIC codes. There is practically no STP in the market.</p> <p><i>Reference: Rec. 3, Q 3</i></p>	<p>Market to move to standard SWIFT message formatting.</p> <p>The Danish Securities Center (VP) introduced the BIC code as a new match criterion. From February 2002 it is used for settlement of certain types of transactions (client to client transactions) and will become mandatory from May 2002. This change does not apply to trades between counterparties which are members of VP which still need to use CD-IDENT (Central Depository code) as matching criterion for trade settlement.</p>	CSD
Russia	<p>ISO standards not widely in use</p> <p>Not all equity issues have ISIN codes allocated. The two depositories NDC and DCC do not use ISO standards for securities messaging, nor for counterparty identification.</p> <p><i>Reference: Rec. 3, Q 1, 3, 4</i></p>	Adopt ISO standards to the extent possible.	CSD, Exchange

Recommendation 4: Uniform Market Practices

Each market must have clear rules assuring investor protection by safeguarding participants from the financial risks of failed settlement and ensuring that listed companies are required to follow sound policies on corporate governance, transfer of economic benefits and shareholder rights.

Questions:

- 4.1 Does the depository or the market have securities lending and borrowing schemes in place, and are these open to all market participants and their settlement agents?
- 4.2 Does the settlement system mark fail trades to market and collect margin from the failing counterparty to protect the innocent counterparty's interest?
- 4.3 Does the market operate a guarantee fund or have an equivalent procedure to protect against the cost of failed transactions; and which sectors of the market does it cover?
- 4.4 Are the stock transfer agents (share registrars) linked electronically to the depository?
- 4.5 Is there a legal maximum time period to complete ownership transfers in the books of the issuer? If so, does market practice adhere to the deadline?
- 4.6 Are investors entitled to all benefits arising on a security from the point of purchase; and how are any rules enforced?
- 4.7 Is proxy voting permissible in the market? and can such proxies be lodged by post or other remote delivery method?
- 4.8 Are there binding rules in the market stating the minimum and maximum lapsed time between the announcement and completion of key events, including registration, the calling of shareholder meetings, the payment of dividends or interest, rights issues, tender offers and other voluntary corporate actions?
- 4.9 Are all voluntary corporate actions advised through a central mechanism assuring consistent information to all investors?
- 4.10 Is information on corporate actions available electronically, and is the minimum lapsed time for responding to such actions sufficient to enable all domestic and foreign investors to respond in a timely and considered fashion?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Australia	<p>Lack of automated borrowing to bridge failed trades <i>Reference: Rec. 4, Q 1</i></p>	<p>All three clearing systems, should examine possibilities of setting up a securities lending and borrowing scheme, in agreement with market participants automatically covering failed transactions caused by lack of securities positions.</p> <p>Further, Austraclear and RITS should service their clients by collecting amounts due from counterparties that fail to deliver securities on the contractual value date.</p>	<p>CHESS, RITS, Austraclear</p>
Finland	<p>Tax barriers to securities lending On-shore securities lending is not practised due to lack of clarity surrounding domestic transfer tax liabilities. <i>Reference: Rec. 4, Q 1</i></p>	<p>Clarify rules and regulations</p>	<p>Regulator</p>
New Zealand	<p>Tax barriers to securities lending Although securities lending and borrowing is permitted it is prohibitive due to tax considerations. <i>Reference: Rec. 4, Q 1</i></p>	<p>A relaxation of the tax constraints would be required in order to encourage on shore securities lending.</p> <p>The New Zealand Stock Exchange is in the process of drafting a paper for the Inland Revenue Department, in regard to lending.</p>	<p>New Zealand Inland Revenue New Zealand Securities Commission New Zealand Stock Exchange</p>
Philippines	<p>Tax barriers to securities lending Regulations on securities borrowing and lending and short selling not clearly defined (e.g. the reluctance of the Bureau of Internal Revenue (BIR) to approve the relevant tax exemption and the BSRD requirement for subsequent repatriation, which limits further development of onshore securities borrowing and lending. <i>Reference: Rec. 4, Q 1</i></p>	<p>Clarify / create clear rules on securities lending and borrowing. This is now being addressed.</p>	<p>Regulators</p>

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Portugal	<p>Short selling definition Need for clarification on whether or not short selling, as is widely understood in international markets - selling with no cover at all, is allowed by the Securities Code of 2000.</p> <p>The Portuguese Brokers Association (APC) and the market commission (CMVM) have recently concluded that the pertinent issue with regards to short selling is that the Financial Intermediary retains the responsibility of presenting the negotiated securities at the time of settlement. A conclusion can be drawn that it is therefore not mandatory to have arranged for a loan/borrow prior to selling short as long as the Financial Intermediary is able to present the negotiated securities at the time of settlement.</p> <p><i>Reference: Rec. 4, Q 1</i></p>	Provide clarification	Regulators
Taiwan	<p>Restriction on use of securities lending programs Securities lending, while permitted in the market, is illegal for foreign institutional investors.</p> <p><i>Reference: Rec. 4, Q 1 and Rec. 7, Q 2</i></p>	Create equal conditions for foreign market participants	Regulators
Austria	<p>Lack of market guarantee fund No guarantee fund to support exchange trading.</p> <p><i>Reference: Rec. 4, Q 3</i></p>	Consider implementation of a central counterparty, or other trade guarantee solution	Exchange
Denmark	<p>Lack of market guarantee fund In the case of broker/counterparty liquidation there is no market guarantee fund. Trades are final and irrevocable and will continue to settle until either stock or cash runs out when all outstanding trades are frozen. In this situation, pending trades will have to be taken to claims court. This is counterparty risk.</p> <p><i>Reference: Rec. 4, Q 3</i></p>	Develop guarantee fund which would cover market trades in this situation.	CSD and market regulators
Finland	<p>Lack of market guarantee fund</p> <p><i>Reference: Rec. 4, Q 3</i></p>	Consider implementation of a central counterparty, or other trade guarantee solution	Exchange
Spain	<p>Scope of guarantee fund The SCLV maintains a guarantee fund, which covers direct depository participants in case of default. A fund is not maintained by the Bank of Spain (BOS).</p> <p><i>Reference: Rec. 4, Q 3</i></p>	A merger of the two entities is currently under way, the SCLV and the BOS need to establish a guarantee fund to cover all market participants and transaction types.	SCLV, BOS and the C.N.M.V.

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Turkey	<p>Handling of physical securities, reregistration</p> <p>Equities have yet to be dematerialised, though the subject continues to be discussed together with that of the establishment of a central registrar.</p> <p><i>Reference: Rec. 4, Q 4 and Rec. 5 Q 5</i></p>	Dematerialise securities and establish a central registrar	Regulators
Pakistan	<p>Handling of physical securities, reregistration</p> <p>The registration process typically takes 15 or more days. For shares deposited into the central depository, only the registrar can validate the authenticity of certificates before shares are reregistered into the CDC nominee name.</p> <p>If purchases settle just before ex-date and shares cannot be reregistered before the ex-date, the purchasers could lose corporate action entitlement and have to claim the seller.</p> <p><i>Reference: Rec. 4, Q 4, 5, and 6</i></p>	Expedite reregistration, improve investors' protection for entitlements.	CSD, Regulators
Spain	<p>Handling of physical securities, reregistration</p> <p>The registration process for equities is cumbersome in Spain, as RR (registered reference) numbers must be tracked closely to substantiate adherence to the regulations prohibiting short-selling. Registration rests upon the local broker. Local custodians have little or no control over the accuracy of the process, which leaves investors exposed.</p> <p><i>Reference: Rec. 4, Q 4, 5, and 6</i></p>	Simplify registration process.	Regulators
Russia	<p>Handling of physical securities, reregistration</p> <p>Securities may not be immediately negotiable due to extended registration or validation periods. Registration periods vary from two to thirty days, depending upon the location of the registrar.</p> <p><i>Reference: Rec. 4, Q 5</i></p>	Shorten/streamline registration procedures by promoting electronic links between CSDs and registrars.	Issuers, registrars, regulators, CSDs
Canada	<p>Foreign ownership restrictions</p> <p>Foreign ownership restrictions are not well controlled. There is no single body responsible for regulating or issuing foreign ownership limits. Transfer agents monitor caps so investors can find out about problems after the fact, when they are unable to register stock and protect their entitlements.</p> <p><i>Reference: Rec. 4, Q 6 and Rec. 7, Q 2</i></p>	Consider introduction of two separate lines of shares for companies imposing foreign ownership limits.	Issuers
Greece	<p>Shareholder Reporting</p> <p>There is a lack of specific guidelines relating to the monitoring of investors' acquisition of shares, surpassing pre-defined thresholds.</p> <p><i>Reference: Rec. 4 Q 6</i></p>	Appeal to regulators to clarify.	Regulators

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Mexico	<p>Entitlements, claims</p> <p>Lack of standards for cash or securities claims between broker/dealers and custodians and their customers.</p> <p><i>Reference: Rec. 4, Q 6</i></p>	Lobby CNBV or BMV to issue circular defining the compensation rules that will apply in the event of a cash or securities fail. Agree to industry wide standards among market participants.	AMIB Association of Mexican Financial Intermediaries
Taiwan	<p>Rules governing entitlements</p> <p>Grey areas in regulations (e.g. whether breach of FOLs will incur penalties).</p> <p><i>Reference: Rec. 4 Q 6</i></p>	Appeal to regulators to clarify.	Regulators, market participants
Venezuela	<p>Entitlements, claims</p> <p>Currently ex-date and announcement publications/regulations are subject to interpretation.</p> <p><i>Reference: Rec. 4, Q 6 and 8</i></p>	Establishment by the National Securities Commission of standards regarding the interpretation of these regulations would contribute to reducing the number of claims in the market.	National Securities Commission
Australia	<p>Proxy voting</p> <p>There is a lack of proxy voting services. It is left to the investor to contact the company concerned in order to cast votes.</p> <p><i>Reference: Rec. 4, Q 7</i></p>	Introduction of a central proxy voting service by CHES and Austraclear	CHES, Austraclear
France	<p>Proxy voting</p> <p>Proxy Cards must be signed by beneficial owner and submitted to the issuing company five days prior to the meeting.</p> <p><i>Reference: Rec. 4, Q 7</i></p>	Enable intermediaries (global custodian/local sub-custodian) to sign proxy cards on behalf of investors. The new economic Regulation bill should resolve this issue if/when the new law is passed and published.	Ministry of Justice/Issuing Companies Association (ANSA)
Norway	<p>Proxy voting</p> <p>Mandatory re-registration of securities in the name of the beneficial owner is required for proxy voting purposes</p> <p><i>Reference: Rec. 4, Q 7</i></p>	Allow proxy voting without actual reregistration or enable intermediaries to vote on behalf of investors.	Regulators
Switzerland	<p>Proxy voting</p> <p>Many Swiss companies do not accept shares registered in nominee name to grant proxy voting privileges, but request shares to be registered in the final beneficiary name. The process of registering shares in the final beneficiary name before a meeting and deregistering them after the meeting is very time consuming given the often tight time constraints.</p> <p><i>Reference: Rec. 4, Q 7 and Rec. 8, Q 3</i></p>	Promote nominee registration	Issuers

Market	Deficiency / Risk Description	Proposed Action	Party to Act
United Kingdom	<p>Proxy voting</p> <p>Proxy voting in the U.K. is still extremely manual and far too informal. There are no guidelines on reporting. Letters of Representation (where a client can ask for permission to vote on his/her/their own behalf) are a major problem given that one client could potentially cast a vote which is perceived to represent the whole holding in the custodian's nominee name. Filling in physical voting cards is an antiquated process, but still dominates the market.</p> <p><i>Reference: Rec. 4, Q 7</i></p>	CRESTCo is currently working on an electronic solution, but it is at least one year away.	CrestCo, Issuers
Turkey	<p>Corporate actions</p> <p>Lack of a fixed pay-date, time consuming and paper-intensive proxy-voting process; no standard period for notice of General Meetings.</p> <p><i>Reference: Rec. 4, Q 7 - 10</i></p>	Standardise and streamline corporate action procedures and deadlines.	Issuers, custodians
Canada	<p>Corporate actions</p> <p>The environment for corporate actions is difficult and risky. There are no mandated entitlement notification rules, no regulated lead times for event notification and no central reporting process. Last minute instructions are processed relying on "good will" between parties. It is common for tenders to undergo numerous amendments prior to finalisation.</p> <p><i>Reference: Rec. 4, Q 8, 9 and 10</i></p>	Note that in April 2001 CCMA wrote to all 10 provincial authorities to propose that issuers or their agents report entitlements.	Regulators, continued lobbying by trade organizations representing custodians, issuers
Argentina	<p>Corporate respectively government actions</p> <p>Programs related to the restructuring of the government debt are not always available to all investors at the same time and under the same terms.</p> <p><i>Reference: Rec. 4, Q 9</i></p>	Improve communication flows and ensure equal treatment of all investors	Treasury Department, Central Bank
Colombia	<p>Corporate actions and corporate governance standards</p> <p>The flow of information from companies to investors is very limited and lacks consistency.</p> <p><i>Reference: Rec. 4, Q 9</i></p>	Enforcement of corporate governance standards to increase transparency is needed. Also standardised data dissemination.	Regulators, Issuers, CSD
United Kingdom	<p>Electronic corporate action processing</p> <p>There is potential to take vast amounts of paper out of the system, given that CREST does have considerable capabilities to handle various corporate action events electronically, the latest being takeovers. However, there seems hesitancy on the part of the market to make the most of these facilities.</p> <p><i>Reference: Rec. 4, Q 9 and 10</i></p>	Promote/enable paperless corporate action processing	CrestCo

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Greece	<p>Entitlements paid by check</p> <p>Dividend proceeds are paid via check. This results in both risk in terms of lost checks and delays in receiving cleared funds.</p> <p><i>Reference: Rec. 4 generally (access to entitlements)</i></p>	<p>Electronic payment on a fixed date via the Cash Settlement Bank or other Bank appointed by the CSD.</p> <p>In November 2001, the Central Services Depository announced that it intends to automate the distribution of dividends and other corporate entitlements in early 2002.</p>	CSD, issuers
Hungary	<p>Corporate Governance</p> <p>Ownership restrictions are determined at the company level. Issuers are not required to publish such restrictions.</p> <p><i>Reference: Rec. 4 generally (transparency towards investors)</i></p>	Improve transparency of investment restrictions	Issuers, Regulators
United Kingdom	<p>Entitlements distribution</p> <p>Entitlements are currently paid by a variety of methods, (physical check, via CHAP's, by BAC's), but no process is particularly helpful with reconciliation, or clearing up market claims etc. or getting the money to clients on pay date.</p> <p><i>Reference: Rec. 4 generally (access to entitlements)</i></p>	The market is pushing for electronic payment via Crest.	CrestCo, Issuers

Recommendation 5: Reduction of Settlement Risk

The major risks in Securities Systems should be mitigated by five key measures, namely:

- the implementation of real delivery versus payment
- the adoption of a trade date plus one settlement cycle in a form that does not increase operational risk.
- the minimisation of funding and liquidity constraints by enabling stock lending and borrowing, broad based cross collateralisation, the use of repos and netting as appropriate
- the enforcement of scripless settlement
- the establishment of mandatory trade matching and settlement performance measures.

Questions:

- 5.1 Does the market use DVP settlement procedures in accordance with one of the recognised BIS models? If so, which one? If the model is not BIS model 1, are there plans to move to this model?
- 5.2 Does the market have a rolling settlement cycle of T+3 or shorter for all exchange traded instruments?
- 5.3 Could the market reduce the current settlement period to T+2 or below, without increasing fails rates? If so, how would this be achieved, and what plans are there to shorten the existing settlement cycle?
- 5.4 Is matching of trade details achieved on trade date, at least for direct market participants; and by trade date plus one for indirect participants?
- 5.5 Is the depository scripless, and, if not, is it working to enable scripless settlement?
- 5.6 Does the market allow partial settlements?
- 5.7 Can the depository accommodate same day turnarounds?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Argentina	<p>Lack of DVP for equity trades / most frequently used settlement process depends heavily on manual transport of documents.</p> <p>The settlement structure at the CVSA is a mix of electronic- and paper-based processes: trade instructions may be delivered to the depository as transfer slips or electronically via the infrequently used Custody Transfer System (STC). In the widely used transfer slip process, the depository stamps the slips thereby certifying that securities have been blocked in the purchaser's favour and returns the slips to the subcustodian. Volume surges may result in stamping delays due to backlogs at the depository. The subcustodian resubmits the slip after confirmation that the funds have been transferred through the central bank's electronic system. Blocked positions are returned to seller's accounts if the certified slip is not resubmitted to the CVSA by 7:00p.m. on SD. Security transfers must then be reinitiated by the counterparty the following day. It is possible that delays by the subcustodian in submitting the certified slip might lead to a funds transfer without a related securities movement.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Strive to streamline/automate settlement procedures	CSD, Central Bank
Bermuda	<p>DVP</p> <p>Value of either cash (purchase) or securities (sale) is relinquished prior to receiving countervalue. There is no finality of settlement defined by law.</p> <p><i>Reference: Rec. 5, Q 1, and Rec. 6, Q 1</i></p>	<p>Amend laws, rules and regulations to define finality.</p> <p>On an operational level, to increase efficiency and mitigate settlement risk, the central bank and market participants must connect the existing interbank wire transfer payment system to the depository's system so that securities and fund movements are linked.</p>	BSX, Bermuda Monetary Authority (BMA)
Brazil	<p>DVP</p> <p>Currently the market does not offer same day funds as subcustodians are able to confirm availability of funds only on SD+1. The exchange of securities and funds is not simultaneous and irrevocable for trades executed through Companhia Brasileira de Liquidacao e Custodia (CBLC). Securities released on SD – 1 are blocked for two days to allow payment confirmation.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Implement true DVP system.	CSD

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Bulgaria	<p>DVP</p> <p>The depository (CDAD) does not maintain funds accounts for its members and relies on commercial banks and their interbank payment system (BISERA) to effect cash movements. Securities are blocked in the selling member's CDAD account until BISERA processes the buyer's payment instructions. BISERA clears through an overnight process and, unless both buyer and seller use the same commercial bank, foreign exchange must be done for settlement date (SD)-1. Funds are debited from the investor on SD-1 and credited to the broker on settlement date for same-day value.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Implement a settlement process with linked cash and security transfers such that the actual transfers are culminated on the same day.	CSD, Central Bank, Regulators
Canada	<p>DVP, same day finality of payment for equities and corporate bonds</p> <p>Canada offers same day finality of payment only for government bonds. Finality of payment for equities and corporate bonds is achieved on SD+1 at noon. The central depository estimates that on an average day there are about 135,000 trades made. The value of trades awaiting settlement at the end of each day ranges from CAD 100 to CAD 150 billion. Under the current arrangements where finality is achieved on SD+1 at noon, this represents an estimate of intra-day counterparty risk. In as much as the current payment systems has significant risk assessment and protection mechanisms in place, there is still a residual risk that can be mitigated further through the achievement of same day finality of payment across the market.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	This can be done through the active co-operation of the Canadian Central Bank and the participants of the Central Depository. It will require significant re-engineering of the batch processing platform at the depository. This process is already in progress with the development of System X. It is expected that System X will become fully functional in 2002.	Canadian Central Bank and the participants of the Central Depository.
Chile	<p>DVP</p> <p>Securities settle in a non - DVP environment. There isn't a payment system linked to the DCV for payment of securities transactions. Thus, "vale vistas" cashier checks are used for securities transaction payments.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	The market needs to develop an electronic payment system and link the irrevocable transfer of funds to that of securities.	CSD, Central Bank, Regulators
China	<p>Lack of DVP in the B-share market</p> <p>Stocks are moved by T+3 in the SSCC or SSCCRC while cash is moved outside China in USD (Shanghai) and HKD (Hong Kong) with intra day cash risk.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Implement RTGS system. This is a much wider issue of convertibility of the currency. This is not currently expected pre-2005/6	CSD, Central Bank, Regulators
Colombia	<p>DVP</p> <p>Settlement of securities occurs separately from the money settlement. No DVP environment is provided for securities that settle through DECEVAL. There is a qualified DVP environment for interbroker and broker-custodian transactions as payment is verified prior to securities delivery.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	For settlement of equities, the market participants should develop a link between the central bank's electronic payment system and the transfer of securities at DECEVAL to allow simultaneous exchange.	CSD, Central Bank, Regulators

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Denmark	<p>DVP</p> <p>The CSD still operates BIS model 3 (non- RTGS) for a large number of market transactions. The model works on a batch process and as the CSD is not responsible for the movement of cash, there is no true DVP.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Replace current batch settlement cycles with Real Time Gross Settlement (RTGS) product. RTGS is available for certain transactions in Denmark.	CSD and market regulators
Hong Kong	<p>DVP</p> <p>Non DVP settlement risk for SI (electronic payment option) and physical securities.</p> <p><i>Reference: Rec 5, Q 1</i></p>	DVP is available in the market, but largely ignored as usage is optional – regulators perhaps could more strongly encourage participants to use the system.	CSD and market regulators
Hungary	<p>DVP</p> <p>If investors elect to use the GIRO payment system, rather than the real-time VIBER system, securities will be irrevocably transferred to the trade counterpart in exchange for funds that will not be cleared until SD+1. This is not a significant risk exposure to the trade counterpart in that the cash transfer is irrevocable upon acceptance of the instruction into the GIRO system. The risk exists in the impairment of liquidity or use of the funds.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Implement RTGS system for all market transactions.	CSD and market regulators
Indonesia	<p>DVP</p> <p>Non-DVP risks (for physical securities only).</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>Complete dematerialization and implement RTGS system for all market transactions.</p> <p>All securities are targeted to be dematerialised by June 2002, which will remove the physical securities risk. Risks will still exist in regard to the settlement of securities vs. cash which is not RTGS at present.</p>	CSDs, regulators
Korea	<p>Non-DVP settlement between broker and custodians</p> <p>Non-DVP settlement between broker and custodians. Even with the introduction of INAS, true DVP cannot be achieved. There is net non-simultaneous DVP in place between custodians and brokers through the INAS system, though use of this system is not compulsory.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Implement DVP system for all market transactions.	Central Bank, CSD
Latvia	<p>Limited Real Time Gross Settlement</p> <p>Settlement is based on a batch processing system.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	Replace current batch settlement cycles with a Real Time Gross Settlement (RTGS) product.	Central Bank, CSD

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Lithuania	<p>Limited Real Time Gross Settlement Settlement is based on a batch processing system. <i>Reference: Rec. 5, Q 1</i></p>	Replace current batch settlement cycles with a Real Time Gross Settlement (RTGS) product. These initiatives are already being discussed by market authorities.	Central Bank, CSD
Malaysia	<p>Non DVP settlement for Ordinary Transfers Above applies tot the Fixed Delivery Settlement System (FDSS). There is also non-DVP for ISS (Institutional Settlement Service) transfers. However, this is usually only a matter of 60 minutes. <i>Reference: Rec. 5, Q 1</i></p>	Implement RTGS system for all market transactions.	CSD and market regulators
Pakistan	<p>Limited DVP An optional delivery versus payment (DVP) system is available, but only to Karachi-based CDC account holders for the settlement of CDC-eligible securities. Payment for securities takes place outside of the settlement system. While cash RTGS is available, it is rarely used due to the need to pre-fund and the delay in withdrawing funds. <i>Reference: Rec. 5, Q 1</i></p>	Implement RTGS system for all market transactions.	CSD and market regulators
Pakistan	<p>DVP, payment may be made in next day funds Brokers settle physical trades at the counter of the subcustodian against a central bank check, which provides same-day funds only if deposited by 12:30 p.m. local time. Other checks require a 24-hour check clearance period. <i>Reference: Rec. 5, Q 1</i></p>	Implement RTGS system for all market transactions.	CSD and market regulators
Peru	<p>DVP, payment may be made in next day funds If payment is not made in the form of an interbank transfer, securities are irrevocably transferred to the trade counterpart in exchange for a check which carries next day value. However, approximately 90 percent of the payments are done through interbank transfers, providing investors with same-day funds. Issuance of payment is not contingent upon securities settlement. A real-time electronic payment system should be linked to the transfer of securities. A new Multi-Clearing Bank system has been approved for the settlement process of real time fund transfers. <i>Reference: Rec. 5, Q 1</i></p>	Implement RTGS system for all market transactions.	CSD and market regulators

Market	Deficiency / Risk Description	Proposed Action	Party to Act
<p>Philippines</p>	<p>Non DVP settlement Cash settlement between brokers and custodians is outside the clearing batch of the Securities Clearing Corporation of the Philippines (SCCP) via Manager's Checks or cashier orders. <i>Reference: Rec. 5, 1</i></p>	<p>Implement true DVP system for all market transactions, including broker to subcustodian settlements. An Electronic Funds Transfer Instruction System has been introduced by the Bangko Sentral since September 2001. Although not currently used for securities transaction payments, it is anticipated that standards on use and operation will be agreed by market participants within the next year.</p>	<p>CSD and market regulators</p>
<p>Russia</p>	<p>Non-DVP environment for equity settlements Movements of cash and securities are under the control of separate parties; the registrar effects ownership changes through the registration process and the subcustodian instructs the transfer of cash. Securities settle free-of-payment in Russia. Payment for equities is generally made outside of Russia in foreign currency, usually within two days of the subcustodian receiving the extract from the registrar. <i>Reference: Rec. 5, Q 1</i></p>	<p>Implement true DVP for all market transactions. However, there are important issues whose resolution should be a prerequisite to the implementation of DVP. These are easing of currency restrictions and clarification of tax laws and regulations. Forcing DVP settlement against rubles will not serve foreign investors. Furthermore, foreign institutional investors currently enjoy better than DVP arrangements as they do not pay for purchases until shares are received and they receive sale proceeds before they deliver shares.</p>	<p>Exchange, CSD, regulators</p>
<p>Singapore</p>	<p>Lack of true DVP Payment for shares could still be settled by check which may clear the next day, but by which time the shares would have been transferred. Though there is an existence of a DVP system where all member companies can appoint a settlement bank to settle their trades electronically, the participation is not compulsory. <i>Reference: Rec. 5, Q 1</i></p>	<p>To re-examine the need to have all trades settled via the electronic system in order to achieve true DVP.</p>	<p>Association of Banks and the Stock Exchange/Central Depository</p>

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Spain	<p>Lack of true DVP</p> <p>Cash and securities are controlled by two different entities. The Servicio de Compensacion y Liquidacion de Valores (SCLV) controls the transfer of equity and corporate debt. Government debt is settled via the Bank of Spain (BOS) which also controls the cash process. Therefore true delivery versus payment does not exist except for Government Bonds. Securities are blocked at 10am on settlement date, but cash does not move until 2pm in a batch process. Concerns exist regarding brokers entering receivership between these times.</p> <p>Settlement through the SCLV is not true DVP and improvement may be seen with the implementation of Iberclear. However, it should be noted that the SCLV does provide ensured settlement for matched transactions; settlement is guaranteed for accepted rapport trades, or non-rapport transactions that have matched in the SCLV system.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>To have both processes managed by one entity. There is an ongoing project "Iberclear" which sees the merger of the two entities where equities, cash and all fixed income will be settled on the same platform, thus enabling true DVP</p>	<p>SCLV, BOS and the market regulator, C.N.M.V. (Comision Nacional del Mercado de Valores)</p>
Sweden	<p>Limited Real Time Gross Settlement</p> <p>Settlement is based on a batch processing system.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>Replace current batch settlement cycles with Real Time Gross Settlement (RTGS) product</p>	<p>Central Bank</p>
Taiwan	<p>Non-DVP settlement</p> <p>Securities are moved by the TSCD on T+1 and cash is moved outside of the TSCD systems on T+2. Risk is mitigated by the ability of bona fide investors to claim against investor protection funds.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>Implement true DVP for all market transactions</p>	<p>Exchange, CSD, regulators</p>
Thailand	<p>Non-DVP settlement</p> <p>Although BAHNET is extended to TSD, it is not fully integrated within TSD. Counterparty risk still exists and unwinding relies on TSD's ability to reverse the securities movement upon non-receipt of good funds.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>Implement true DVP for all market transactions</p>	<p>CSD, regulators</p>

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Turkey	<p>Non-simultaneous movement of cash and securities possible for indirect participants</p> <p>Security movements may precede cash transfers. Direct ISE participants, including equity brokerage houses, are required to meet all their cash and securities obligations to the exchange by 3:00 p.m., or face default to the exchange. Indirect participants, including custodian banks, are not subject to this deadline, and have the facility to execute payment via electronic funds transfer (EFT), or the Takasbank Electronic Funds Transfer System (TETS) until their closure at 5:30 p.m.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>Takasbank introduced a true DVP settlement system into the market on September 17, 2001. The new DVP system is non mandatory and is used across the board by all local custodians. Usage is expected to increase in 2002 as trade volumes increase and local custodian banks work with the Takasbank to resolve perceived 'teething' problems.</p>	<p>CSD, regulators</p>
Venezuela	<p>Lack of DVP</p> <p>The current settlement process, where the movement of cash and securities are not synchronised and are performed on different systems, entails periods where investors are exposed to full value risk.</p> <p><i>Reference: Rec. 5, Q 1</i></p>	<p>Although this risk is mitigated to an extent by the Caracas Stock Exchange guarantee fund, it is recommended that the market introduces a true DvP settlement system. The Central Bank of Venezuela would be a key entity driving this effort as it would in particular require to put in place an interbank cash clearing system, which currently does not exist. The implementation of a true DvP system would also contribute to do away with the physical transfer slip, which is currently used for securities settlements and which has limited reliability especially in case of increasing volumes.</p>	<p>Central Bank of Venezuela</p>
Russia	<p>Negotiable, extended settlement cycle</p> <p>The settlement period for equities is negotiable and usually ranges from T+5 to T+15, depending upon the location of the registrar. The depository does not have authority to assess penalties or initiate buy-in procedures.</p> <p><i>Reference: Rec. 5, Q 2</i></p>	<p>Implement a standard settlement cycle</p>	<p>CSD, Exchange</p>
Australia	<p>CHES matching criteria</p> <p>Inability of CHES to match at the participant's client (beneficiary) level. While this was not identified in designing CHES because of the omnibus account structure and the remoteness of almost-identical transactions, this is a practical inconvenience and there are counterparty risk issues if delivery is made to the wrong party.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	<p>Extend CHES matching criteria to include participant subaccounts. CHES has PIDS which identify participants; it is the structure of the participant that determines whether the beneficial owner is identified. However, the market still allows for multiple structures.</p>	<p>CHES</p>

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Belgium	<p>Trade matching on subaccount or beneficiary level</p> <p>The subaccount or beneficiary is not a matching criteria at the CIK. The clearer is the lowest level of identification. This has resulted often in the CIK system matching and settling trades with identical matching elements but which in fact are not for the correct beneficiary. The introduction of the ISO 15022 SWIFT messages will make it easier for custodians to identify the beneficiaries in trades with identical trade details, but it will not prevent cross-matchings when the trades goes STP all the way, matches and settles automatically at the CIK.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	The CSD should add another level of matching but this does not seem to be in the pipeline.	CSD
Belgium	<p>Non-binding matching</p> <p>Matched CIK transactions are never binding even up to the last minute which adds an unnecessary element of uncertainty. (The National Bank of Belgium, the CSD for most bonds, has made matching binding as of 11:00 am on SD).</p> <p><i>Reference: Rec. 5, Q 4</i></p>	The CSD should make matching binding in order to give a reasonable level of certainty when processing back-to-back trades for example.	CSD
Belgium	<p>Weak matching failure reason codes</p> <p>The CIK does not provide a great deal of information when trades are unmatched therefore slowing down the process of identifying failure reasons. Custodians have mostly corrected that weakness through enrichment of the reason codes by manually accessing the CIK system and looking up potential matching transactions. However this remains a manual process to a large extent.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	The CSD should refine its failure reason codes.	CSD
Colombia	<p>Manual trade matching</p> <p>Manual prematching of trade instructions may occur between the subcustodian and counterparty.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	Consider automation	CSD, Custodians
Finland	<p>Paper-based prematching</p> <p><i>Reference: Rec. 5, Q 4</i></p>	Shift current paper based settlement instruction pre-matching to an automated, online format.	HEX, market participants
France	<p>Central matching criteria</p> <p>Although assets (equities and bonds) can now be segregated at sub-account level at the CSD level (Euroclear France), it is not presently feasible for a General Clearing Member to use this facility as they must use omnibus accounts until Clearnet has modified the ISB and SBI settlement systems</p> <p><i>Reference: Rec. 5, Q 4</i></p>	Clearnet to modify the ISB and SBI settlement systems.	Clearnet

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Germany	<p>Matching criteria at beneficial owner account level</p> <p>Lack of central matching at the sub-account level. Inability of matching at sub-account level within the CSD.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	Develop matching capability at beneficial account owner level within the CSD.	CSD, custodians
Germany	<p>Matching criteria for free of payment transactions</p> <p>Inadequacy of matching for free of payment transactions. Today there is no matching in Germany for free of payment transactions. As a result, improper allocation of shares occur too often.</p> <p><i>Reference: Rec. 5, Q 4 although the recommendation is not targeted at FOP transfers</i></p>	Introduce matching for free of payment transactions	CSD, custodians
Hungary	<p>Manual trade matching</p> <p>There is no electronic pre-matching system in the market, which results in a manual process (phone or fax). Foreign investors' settlements are solely conducted OTC, but settle the same day as the linked exchange trade. However, instructions can only be input into the settlement system to match by local custodians on SD. Since there is no time to correct mismatches, agents pre-match trades manually via phone and fax on the days preceding SD.</p> <p><i>Reference: Rec. 5 Q 4</i></p>	Implement automated pre-matching facility.	CSD
Italy	<p>Manual prematching</p> <p>No automatic pre-matching facility in Monte Titoli. Agent banks pre-match over the phone. Settlement risk in case of human error during the pre-matching process. If prematching does not occur by 9:00 p.m. on SD-1, the trade will settle outside the clearinghouse. Outside settlements are not automated. Participants settle securities transfers directly with <i>Monte Titoli</i> and, once the securities are transferred, payment is made through the cash clearing system for same-day funds. Investors are exposed to counterparty default during this process. Approximately 10 to 15% of non-resident exchange transactions settle in this manner.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	Automate pre-matching.	CSD
Italy	<p>Lack of central matching on subaccount level</p> <p>Inability of Monte Titoli to match at a sub-account level within the agent bank, as General Clearing Members maintain omnibus account and RRG does not recognise sub-accounts as matching criteria.</p> <p><i>Reference: Rec. 5, Q4</i></p>	Extend matching criteria to include sub-accounts	CSD

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Lithuania	Pre-matching is not market practice <i>Reference: Rec. 5, Q 4</i>	Implement pre-matching, if volumes justify.	CSD
Mexico	Manual pre-matching between brokers and custodians Pre-matching is executed over the phone to confirm trade instructions. After confirmation, transactions must be entered manually in INDEVAL's SIDV system. <i>Reference: Rec. 5, Q4</i>	Automate prematching and settlement confirmation.	CSD
Netherlands	Lack of matching on subaccount level Inability of Necigef to match at a sub-account level within the agent bank, as General Clearing Members maintain omnibus account and Necigef does not recognise sub-accounts as matching criteria. <i>Reference: Rec. 5, Q 4</i>	Extend matching criteria to include sub-accounts	CSD
Netherlands	Lack of pre-matching Pre-matching is not market practice and not supported by all market participants. Free of payment delivery instructions can settle (i.e. shares deposited into counterparty account) without a matching receipt instruction. The shares would be returned to the delivering party within a week if no matching receipt instruction was sent. <i>Reference: Rec. 5, Q 4</i>	Implement pre-matching functionality	CSD
Philippines	Prematching is manual There is no electronic prematching of PSE-member transactions. Manual prematching of trade instructions may occur between the subcustodian and the counterparty by T+3 via telephone or facsimile exchanges. <i>Reference: Rec. 5, Q 4</i>	Implement automated pre-matching	CSD
Singapore	Prematching / voluntary use of affirmation system Participation in the Institutional Delivery and Affirmation System (IDAS) is voluntary for those who are not members of CDP. Pre-matching with non-members can only be done manually, usually by phone. Broker-to-broker transactions are automatically matched through the SGX's computerised trading system, CLOB. For broker-to-custodian transactions, the subcustodian bank prematches the trade details with the broker over the telephone upon receipt of settlement instructions from the client. Prematched instructions are then keyed into IDAS by the broker for affirmation with the subcustodian banks. <i>Reference: Rec. 5, Q 4</i>	Extend/enhance pre-matching system to include all market participants.	Exchange, CSD, custodians

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Switzerland	<p>Matching criteria at ultimate beneficiary level</p> <p>Currently matching is only between agent banks; inability to match at subaccount level.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	Extend matching criteria to include subaccounts.	CSD
United States	<p>Inefficiencies in institutional client allocation and institutional settlement process</p> <p>Institutional client allocation and institutional settlement process has many inefficiencies. Many rely on phone trading and manual tickets. The information flow and allocation process is very manual.</p> <p><i>Reference: Rec. 5, Q 4</i></p>	This is expected to be addressed by the T+1 initiative.	T+1 initiative
India	<p>Dematerialisation / counterparty risk</p> <p>Although the impact of dematerialization has been significant to date and has improved overall settlement rates, trades of physical securities in India rarely settle on the contracted settlement date. Many of India's hundreds of brokers are thinly capitalised and face cash flow problems. Consequently, the fail rate in India remains among the highest in the emerging markets.</p> <p><i>Reference: Rec. 5, Q 5</i></p>	<p>Complete dematerialization and implement DVP system for all market transactions.</p> <p>With the introduction of T+5 compulsory rolling settlement across all securities, the number of trades in physical securities is very negligible. The fail rate, based on our understanding, has drastically reduced in the past few months.</p>	CSD and market regulators
United Kingdom	<p>Lack of full dematerialisation</p> <p>Some physical certificates still exist in the market. Although most major UK securities are in dematerialised form, physical holdings of securities also exist, registrars maintain records of holdings both within CREST and externally. For securities held outside of the CREST settlement system, registration can take up to 2 weeks, although securities can be sold during this period and settlement can be made.</p> <p><i>Reference: Rec. 5, Q 5</i></p>	It has now been agreed that any new issues have to be CREST eligible.	-

Recommendation 6: Market Linkages

Convergence of Securities Systems, both within countries and across borders, should be encouraged where this eliminates operational risk, reduces cost and enhances market efficiency.

Questions:

- 6.1 Is the depository linked electronically and in real time with other segments of the core market infrastructure (e.g. trading platforms, netting systems, matching platforms, payment systems)?
- 6.2 Is there one or more depository or settlement system in the market?
- 6.3 If there are several, has a consolidation been considered? If yes, by when?
- 6.4 Does (do) the securities system(s) allow other domestic or foreign systems to establish direct links on an equal basis to local members?
- 6.5 Does (do) the securities system(s) allow foreign market participants to become direct participants?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Argentina	<p>Trading system The creation of a single trading system and clearinghouse could assist in making the market more efficient. <i>Reference: Rec. 6, Q 1</i></p>	Consider consolidation of market infrastructures.	Stock Exchange
India	<p>Funds Transfer The current funds transfer systems rely on checks or on accounts maintained privately between the subcustodian banks. <i>Reference: Rec. 6, Q 1</i></p>	Electronic funds transfer should be developed. The Reserve Bank of India is working on it, but it remains a problem for the time being.	Central Bank

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Indonesia	<p>Same day funds</p> <p>Cash payments for securities, as affected by the KSEI, are made on a gross basis through three separate clearing banks. Each participant to the KSEI may select only one payment bank. There is no interbank, electronic transfer mechanism in place. The payment banks reconcile positions throughout the settlement date and are only able to fully credit cash positions to the participant's account after 4:00 p.m. Funds are unavailable for use until the following day.</p> <p><i>Reference: Rec. 6, Q 1</i></p>	Implement RTGS system for all market transactions.	Central Bank, Regulators
Thailand	<p>Manual link to automated settlement system</p> <p>The details of executed trades must be manually input to the settlement system.</p> <p><i>Reference: Rec. 6, Q 1</i></p>	Enhance STP within the market	Exchange, brokers, CSD
Venezuela	<p>Lack of full electronic connectivity between the brokers, stock exchange and depository</p> <p>Although the brokers have modem connectivity to the exchange and there are initiatives to have brokers send instructions to the stock exchange through the web, faxes are also used and manual reconciliation takes place at the stock exchange. In addition, the stock exchange and the depository are not fully interconnected as they only exchange reports.</p> <p><i>Reference: Rec. 6, Q 1</i></p>	It is recommended that further automation be implemented in the processing of information in and across entities in the market, this in particular as a condition to smoothly handling potential higher trade volumes.	Stock Exchange, Depository
Australia	<p>Multiple Clearing systems and lack of international links</p> <p>Market operates on three separate clearing systems which are not linked to other internationally based clearing systems.</p> <p><i>Reference: Rec. 6, Q 2, 3, 4 and 5</i></p>	<p>Linkage of securities clearing systems.</p> <p>RITS transferred its commonwealth government securities (CGS) to Austraclear. This will consolidate the clearing mechanism of the two depositories.</p> <p>RITS will remain as a cash payments system.</p> <p>In regard to the consolidation of Austraclear and CHES's clearing systems: This would be unlikely as Austraclear (SFE) focuses on debt and futures while CHES (ASX) focuses on equity.</p>	ASX, SFE

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Greece	<p>Complex market infrastructure</p> <p>The local infrastructure is complex as a result of multiple clearinghouses and depositories</p> <p><i>Reference: Rec. 6, Q 2</i></p>	Linkage of different depositories	CSDs
India	<p>Multiple depositories</p> <p>The existence of multiple depositories and the requirement of volatility margin (cash or early securities pay-in on T+1) cause settlement inefficiency</p> <p><i>Reference: Rec. 6, Q 2</i></p>	There is a need for interdepository settlement to take place at the time of market settlement. Today it takes place after market settlement has been completed.	CSDs, regulators
United States	<p>Complex market infrastructure</p> <p>Fairly complicated infrastructure with multiple clearinghouses, depositories, and payment vehicles.</p> <p><i>Reference: Rec. 6, Q 2</i></p>	Explore scope for further convergence.	Operators of market infrastructure
United Kingdom	<p>Post-order infrastructure of the open-ended investment funds industry.</p> <p>The current process is very labour intensive with little opportunity for STP. Market participants are keen to see the benefits of electronic asset holding and settlement extended to the open-ended securities market, but issuers continue to use largely manual and paper-driven issuing, reconciliation and redemption practices.</p> <p>Distribution channels in the UK are diverse, there is no central market for unit trusts, and there is an absence of central infrastructure co-ordination which results in varying settlement, registration and reconciliation practices.</p> <p><i>Reference: Rec. 6 to some extent, although funds are not specifically in the Recommendations</i></p>	Extend/require use of Crest settlement solution for unit trusts, which is currently used by only eight product providers.	Investors, CrestCo

Recommendation 7: Investor Protection

Regulators in each country should review whether locally domiciled institutions have a process in place that enables them to comply with the laws and regulations of the countries where their investments are placed. In turn, foreign investors should always be treated in like fashion to indigenous investors, especially in respect of their rights to shareholder benefits.

Questions:

- 7.1 Do domestic regulators monitor the procedures in place at their locally based cross-border custodians to assure compliance with the laws and regulations of the home countries of their investments?
- 7.2 What are the areas (e.g. benefits, investor compensation) where foreign investors are not treated in the same way as local investors?
- 7.3 Can sales proceeds and income be repatriated without any restrictions?
- 7.4 Are double tax agreements simple to apply, and do foreign investors receive promptly their full entitlement to dividends and interest payments?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Argentina	<p>Ambiguous legislation</p> <p>Legislation needs to be more transparent, well defined, efficient, and conducive to the needs of all investors. For example, repatriation requests require Central Bank approval but the newly passed resolutions had no implementation procedures.</p> <p><i>Reference: Rec. 7 generally</i></p>	Consider consultation process with parties affected by new legislation, prior to enactment	Regulators
Brazil	<p>Documentation Requirements</p> <p>Eliminate the requirement that foreign institutional investors file documentation to enter the market.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Ease market entry requirements for foreign investors.	Regulators
Brazil	<p>Currency Restrictions</p> <p>The central bank should allow financial institutions to pay interest on foreign institutional investors' cash accounts.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Align treatment of domestic and foreign investors.	Central Bank

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Brazil	<p>Lack of Free Transfers</p> <p>Allowing free transfer of securities would eliminate the need for local authorities to monitor foreign institutional investor activity or process name change approval requests.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Allow free of payment transfers of securities.	Regulators
China	<p>Limited foreign participation in the securities market</p> <p>Foreign investors are only allowed to trade B shares and the liquidity tends to be small and price volatile. Lack of access to A shares and the subsequent illiquidity and volatility in the B share market is a risk issue.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	<p>Consider further market opening</p> <p>This is currently receiving airtime with all major market regulators including proposals to open via a Taiwan QFII or Korean IRC mechanism. Any opening will be gradual and highly controlled, though could be as early as 2003.</p>	Regulators
Japan	<p>JASDEC's inability to monitor Foreign Ownership Limits, giving rise to the need for foreigners to remove FOL stocks from JASDEC over each record date. Removal, reregistration, re-deposit is costly and time-consuming, and the resultant maintenance of FOL stocks perpetually in physical form is inefficient and risky.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Implement an electronic system for monitoring FOL that allows all securities to be safekept in JASDEC without negative repercussions.	JASDEC
Malaysia	<p>Restrictions for foreign investors</p> <p>Capital controls (foreign investors are required to maintain segregated securities accounts) and restrictions in transferring securities between different types of securities accounts. The restrictions in moving between securities accounts are between those belonging to different investors.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Consider introduction of two separate lines of shares for foreigners and domestic investors. In practice, this is already in place but rarely used (when foreign ownership limits are hit, the security is split and foreigners usually still get all entitlements). The Stock Exchange is reviewing this now.	Regulators
Mexico	<p>Foreign ownership restrictions</p> <p>Foreign investors purchasing a restricted security that is not backed by a corresponding CPO may lose ownership of these securities since they can be confiscated by the CNBV.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Consider introduction of two separate lines of shares for foreigners and domestic investors?	Regulators

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Pakistan	<p>Insufficient legal stability and clarity of rules</p> <p>Risks and lack of clarity on certain regulations (e.g. whether foreign investors may participate in securities lending and borrowing).</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Consider intensified consultation process with parties affected by new legislation, prior to enactment	Regulators
Poland	<p>Improvements needed for international brokers</p> <p>International brokers are not permitted to select a single local custodian to act as their clearing agent in the market. Instead, international brokers need to set up clearing relationships with each local custodian that their clients have custodial relationships with. (These initiatives are already being discussed by market authorities.)</p> <p><i>Reference: Rec. 7, Q 2</i></p>	Allow international brokers to appoint global clearing agents.	Regulators
Thailand	<p>Foreign ownership restrictions</p> <p>Risk that foreign investors lose all corporate entitlements should they not be able to convert their local holdings into foreign shares although this is somewhat mitigated with the introduction of NVDR.</p> <p><i>Reference: Rec. 7, Q 2</i></p>	<p>Consider introduction of two separate lines of shares for foreigners and domestic investors.</p> <p>This is in place at the moment however, foreign registered shares tend to trade at a premium. There is also a possibility being reviewed now that foreign holders of NVDRs may be allowed to vote their shares. This, if implemented, would have a major affect on FOL issues.</p>	Regulators
France	<p>The tax regime for foreign investors is complex</p> <p>Entitlement to tax refunds and tax credits like the “precompte” and “avoir fiscal” is not straight-forward under DTA’s, as numerous exemptions apply.</p> <p>Currently French tax authorities only reimburse reclaims when withholding agent and reclaiming agent are one and the same.</p> <p><i>Reference: Rec. 7, Q 4</i></p>	A simpler regime allowing foreigners to reclaim taxes.	Tax Authorities

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Japan	<p>Cumbersome QFI requirements</p> <p>Complicated requirements for foreign investors to apply as a Qualified Foreign Intermediary to enjoy interest withholding tax exemption for JGB. Japanese legislation establishes two intermediary statuses (FIP and QFI) for foreign institutions (e.g. global custodians) through which foreign investors may gain access to, and enjoy withholding tax exemption through, the Bank of Japan's BoJ-Net system for Japanese Government Bonds (JGBs). As Foreign Indirect Participant (FIP), a global custodian is responsible for ascertaining that the ultimate beneficial owner of deposited JGBs has been identified. As Qualified Foreign Intermediary (QFI), a foreign institution is responsible for confirming the tax exempt status of its clients; i.e. beneficial owners. Obtaining these statuses is a cumbersome process and the associated functions carry with them major legal and procedural burdens. Additionally, even if all of these hurdles have been surmounted, client / beneficial owner eligibility for tax exemption on JGB interest is restricted to a limited number of end investor types; i.e., foreign individuals, foreign corporations, and recognized sovereign entities. Current draft legislation, if passed, would expand eligibility to include a number of investment trust types. This cumbersome process does not achieve the government's stated goal which is to ensure that local investors do not gain access, directly or indirectly, to tax exemption on JGB coupon interest.</p> <p><i>Reference: Rec. 7, Q 4</i></p>	<p>Seek to eliminate the extraordinary intermediary roles and make JGB withholding tax exemption eligibility broadly available to all types of foreign institutional investors.</p>	<p>Ministry of Finance (tax authorities) and Bank of Japan</p>
Turkey	<p>Tax requirements in Turkey remain complex and onerous</p> <p>Instead of end of year calculations based on realised capital gains, local tax consultants must be hired to calculate realised and unrealised gains at an asset level, make offsetting adjustments for interest and other taxes paid, incorporate the portfolio % of equities in each fund to determine tax rates, etc.</p> <p>Recent changes, relating to the need for funds to apply for individual tax IDs rather than using the global custodian's umbrella tax ID, compounded this complex situation by imposing new documentation requirements.</p> <p><i>Reference: Rec. 7, Q 4</i></p>	<p>Implement a tax system that falls in line with other markets; standard capital gains tax calculated annually at the end of each year based on realised portfolio gains.</p>	<p>Regulators</p>

Recommendation 8: Legal Infrastructure

Local laws and regulations should ensure that there is segregation of client assets from the principal assets of their custodian and no claim is possible on client assets in the event of custodian bankruptcy or a similar event. Regulators and markets, to further improve investor protection, should work:

- to ensure clarity on the applicable law on cross border transactions
- to seek international agreement on a legally enforceable definition of finality in a securities transaction
- to ensure that local law fully protects the rights of beneficial owners
- to strengthen securities laws both to secure the rights of the pledgee and the protection accorded to client assets held in Securities Systems.

Questions:

- 8.1 Under local rules and regulations, what are the segregation requirements for keeping client assets and custodian assets in the depository?
- 8.2 How are clients' assets protected in the event of insolvency of a custodian or depository?
- 8.3 Does local law recognise the existence of beneficial owners who may differ from the legal owner of a security?
- 8.4 Does local law clearly define the point of time when a settlement, both for the security and the cash involved, achieves finality and thus cannot be unwound?
- 8.5 Does a pledgee have an absolute right to realise their security at all times?
- 8.6 Does the depository have loss sharing provisions in its rules, and how would these be applied?

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Australia	<p>Unclear consequences of custodian or CSD system insolvency</p> <p>In the event of insolvency of a custodian or a depository, Australian law usually recognises Custody as a part of 'Trusts' legislation and thereby places ownership with the beneficial owners. This, however, does not make clear the level of protection afforded.</p> <p><i>Reference: Rec. 8, Q 2</i></p>	Clarify Australian law to protect the clients' interests in case of insolvency.	Regulators and/or custodians

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Bulgaria	<p>Nominee Concept</p> <p>While Bulgarian law recognizes the fact that a foreign entity might be holding securities on behalf of an underlying investor, the law does not explicitly express the ramifications of this policy.</p> <p><i>Reference: Rec. 8, Q 3</i></p>	Clarify legislation relating to nominee / fiduciary structures.	Regulator
Greece	<p>Nominee Concept</p> <p>Securities are maintained on the records of the CSD at the client or fund level and any name change requires securities to be “crossed” at the exchange, incurring costs. In December 2001, the Capital Market Authority stated they do not want to adopt a nominee concept but maintain segregated accounts.</p> <p><i>Reference: Rec. 8, Q 3</i></p>	Nominee concept to be recognised.	Regulators
Lithuania	<p>Nominee Concept</p> <p>Lithuanian law does not recognize the nominee concept.</p> <p><i>Reference: Rec. 8, Q 3</i></p>	Implement nominee concept.	Legislators
Hungary	<p>Nominee Concept</p> <p>In Hungary the nominee concept is not recognised, although there are legislative developments that may further clarify and improve this situation. The books of the local sub-custodian are recognised as the record of legal ownership of securities. Market practice is for the global custodian to maintain omnibus accounts at KELER, and to have segregated accounts by beneficial owner at the local sub-custodian. This means that a large number of accounts must be maintained at the local sub-custodian.</p> <p><i>Reference: Rec. 8, Q 3</i></p>	Further legal changes to facilitate implementation of nominee concept. Though the new Securities Act introduced the nominee concept in Hungary, other related regulations, namely the tax law, need to be amended for the nominee concept to be implemented.	Regulators
Malaysia	<p>Account Naming Conventions:</p> <p>The Malaysian Central Depository (MCD) requires that all accounts be held in the name of the end beneficial owner and that the account name meet certain local standards. In many cases, the MCD regulations do not take into consideration naming conventions which are legal in other countries. In addition, there is no process to address a clerical error in an account name.</p> <p><i>Reference: Rec. 8, Q 3</i></p>	Review appropriateness of account naming procedures.	CSD
Peru	<p>Nominee Concept</p> <p>The nominee concept recognized by law has not yet been implemented by market participants.</p> <p><i>Reference: Rec. 8, Q 3</i></p>	Implement nominee concept	Market participants

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Poland	Nominee concept Polish law does not recognize the nominee concept. <i>Reference: Rec. 8, Q 3</i>	Introduce nominee concept	Legislators
Slovenia	Nominee Concept Slovenian law does not recognize the nominee concept. <i>Reference: Rec. 8, Q 3</i>	Introduce nominee concept	Legislators
Spain	Nominee Concept In Spain, the nominee concept is not recognised. Ownership is determined by registration name and this forms a fundamental element of successful settlement. <i>Reference: Rec. 8, Q 3</i>	Consider implementation of nominee concept	Regulators
Turkey	Nominee Concept There is no recognition of the nominee concept in Turkey. <i>Reference: Rec. 8, Q 3</i>	Introduce nominee concept	Legislators
India	Clear Title Ownership of securities can be disputed despite holdings being dematerialized. Specifically, third parties can claim that they owned the underlying securities that were dematerialised. In many cases, the underlying shares are untraceable. Each investor deemed to have had ownership of the securities post-dematerialization is named as a defendant in a court case and may ultimately be responsible for compensating the plaintiff for corporate entitlements. Effectively, share disputes are frozen pending resolution through the court system, which takes between 10 to 15 years. <i>Reference: Rec. 8 Q 4</i>	Perfect ownership laws as applicable to dematerialised assets.	Legislators
Italy	Lack of clarity on point of finality of settlement RRG: At the present performs both trading and clearing functions. These two functions should be split in order to precisely identify when the settlement becomes final. <i>Reference: Rec. 8, Q 4</i>	RRG should separate trading and clearing functions.	Operators of the RRG System (i.e. SIA)

Market	Deficiency / Risk Description	Proposed Action	Party to Act
Mexico	<p>Indeval implemented a multilateral netting scheme for broker-to-broker settlements, however it lacks an adequate legal basis.</p> <p>The depository will function as a central counterparty in all but the legal sense. Broker/dealers must sign a contract agreeing to accept any other broker/dealer (subject to Indeval netting daemon) as counterparty to settlement. Since the concept of transfer of obligations/rights <i>a priori</i> does not exist under Mexican law, this weakens any legal claim a participant might have in the event of a fail.</p> <p><i>Reference: Rec. 8, Q 4</i></p>	<p>Establish a central counterparty upon receiving authorisation from BMV and/or CNBV. Indeval and AMIB are currently working on constituting an Indeval subsidiary as a central counterparty.</p>	<p>AMIB, Indeval, custodians, broker/dealers</p>
United Kingdom	<p>Finality of stock delivery vs cash payment</p> <p>The market allows physical delivery of stock (the so called "residuals" process) for non CREST eligible securities. Finality is only received on stock once it has been received by the stock transfer agent and passed through their books. There is thus no DVP.</p> <p><i>Reference: Rec. 8, Q 4</i></p>	<p>The market participants should put pressure on issuers to enable their stocks to be CREST eligible. Agreement has been reached with primary market players that all new UK securities will be CREST eligible.</p>	<p>-</p>
United Kingdom	<p>Finality of stock delivery vs cash payment</p> <p>The Central Money Markets Operation (which is run by CREST on a separate platform to its main operations) is a high value book entry transfer platform for short dated GBP money market instruments. It operates intraday finality of stock and end of day finality of cash. This places investors at risk should there be a non payment by a buyer at the end of the day.</p> <p><i>Reference: Rec. 8, Q 4</i></p>	<p>The market plans to move CMO onto the CREST system. The scheduled date is mid 2003. This is no great technical challenge, but requires some quite complex changes in law. The UK government has agreed to prioritise this change and it seen as non controversial although technically complex.</p> <p>Users should put pressure on the UK authorities to ensure that the target date for the move of CMO instruments onto the CREST platform is expedited and in any event occurs no later than mid 2003.</p>	<p>The re-engineering of the CMO is the responsibility of the Bank of England/Government (legislation needed) and CREST as operator.</p>