THE ASSOCIATION OF GLOBAL CUSTODIANS

THE BANK OF NEW YORK
BROWN BROTHERS HARRIMAN
CITIBANK, N.A.
DEUTSCHE BANK AG
INVESTORS BANK & TRUST COMPANY
JPMORGAN CHASE BANK
MELLON TRUST/BOSTON SAFE DEPOSIT
& TRUST COMPANY
THE NORTHERN TRUST COMPANY
STATE STREET BANK AND TRUST COMPANY

COUNSEL TO THE ASSOCIATION:
BAKER & MCKENZIE
815 CONNECTICUT AVENUE, N.W.
WASHINGTON, D.C. 20006

TELEPHONE: 202/452-7013
FACSIMILE: 202/452-7074

March 15, 2002

Permanent Bureau
Hague Conference on Private International Law
Scheveningseweg 6
2517 KT The Hague
Netherlands

Attn: Christophe Bernasconi, First Secretary

Re: Comments on the Preliminary Draft Convention on the Law Applicable to Certain Rights in Respect of Securities Held with an Intermediary

Ladies and Gentlemen:

On behalf of the Association of Global Custodians, thank you for the opportunity to comment on the Preliminary Draft Convention on the Law Applicable to Certain Rights in Respect of Securities held with an Intermediary as adopted by the Special Commission on January 17, 2002 ("Preliminary Draft"). As set forth in our October 31, 2001 comment letter,[1] the members of the Association, which are listed above, would be directly affected, both in their capacity as custodians and in their capacity as holders of security interests, by the provisions of the Preliminary Draft.

At the outset, the Association wants to reiterate its support for the Convention. It is important to lenders that they be able to perfect, with a high degree of certainty, security interests granted to them in a portfolio of global securities. The Preliminary Draft goes a long way in accomplishing this goal.

It is equally important, however, in order for the Convention to accomplish its purpose, for the relevant intermediary and its customer to be able to select ("agree upon") the jurisdiction which will ultimately be relied upon by the secured lender in

---

1/ Letter, dated October 31, 2001, to Christophe Bernasconi, First Secretary, Permanent Bureau, Hague Conference on Private International Law, from Daniel L. Goelzer, Baker & McKenzie, on behalf of the Association of Global Custodians.

perfecting its security interest; and for the secured lender to be able to verify, with relative ease and minimal due diligence, the appropriateness of such selection.

In this regard, the Association supports Article 4(2) in the Preliminary Draft. As the revisions to Article 4(2) recognize, because of advances in technology and communications systems, global custody accounts, and the functions and services which, in the aggregate, comprise and define global custody accounts, may not be maintained in a single location. Rather, as also recognized by the revisions to Article 4(2), global custody accounts, and the functions and services which comprise them, may be performed in multiple locations in different jurisdictions. Because, under the Convention, the relevant intermediary and its customer are required to agree upon a jurisdiction of the relevant intermediary (in which the relevant intermediary is engaged in a business or other regular activity of maintaining securities accounts) for perfection purposes, the relevant intermediary will be required to select one of various jurisdictions in which it is performing such services or functions. The secured lender will then rely upon that selection (as embodied in an agreement with its customer) and use the law of the jurisdiction so selected to perfect, pursuant to the Convention, its security interest in the customer's portfolio of global securities.

While Article 4(2) lays the foundation for selecting the appropriate jurisdiction, it is not, in and of itself, sufficient. The Convention must, in addition, contain a "safe harbor" which the relevant intermediary and its customer can rely upon in selecting ("agreeing upon") the jurisdiction which will ultimately be relied upon by the secured lender. The relevant intermediary cannot risk being "second guessed" at some point in the future by a court in the context of the customer's insolvency proceeding (or other form of proceeding) in which the validity of the security interest is challenged. If the court determines that the jurisdiction so selected was the "wrong" jurisdiction, the secured lender, which relied upon the jurisdiction identified by the relevant intermediary, may attempt to recoup its losses from the solvent relevant intermediary. Consequently, in order to minimize risk to relevant intermediaries, the Convention must contain a list of functions and services which the relevant intermediary and its customer can conclusively rely upon in selecting the jurisdiction for Article 4 purposes -- which is the purpose of Article 4"bis" and the reason it needs to be included in the Convention.

Although the Association believes that Article 4"bis" as currently drafted provides, in most instances, an appropriate "safe harbor" for relevant intermediaries, the Association recognizes that Article 4"bis" may need to be clarified to better define and describe the nature and type of global custody functions and services which are

performed at particular locations for purposes of Article 4(2). To the extent that Article 4"bis" needs to be clarified, the Association has set forth below the nature and types of global custody functions and services which define and comprise a global custody account and which should be the basis for the tests set forth in Article 4"bis"(1) (the so-called "white" list). In addition, because the Association believes that there are criteria which should definitely not be taken into consideration, the Association has also set forth below its views with respect to Article 4"bis"(2) (the so-called "black" list).

The Association also supports the methodology embodied in Article 4(3) for establishing the agreement required by Article 4(2). However, because the Convention applies to agreements which will have been executed before the Convention is adopted, the Association is concerned that an extremely large number of agreements, executed prior to the adoption of the Convention, will not be in compliance with Articles 4(2) and (3) and will need to be amended. Given the number of existing agreements, such an endeavour would be very costly and burdensome and would undermine the utility and efficiency of the Convention. The Association therefore urges, as will also be discussed more fully below, that the Convention contain a provision, whether in Article 17"bis" or Article 4(3), that permits certain jurisdictional-related provisions which are clearly set forth in the pre-Convention agreements -- such as governing law provisions or, with respect to banks, a clear reference to a particular branch -- to satisfy the "agreement" requirement of Article 4(2).

Comments

Our comments on Articles 4"bis", 17"bis" and 4(3) (to the extent it relates to Article 4(3)) are set forth below.

Article 4"bis" - Generally

Article 4"bis"(1) is intended to provide clear guidance and certainty to the relevant intermediary and its customer in their selection, for purposes of Article 4(2), of a jurisdiction which provides only some, but not all, services for a global custody account. It essentially serves as a "safe harbor" by setting forth a list of factors which the relevant intermediary and its customer can conclusively rely upon in identifying and selecting locations where the relevant intermediary will be deemed to be "engaged in a business or other regular activity of maintaining securities accounts" within the meaning of Article 4(2). If the jurisdiction selected is covered by Article 4"bis"(1), a court, in the

context of an insolvency proceeding (or other type of proceeding which challenges the validity of the security interest) should not be able to overturn or reject such selection.

On the other hand, the "safe harbors" are not intended to be the only locations which satisfy the Article 4(2) requirements. Relevant intermediaries and their customers should be able to agree upon other jurisdictions, but such selection may be subject to close judicial scrutiny and to possible rejection by the courts -- but that is always a risk of acting outside the protection of the "safe harbor." Consequently, the Convention must be sufficiently flexible to accommodate such alternatives, as well as change and innovation which may occur in the future.

The Association also believes that, if Article 4"bis" is included as mere commentary to Article 4, there may be less certainty that the location selected will be upheld in proceedings challenging the validity of such selection, particularly in those jurisdictions in which the courts do not recognize commentary as a legal source of guidance in the interpretation of treaty provisions. To minimize risk to the relevant intermediary, the list of factors that determine the locations which the relevant intermediary and its customer may conclusively rely upon must be in the Convention and not relegated to commentary.[2]

In contrast, Article 4"bis"(2) sets forth the list of those factors that should not be considered in determining the location pursuant to Article 4(2) -- the so-called "black" list. The Association believes that the inclusion of the "black" list in the text of the Convention is equally important as the inclusion of the "white" list for the same reasons noted above. The inclusion of the "black" list provides certainty that the enumerated factors, and resulting locations, will not be used as the basis for determining compliance with Article 4(2). This becomes particularly important in the context of parties which are not relying on the "safe harbors" of Article 4"bis"(1).

2/ From the lender's perspective, the inclusion of this list is equally important. A lender performing due diligence will be confident in perfecting a security interest in the jurisdiction specified in the agreement between the relevant intermediary and its customer if the location so specified is consistent with, and is clearly covered by, the Convention.

Article 4"bis"(1)(a)-(g)

In general, the Association supports the inclusion of Articles 4"bis" (1)(a)-(g) in the Preliminary Draft because the activities described in these provisions essentially comprise and define, in the aggregate, a global custody account. Consequently, any one of the locations where such activities are performed by the relevant intermediary should be, at a minimum, sufficient to satisfy Article 4(2). The Association recognizes, however, that these provisions may be viewed by some delegations as being too general and not sufficiently descriptive, requiring some modification and clarification. In addition, the Association believes that certain provisions are sufficiently unclear to warrant clarification. Accordingly, the Association offers the following suggestions and guidance.

Article 4"bis"(1)(b) refers to those locations where accountholders can communicate with the relevant intermediary with regard to their securities account. To the Association and its members, this provision is intended to refer to the location at which administrative services are provided by personnel of the relevant intermediary -- often referred to as account administrators, relationship managers, client service representatives and by other similar titles -- who are assigned to specific customers, who are generally responsible for the relationship with customers and who are available to communicate and meet, on a regular and ongoing basis, with customers regarding their securities accounts. It is not intended to include, for example, telephone answering centers.

Similarly, with respect to Article 4"bis"(1)(a) the location where a relevant intermediary executes contracts or receives contracts regarding securities accounts -- the Association also interprets this provision as referring to locations where sales and administrative services are provided on a regular basis. Agreements are typically signed by the relevant intermediary's sales force and then forwarded to the administrative staff (referred to in Article 4"bis"(1)(b) above). These are appropriate locations for the purpose of Article 4(2). The criteria currently contained in Article 4"bis"(1)(a) can either be incorporated in (1)(b) or can be included as a separate provision as in the Preliminary Draft. The Association notes, however, that agreements are only one of several account opening documents forwarded to such location; and the Association recommends that consideration be given to expanding this provision to include the location to which all account opening documentation is sent in connection with the establishment of global custody accounts. The Association, however, does not intend for the provision to encompass locations such as central mail rooms or central

file rooms with which the customer has minimal contacts -- both of which are locations where agreements might be deemed to be "received."

Article 4"bis"(1)(c) refers to those locations of the intermediary where legal, regulatory, auditing, position monitoring, or accountholder support functions are provided. While we generally agree that some of these services are relevant to global custody accounts and that the locations at which they are performed should be acceptable for compliance with Article 4(2), we also believe that, to the extent these services are appropriate, they may overlap with services which are covered by or are included within other provisions (for example, accountholder support functions would likely fall within those activities covered in Article 4"bis"(1)(b) and position monitoring may fall within Article 4"bis"(e) discussed below). However, it is not clear to the Association what is intended by certain of the referenced services (such as legal, regulatory and auditing). Consequently, the Association believes that this provision should either be further clarified, incorporated in other provisions or deleted as unnecessary.

Article 4"bis"(1)(d) refers to the location of the address appearing on an account statement or the location where account statements are prepared. Typically, the address on an account statement or the address at which the account statement is prepared is merely a processing center and not an actual location of an office of the relevant intermediary. These locations can easily be changed and may not bear a reasonable relationship to the location at which global custody services or functions are provided. It is unlikely that the Convention intended to include such transitory locations and, indeed, to the extent the location is simply a processing center, may be excluded under Article 4"bis"(2). Therefore, the Association believes that this provision should be deleted. If the Permanent Bureau determines to leave this reference in, the Association suggests more clearly defining the locations that are intended to be included in this reference.

In the Association's view, Articles 4"bis"(1)(e) and (f), should be referring to those locations where fundamental or core activities are performed and services are provided relating to the maintenance and operation of a global custody account. The Association therefore believes that these two provisions in the Preliminary Draft should be significantly revised to more clearly indicate that Article 4(2) includes those locations of the relevant intermediary where one or more fundamental or core global custody functions relating to the maintenance or operation of a securities account occurs and fundamental client services relating to a global custody account are provided.

Examples of such core functions and services include the locations where customer accounts are updated, trade and settlement instructions are received and processed, corporate actions are received and processed, cash management services are provided, asset reconciliation services are provided, tax reclamations are processed and account statements are prepared and issued. These examples should be reflected either in the Convention itself or in the commentary accompanying the Convention.

Finally, Article 4"bis"(1)(g) refers to those locations where a single account number, bank code or other means of identification exists that identifies the office as maintaining securities accounts. This provision, as contained in the Preliminary Draft, is acceptable to the Association and it has no recommendations for change.

Article 4"bis"(2)

As noted above, the Association is in favor of retaining this provision in the Convention and has no recommended changes.

Article 17"bis" - Interpretation of Pre-Convention Agreements

Article 17"bis" addresses the applicability of the Convention to agreements that were finalized prior to the effective date of the Convention but do not expressly address the location of the securities account in compliance with Articles 4(2) and (3). The Association believes that such agreements should not have to be amended after the adoption of the Convention in order to comply with the Convention. Many existing agreements have "jurisdictional tests" embodied in them which should be sufficient for compliance with Article 4(2). One obvious "jurisdictional test" is the governing law provision -- which is incorporated in Article 17"bis" of the Preliminary Draft. Another clear "jurisdictional test," at least for banks, is the specific reference to a branch or office in the agreement.

The Association urges that the Convention include, either in Article 17"bis" or in Article 4(3), a provision which recognizes, for pre-Convention agreements, traditional "jurisdictional" indicators -- such as governing law and reference to a particular branch or office of the relevant intermediary. Such a provision will obviate the need to amend thousands of agreements which would have been entered into prior to the adoption of the Convention -- something which would be quite burdensome and will undermine the effectiveness of the Convention.

* * *

The Association supports the efforts of the Hague Conference to address the important and difficult issue of creating greater certainty concerning the law that governs cross-border financial collateral arrangements in the globalized securities markets. We would be pleased to work with the Permanent Bureau and other interested parties to address these issues. If you have any questions concerning these comments, or if there are specific issues concerning the activities and practices of global custodians that would be of interest, please contact the undersigned at 202/452-7013.

Sincerely,

Daniel L. Goelzer

7130821v1