

Call for evidence

Directive 1997/9/EC on Investor-Compensation Schemes

Comments from the Danish Financial Supervisory Authority

8 April 2009

Ref.

J.no.

The Danish Financial Supervisory Authority welcomes the call for evidence on the application of Directive 1997/9/EC to evaluate whether and how it should be modified in order to better protect investors.

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General observations:

Directive 1997/9/EC has fulfilled its mission. It has provided a minimum protection for private investors. The scheme is simple to operate.

MINISTRY OF ECONOMIC AND
BUSINESS AFFAIRS

The call for evidence raises two questions: Firstly may the directive be amended to improve the functioning of the protection provided? Secondly should the scope of the directive be enlarged?

The point of departure for us is that the ICSD should cover retail investors only. Amending the scope of the directive to include professional operators in the financial sector will substantially change the schemes. Any change should be based on impact assessments which clearly demonstrate the added value of the amendment.

May the directive be amended to improve the functioning of the protection provided?

5) Do you agree with the idea that the amount covered by the ICSD should be adapted following the updating of the DGSD?

The ISCD may not be compared directive 2009/14/EC. The increase of the minimum cover for deposits was a response to the liquidity and confidence crisis in the banking sector. The purpose of the Directive 1997/9EC is built and maintain confidence for holders of securities.

An increase in the amount covered should be considered to reflect inflation since the adoption of the directive. A further increase may be considered if there has been an increase of the holding of retail investors of securities.

6) The ICSD does not harmonize the funding systems of the schemes. Should the ICSD provide for some general principles concerning the funding of the schemes?

The experience gained from the financial crisis has demonstrated that guarantee schemes should be pre funded in order to provide a sufficient buffer for the scheme. Pre funding means that firms which trigger payments from the scheme will have contributed to the compensation scheme. Pre funding levels out the financial burden on the contributors to the compensation scheme.

7) Should loss events include also any losses suffered by (retail) investors as a consequence of the violation of conduct of business rules?

ICSD should cover private investors' cash and securities only. Widening the scope of the directive raises many questions with regard to the nature of the investor protection. Compensation in case of violation of conduct of business rules will change the nature of the scheme and complicate the operation of the schemes. It will become more difficult to determine the fees for funding the scheme in cases involving breach of rules on conduct of business – and notably on the risks associated with the cover.

8a) Does the legislation of the Member State you know the best provide mechanisms aimed at limiting compensation schemes' obligations over time? If yes, how many clients saw their compensation unpaid as a result of such mechanisms?

There are no such mechanisms in Denmark.

8b) Should this kind of mechanisms be prohibited?

Mechanisms of this sort should not be introduced in the directive. It should remain a national option.

9a) Should the process of recognizing the eligibility of the claim be regulated for the purposes of the ICSD ?

The directive could reflect the changes made in directive 2009/14/EC.

9b) Should, at least, a mechanism be introduced providing for provisional partial compensation based on a summary assessment of clients' positions?

A partial provisional partial compensation could be an option – and therefore unregulated. An obligation to compensate in more stages will increase the cost to the scheme and may delay the final/total payment of the compensation.

9c) Irrespective of the harmonisation of their funding systems, should compensation schemes ensure that they have minimum reserve funds in order to comply rapidly with any immediate needs ?

It is unclear what “any immediate needs” covers. An obligation of such a nature would easily become arbitrary and delay the processing of the payments of the compensations.

Should the scope of the directive be enlarged?

Widening the scope of the directive raises many questions with regard to the nature of the investor protection. ICSD should cover private investors’ cash and securities only. Inclusion of other services will complicate the operation of the schemes. Any extension of the scope of the ICSD to cover professional actors must be examined in depth. Our initial response is that the present scope of the ICSD should remain focused on retail investor protection.

1) Should the operation of multilateral trading facilities be excluded from the scope of the ICSD ?

The operation of multilateral trading facilities is a professional activity. There seems no need for protection because multilateral trading facilities are platforms and not investors.

2) Would it be appropriate to include in the scope of the ICSD all investment firms seeking authorisation to the provision of investment services, although their authorisation would not allow holding clients’ assets?

The provision of investment services, although their authorisation would not allow holding clients’ assets is a service which is different from holding securities. Such services differ significantly from the holding of securities. Widening the scope of the directive raises many questions with regard to the nature of the investor protection. Inclusion of other

services will complicate the operation of the schemes. Also inclusion of professional parties would complicate the operation of the schemes.

Including the said services will mean that the compensation schemes change status and that they enter fields similar to of redress schemes. Such a change in the operation of the schemes may lead to increased costs for the secretariats and to cross-subsidising on the new activities.

3) Would it be appropriate to include the scope of the ICSD all investment firms seeking authorisation to the provision of investment services, although they provide their services only to non-retail clients?

ICSD should cover private investors' cash and securities only. Widening the scope of the directive raises many questions with regard to the nature of the investor protection. Inclusion of other services will complicate the operation of the schemes. It seems highly likely that the contribution to the schemes must be increased if professional service providers become cover under the ICSD..

4a) Should investors be able to claim compensation in the case of default of the third party where their assets had been deposited?

Introduction at EU level of a right to claim compensation in the case of default of the third party where their assets have been held in custody raise several questions.

The increase in investments in shares from other Member States raise the question of protection of sub holdings by depositaries outside the Member State covered by the national ISCD. If the depository holds sub deposits with other depositories the protection may depend on national law in both the home Member State of the depository and the national law in the sub depository member states. In some cases the

securities may be covered by an ISCD scheme. In other cases there may be no cover.

The different situations for different types of securities should be clarified with regard to the actual cover. The cover may also depend on the form of the security – paper based or electronically / dematerialised registered. The protection may depend on the number of intermediaries and on their legal status as well. Similarly the way the security is held may lead to differences in the cover provided. The review should analyse differences in the treatment of sub holdings with depositaries outside the Member State of the investor.

A right to claim compensation in the case of default of the third party where their assets have been held will introduce unlimited liability on safe keepers. An obligation of this nature will consequently mean an unlimited liability for the guarantee scheme. An unlimited protection could have a spill over effect to deposits and require an unlimited guarantee for deposits.

The costs of any increase in the cover must be carefully considered.

4b) Should investors (such as UCITS or a UCITS unit holder) be able to claim compensation for loss of assets under the ISCD in those cases where the UCITS depositary or the institution which has been mandated to safe keep the assets, fail to perform its duty ?

Professional asset managers must be aware of the risks they are taking. It would be very expensive to establish a compensation scheme for loss of assets in case the depository fails to perform its duty.

5) Should loss events include also losses suffered by (retail) investors as a consequence of the violation of conduct of business rules?

ICSD should cover private investors' cash and securities only. Widening the scope of the directive raises many questions with regard to the nature of the investor protection. Inclusion of other services risks to complicate the operation of the schemes. Also inclusion of professional parties risks complicate the operation of the schemes. Compensation in case of violation of conduct will complicate the scheme. It is difficult to determine the fees for funding the scheme in cases involving rules of conduct. There is a risk that contribution for securities dealing will increase for the services offered under the directive.

10) Do you think special attention should be given to money market funds?

No.

11) Based on the concrete application of the ICSD do you see further issues other than the ones mentioned in the present document that might be of relevance to this analysis?

No.