Book-entry, Clearing and Settlement

Summary of the Report SOU 1993:114
Konto, clearing och avveckling
by the Clearing Inquiry

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Clearingutredningen

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Introduction

The Clearing Inquiry has in January 1994 presented its proposals in a report called SOU 1993:114 Konto, clearing och avveckling (Book-entry, Clearing and Settlement). The Clearing Inquiry has proposed that the reformed legislation should come into force January 1st 1995.

At first the proposals will be subjected to an extensive circulation for comment, in which various organizations, such as associations representing the different parties on the securities market, trade unions and employers' associations, courts and public authorities will be provided the possiblity to submit their views on the proposals. Upon the conclusion of the circulation for comment, the Government will decide which proposals are to be presented before the Parliament.

Summary of the Report

Background

Acting on a Government authorization, in January 1992 the Minister for Fiscal and Financial Affairs, Mr Bo Lundgren, commissioned Mr Johan Munck, Justice of the Supreme Court, to undertake a review of clearance, payment and delivery in the securities market. Experts from the securities market have assisted the inquiry, which has been named the Clearing Inquiry.

The background to the Inquiry was the lack of a comprehensive overview of the concluding functions in securities trading - clearance and settlement. The terms of reference required the Inquiry to map the forms of clearance and settlement that are currently used in Sweden, to study those in use abroad and to consider which system or systems are capable of managing the risks involved in clearance and settlement reliably and efficiently. Current rules and regulations for clearance and settlement were to be surveyed, with an appraisal of the need for uniform, general laws. The review was also to cover book-entry rules in the Share Accounts Act concerning equity and other securities.

The terms of reference stressed the importance of having Swedish rules for clearance, settlement and book-entry systems that are internationally adapted and which conform to international practice and international recommendations.

The situation in Sweden as regards book-entry systems, clearance and settlement in the autumn of 1993 was briefly as follows.

Equity is handled mainly in the VP system, a book-entry system managed by Värdepapperscentralen VPC AB, which is owned by the State (50 per cent), securities firms (25 per cent) and issuers (25 per cent). The VP system is a dematerialized system, based on the Share Accounts Act, and includes some clearing and settlement functions. VPC generates information on payments due on completed trades and control that payment precedes delivery of the securities in the VP system. But VPC does not participate as a counterparty or guarantor in the settlement of securities transactions. The settlement of payments is arranged in the banking system, first between the banks and the securities companies and finally in the central bank's clearing system.

In the money and bond market, the introduction of a modern book-entry and clearing system in Sweden has been discussed for a long time. In 1993 VPC initiated a new system for handling money-market instru-

ments that is a development of the VP system for handling equity. This was accompanied by a comprehensive adaptation of the instruments in question, including treasury bonds and bills and housing bonds.

SwedeSettle AB, which cooperates with the international clearing organization Cedel, is a new affiliate of the Postal Giro. In the spring of 1994 SwedeSettle plans to begin settlement operations for bonds and foreign securities, for instance.

OM Stockholm AB, a subsidiary of a listed company, OM Gruppen AB, is a marketplace and clearing organization for standardized options and futures. It manages the clearing and settlement of derivative instruments, e.g. equity options and equity futures, for which OM constitutes the marketplace, as well as of other instruments, primarily interest rate futures, for which OM is not a marketplace. OM also provides clearing services for further instruments such as swaps and FRAs. OM functions as a central counterparty in clearing and settlement operations.

The Share Accounts Act (1989:827) contains provisions concerning the registration of equity, bonds and a number of other instruments in a dematerialized book-entry system. The legal consequences associated with possession of the instrument in a conventional system are instead tied to the registration in book-entry system. VPC has the sole right to undertake registration based on the Share Accounts Act.

The Act (1992:542) governing Securities Echanges and Clearing Operations mainly regulates authorization for exchanges and marketplaces and also contains rules about the clearance of options and futures. The Act stipulates that clearing operations may be undertaken only by entities holding a licence as a clearing organization and also defines what is meant by clearing operations, clearing organization and clearing member. Chapter 8 sets forth the conditions for obtaining a licence as a clearing organization. Provisions concerning the operations of a clearing organization are contained in Chapter 9. Authorized exchanges and clearing organizations are supervised by the Financial Supervisory Authority.

In recent decades financial markets throughout the world have been involved in major changes. Familiar features of this process are the deregulation and internationalization of financial markets and the technical innovations in, for instance, computer and communication systems. Information about financial markets is now spread worldwide instantaneously. Another feature is the steady stream of new instruments. Notable changes have also occurred in trading techniques, accompanied by the entry of new participants, such as institutional investors, to markets that used to be the preserve of banks and securities companies. Other crucial tendencies, not least for clearance and settlement, are the increasingly strong links between markets and the blurring of market boundaries. Many finacial institutions are, moreover, active in more than one market, at home as well as abroad. The developments briefly outlined here have been accompanied by substantially increased market turnover and a rising value of the traded assets.

These factors and the associated changes, in conjunction with certain events, such as the worldwide share price fall in October 1987, have affected conditions for clearance and settlement. Simplifying somewhat, it can be said that, having previously attracted little attention as specialized activities for certain organizations and the back offices of banks and security firms, clearance and settlement have been spotlighted in the discussion of necessary changes in financial markets. This reflects both an awareness that these activities contain the most serious remaining risks in securities trading and an increased recognition of inherent risk.

One of the risks in financial markets is the domino effect - the possibility of a disturbance, for instance the inability of one participant to meet delivery or payment obligations, spreading to other participants in clearing activities as well as to other markets. Such a disturbance can conceivably threaten the overall stability of the financial system, a risk that is commonly known as systemic risk.

Clearance and settlement in Sweden and other countries

Clearance and settlement systems in Sweden and risk management in these systems have been mapped by the Inquiry in considerable detail. Particular attention has been paid to clearing and settlement procedures in equity, money and bond markets.

A study has also been made of clearing and settlement procedures in some of the main countries and regions. Conditions in Denmark, the United Kingdom and the United States were considered particularly relevant.

EC rules and regulations concerning clearance and settlement have likewise been studied. In this context the Inquiry notes that the two recently adopted directives, on investment services and capital adequacy, respectively, will no doubt be of major importance for future securities trading in the EEA and also affect the regulation of clearing in Sweden. It can be noted, for instance, that the directives regulate both the right of access to clearing and settlement systems and the criteria that may be set for this.

Another aspect considered by the Inquiry is the work on clearance and settlement that has been done by other international organizations, for instance the Group of Thirty and the G-10 Central Banks. The ongoing discussion of risks in currency trading and OTC trading in derivative instruments is also taken up. Turnover in these two respects is very large; in the spot forex market it has been estimated to average around USD 1,000 billion a day, while at end-1991 the nominal value of outstanding derivatives traded OTC was calculated to be almost USD 4,500 billion. Together with the derivatives in exchange trading, the aggregate total was almost USD 8,000 billion. The corresponding totals for equity markets and bond markets at that time were USD 10,000 billion and USD 15,000 billion, respectively.

Risks associated with clearance and settlement are discussed relatively fully in the report and the Inquiry presents measures for limiting risks.

The latter include systems that guarantee delivery versus payment, standards for the financial and operational strength of clearance organizations and their members, supervision of the members' trading positions, shorter settlement periods, efficient netting systems and standards for collateral requirements.

General considerations

Reliable and efficient systems for clearance and settlement are needed to enable securities markets to perform satisfactorily in every respect and earn the confidence of participants and the general public. These systems must be able to provide acceptable management of the risks involved in clearance and settlement, including credit and liquidity risks as well as operational risks. In addition, clearing and settlement in securities markets need to be arranged so that any crises which may arise can be managed within the system for clearing and settlement, minimizing the risk of the disturbance spreading to the financial system as a whole.

In the opinion of the Inquiry, clearance and settlement are of such central importance for securities markets that certain basic rules of operation should have the force of law. This is all the more warranted in that this is the aspect of securities market trading which poses the greatest risks for the financial system. These basic rules should provide incentives for making clearance and settlement reliable and efficient.

Statutory regulation cannot, however, replace the market's own rules and routines in this respect. The reliability of clearance and settlement is crucially dependent on the systems employed by the institutions for the management of the inherent risks. These systems must be capable of managing such risks in a satisfactory and responsible way. It is therefore essential that clearing organizations and their members allocate resources for an ongoing analysis and improvement of their risk-management systems.

Concerning the requirements for a clearance and settlement system, the Inquiry considers that the Group of Thirty Recommendations can serve in essential respects as criteria for how clearing and settlement ought to function. These are:

1. Comparison of trades between direct market participants (stock-exchange members, for instance) shall be accomplished by the trade date plus one day.
2. Indirect market participants (institutional investors, for instance) shall be members of a trade comparison system that achieves positive affirmation of trade details.
3. Each country shall have an efficient and fully developed central securities depository (CSD), organized and directed to encourage the broadest possible participation (direct or indirect).
4. Each country shall examine the size of and participation in its market in order to determine whether a netting system would be beneficial in terms of risk reduction and heightened efficiency. If a netting system is appropriate, it shall be implemented.
5. Delivery versus payment (DVP) shall be employed as the method for settling securities transactions.

6. Payments associated with securities settlements and the management of securities portfolios shall be rendered similar for all instruments and all markets by applying the convention that funds received are made available the same day (same-day funds).

7. A continuous settlement system shall be implemented in all markets. Final settlement shall occur by the trade date plus three days.

8. Securities lending shall be promoted as a method of expediting the settlement of delivery obligations in securities transactions. Existing legal or fiscal obstacles to securities lending shall be removed.

9. Each country shall implement the standard for securities messages that has been developed by the International Organization for Standardisation (ISO, ISO Standard 7775). In particular, all countries shall, at least for cross-border securities transactions, adopt the ISIN numbering system for securities as defined in ISO Standard 6166.

Concerning the VPC's new system for the money and bond market, the Inquiry sees a substantial benefit - fully in line with international recommendations (for instance from the Group of Thirty) and the requirements of modern securities markets - in the circumstance that also bonds and other money-market instruments now can be dematerialized in a book-entry system. For improved risk management the Inquiry finds it a natural development of VPC's system that market participants in some form or other assume a more juridical responsibility for settlement and risk management, accompanied by a clear allocation of liabilities.

The Inquiry also sees a benefit in capital contributions being made to VPC in the existing situation, as well as in a real increase in the guarantees pledged by participants. The Inquiry proposes (see below) that the State ultimately withdraws from its role as owner in VPC; if the ownership were then to be shared among the participants and issuers in the system, this would mean that those who are active in the VP system are also directly responsible for it.

At present VPC has the sole right to operate accounts in dematerialized financial instruments. The Inquiry proposes the abolition of this legal monopoly, accompanied by an amendment to the Share Accounts Act authorizing the Government or an authority nominated by the Government to make the provisions in the Act applicable also to other entities. Such an amendment would enable an entity that meets the necessary criteria to initiate new activities under the Share Accounts Act, for instance in money-market instruments or OTC shares.

The conditions for other companies operating book-entry systems in securities markets should in principle be the same as those which Parliament and the Government have laid down for VPC.

The role of the State as owner in book-entry systems is discussed in the report, partly with reference to a 1992 resolution by Parliament concerning the privatisation of state-owned companies. There is nothing to prevent the State, at least after some time, from disposing of its shareholding in VPC even if the preconditions specified in Parliament's resolution are not met. If the State chooses to retain an influence as owner, the Inquiry considers it would be most natural for the State to be represented by the National Debt Office.

The Share Accounts Act

As mentioned above, the Inquiry proposes that VPC's legal monopoly be abolished and that other entities also be enabled to register financial instruments in accordance with the Share Accounts Act. The Inquiry proposes further amendments to this Act and these are summarized here.

The Share Accounts Act specifies the financial instruments that VPC is entitled to register, with the attendant legal consequences. Experience from the period during which the book-entry system has been in use points to a need for an extension that goes beyond a specification of certain kinds of instrument to a formulation that is more general and flexible. The Inquiry therefore proposes that a possibility is provided under the Act of registering all the Swedish financial instruments that are traded in securities markets as well as such foreign financial instruments as are traded in Sweden.

In order to simplify cross-border trading and improve its reliability and efficiency, international recommendations call for cooperation between national CSDs. A report on Nordic stock-market cooperation has also underscored the importance of such cooperation being unobstructed in law. In the Internal Market of the EEA, moreover, a securities institution with a home-country authorization is to be free to perform investment services without discrimination in other member countries via branches or cross-border operations and also to have the right of access to clearing and settlement systems that undertake this function in the marketplace in question. In view of this, the Inquiry recommends an addition to the Share Accounts Act that expressly gives foreign companies - securities depositories and securities institutions, for example - a general possibility of becoming account-operating institutions.

The Inquiry also proposes that the rules concerning non-resident nominees be simplified. A single licence for equity should suffice, issued appropriately to the non-resident nominee. Apart from this, the Inquiry considers that a set of rules should not be created for nominee registration of other financial instruments, such as bonds.

In keeping with provisions in the rescinded Act about Money-Market Accounts, the Inquiry proposes that the right of an issuer, under the Share Accounts Act, to peruse accounts payable be restricted. Only in the event of an issuer needing information for payments to the creditors should the issuer be entitled to information about the creditors or the nominees managing pertinent instruments of debt. In addition, an issuer withdrawing from the book-entry system needs information about the identity of creditors.

Rules in the Share Accounts Act about compensation for damages are also discussed by the Inquiry, as are other minor issues raised by the review of that Act.

Clearance and settlement

The current statutory provisions in the Act governing Securities Exchanges and Clearing Operations are confined to clearance and settlement

in the sense of participating commercially as a party in option or forward trading or otherwise guaranteeing that the transaction is accomplished. Today in Sweden clearance in this sense is undertaken only by OM. Considering the importance for securities markets, as well as for the financial system, of having clearance and settlement operations that are reliable and efficient, the Inquiry finds that clearance operations which in one way or another involve appreciable risks should be subject to regulation and supervision.

An extension of the statutory concept "clearing operation" is proposed by the Inquiry, along with the introduction of a new concept, "settlement operation", and a provision that a licence shall be required for the performance of clearance and settlement operations. In view of the strong links between the currency and securities markets and the notable similarities, for instance as regards risks, between the clearing operations for currencies and financial instruments, respectively, the Inquiry proposes that a licence shall likewise be required for the clearance and settlement of currency transactions.

Clearing operation is defined as an operation undertaken on a continuous basis by a clearing organization whereby, on behalf of the clearing members, a balance is achieved of those members' commitments to pay in Swedish or foreign currency or to deliver financial instruments to one another or whereby such commitments are guaranteed by the organization becoming a party to the transaction or in some other way. Settlement operation as defined by the Inquiry is an operation undertaken on a continuous basis to ensure, on behalf of the clearing members, that commitments for them to pay in Swedish or foreign currency or to deliver financial instruments to one another are met by the transfer of money or instruments.

With these new definitions, a licence would be required for VPC's operations in this regard, as it would for the planned operations of SwedeSettle.

Clearing organizations

Beside possessing financial strength, a clearing organization must meet the criterion of reliability in a wide sense. This criterion includes high standards as regards organization, risk-management systems and technical systems. The operations must also rest on a firm legal base. The Inquiry finds the need for reliability so essential that it should be mentioned specifically in the law.

In the opinion of the Inquiry, one prerequisite for the operations of a clearing organization is a thorough and detailed analysis of risks in the planned operations. Instead of being confined to the risks run by the organization, this analysis should also cover the risks associated with the system as such for the parties concerned and consequently for the market and the payment system. Such a risk analysis provides a basis in turn for the plan that every clearing organization should draw up for the management of these risks.

Concerning the requirements connected with the risk-management system of a clearing organization, the Inquiry finds it essential that the organization possesses financial and operational integrity. The Inquiry also considers that the following requirements, spelled out in the study *Clearance and Settlement in U.S. Securities Markets*, can serve as a benchmark. Besides limiting losses and liquidity problems in the event of default by a clearing member, a risk-management system shall ensure that settlement can be accomplished in a timely fashion, with any losses covered by other members, and also provide the operational reliability of hardware, software and communication systems that is needed for the clearing organization to complete the settlement.

Together with its financial resources, the risk analysis, risk-management plan and organization plan for a clearing organization should be examined regularly as the scale of the operations grows or diminishes or conditions change in other respects.

The risk-management plan should clearly state how the institution's responsibility for risk management is allocated. The powers of the responsible unit should also be set forth, as well as which office-holder(s) is responsible for ensuring that, in the event of a crisis, the necessary measures are taken. In the arrangement of these matters consideration should also be paid to whether or not the unit responsible for risk management should be separate from the commercial units.

The risk-management plan and the responsibility for managing the risk in clearing and settlement operations are of central significance for clearing organizations, securities companies, banks and other entities in financial markets. In the Inquiry's opinion it is therefore important that the managements of such institutions are well aware of the risks associated with clearing and settlement operations and how these risks should be managed. Matters concerning the risk-management plan and the responsibility for managing risks should accordingly be decided at board level, at least as regards fundamental issues. Moreover, these decisions should be reviewed on a regular basis by the institution's board and executive management.

The Inquiry considers that the operations of a clearing organization shall be restricted to clearing and settlement functions and closely related activities, for example custodial services. In addition, with a separate permit from the Financial Supervisory Authority and in order to expedite the clearing operations, a clearing organization may arrange advances of financial instruments (securities lending) and extend credit against collateral. In the opinion of the Inquiry, a clearing organization should not be allowed to provide the administration of financial instruments belonging to another party, as these organizations should not be exposed to the risks such services may carry. With such an arrangement, moreover, the integrity of the clearing organization might be questioned.

Clearing members

A certain degree of financial strength is also required of institutions that participate in clearing. A clearing member likewise needs an appropriate organization, for instance as regards back-office operations. In order to meet commitments and maintain the necessary readiness, members must have systems for continuous monitoring of their current positions and exposures in financial transactions. A further requirement concerns well-founded and documented routines for risk management in order to avoid clearing and settlement problems. Reliable technical systems are also needed, for instance for data processing and communications. The Inquiry proposes that the eligibility criteria in the Act governing Securities Exchanges and Clearing Operations be specified so that the requirements outlined above have statutory force.

The Inquiry underscores the importance both of supervising clearing members and of the responsibility for this. Matters covered by the supervision should include the financial strength of clearing members, the organization of clearing operations, risk-management routines and technical systems. All parties with an interest in clearing and settlement should have an incentive to monitor counterparties and clearing organizations on a continuous basis. The clearing organizations in turn must monitor their members continuously in these respects. Finally, the central importance of clearing and settlement for the securities markets gives the supervisory authorities good reason to keep a close watch on the management of clearing and settlement issues.

As a means of enhancing the reliability of clearance and settlement, the Inquiry proposes a partly new right of pledge. As security for regressive claims on the purchaser, this gives a clearing organization or clearing member that has made a commitment, in accordance with current rules for clearance and settlement, to pay for another party's purchase of financial instruments, a right of pledge in the instruments provided these are in the possession of the organization. The right can also be held by a clearing organization or clearing member as security for claims arising from funds they have advanced to a party ceding financial instruments. As regards rights registered under the Share Accounts Act, it is necessary instead to register the right of pledge in accordance with that Act, though this is not required for rights registered with a nominee.

The Inquiry draws particular attention to the element of discretion in the supervision of clearing operations, above all when assessing existing risk-management systems, because opinions in this respect tend to differ. For reliable and efficient clearing and settlement it is therefore important that the Financial Supervisory Authority has adequate resources for this.

Netting

Netting consists in balancing delivery and payment commitments between two (bilateral netting) or more (multilateral netting) parties. It should be noted that a clear distinction cannot be made between netting and clearing, which are basically similar procedures.

Netting is a widely debated subject at present. As pointed out by central bank representatives for the G-10 countries, for instance, the efficiency of netting systems is important for the reliability of financial market transactions. A proposal to licence a wider range of bilateral netting for capital adequacy purposes was included in the draft amendment to the 1988 Capital Accord which the Basle Committee on Banking Supervision distributed in 1993. One of the minimum standards set out in the Lamfalussy Report is that netting schemes should have a well-founded legal basis under all relevant jurisdictions. In the United States and other countries, legislation has been used in an attempt to dispel any uncertainty about the legal robustness of netting contracts.

Benefits of netting

- By reducing the number of contracts in the final settlement procedure, netting can ease the operational pressures in the settlement, as well as those on the clearing system, besides cutting clearing and settlement costs.
- Netting can reduce the value of the settlement payments and hence the liquidity requirement and the risk from delayed payment.
- A netting scheme can also lessen problems in the timing of inward and outward flows of financial instruments and funds, thereby reducing settlement risks.
- Netting can lower exposures to counterparties and thereby the capital risk and replacement-cost risk.
- In some cases, finally, capital adequacy requirements can be diminished for participants in a netting arrangement that has supervisory recognition.

The discussion of netting risks has mainly focused on two problems. One concerns the robustness of a netting contract when a party to the contract defaults and the consequences of that default for the counterparties and for the transactions covered by the contract. Is the liquidator of a failed counterparty free to choose which transactions, if any, to complete (cherry-picking) and what are the consequences for forward obligations, such as contracts in futures and options, that are covered by the netting scheme? The other problem concerns the management of a failed counterparty's transactions in a multilateral netting scheme. If a partial or total reversal were to be necessary, it is considered that this might constitute a risk for the financial system as a whole.

The importance of efficient netting arrangements for financial markets, particularly as regards reliable and efficient settlement, prompted the Inquiry to examine the validity of netting agreements in Swedish law. No problems were found in this respect except possibly as regards the above issue which has attracted attention internationally, namely the onus on the estate of a bankrupt defaulter to meet future obligations.

An estate in bankruptcy has no obligation and is normally not in a position to perform all the debtor's undertakings. But this does not mean that the estate is debarred from entering into an agreement by taking over

the rights and obligations of the bankrupt debtor. Such a right of entry is expressly provided in the first paragraph of Article 63 of the Sales of Goods Act, with the addition that, if so requested, the estate has to give reasonable notice and also provide collateral.

The counterparties in the clearing are accordingly at risk in that the liquidator, acting in the interests of the creditors, chooses to perform the transactions that seem beneficial to the estate and annul the others. For the other participants in the clearing procedure, as well as for the system as such, this can produce situations that are very difficult to resolve. Such difficulties are commonly avoided, particularly in international standard agreements, by adopting a clause (known as a close-out agreement) whereby any participant's bankrupt estate is excluded from the procedure, that is to say, the final settlement with the bankrupt or his estate has to be made by the date of the bankruptcy or the day before.

The validity of such an agreement in Swedish law is uncertain. Agreements of this type are used in many contexts, not only in connection with purchases but also in leasing and contracting. The Inquiry finds weighty reasons in favour of the opinion that an estate in bankruptcy is normally bound by an agreement of this nature. However, the complexity of the issues rules out a general conclusion that a particular opinion is definitely correct; different solutions are conceivably applicable to different types of agreement. With reference to clearing, the reasons for considering that an agreement of this type would be binding on an estate in bankruptcy are particularly strong in that it would not be reasonable in practice to permit partial departure from agreements in that context. While the Inquiry holds this opinion, the matter clearly has to be indisputable, not least in international circumstances. As there is no Supreme Court ruling to provide guidance, certainty can only be achieved through legislation.

Under these circumstances the Inquiry proposes a rule to the effect that an estate in bankruptcy shall be bound by a restriction in a clearing agreement which precludes the bankrupt estate of a clearing member or of a clearing organization from continuing to participate in the netting of obligations. The implication of the proposed rule is that, where an agreement of this kind exists, the bankrupt's estate may not participate in the clearing operations or that outstanding obligations are to be settled.

The matters considered above also apply, in principle, when bilateral netting agreements are made without involving any clearing operations. While there is then no clearing as defined by the Inquiry, the validity of a close-out restriction is still rather uncertain. The Inquiry finds predominant reasons for regulating this situation, too, and sees no decisive objection to this being done in the same provision. The solution should clearly be the same as for agreements involving a clearing organization.

The Lamfalussy criteria can serve as a reference for appraising clearance and settlement systems which involve netting of payment and/or delivery obligations. It should be noted that the criteria, which are reproduced here, were drawn up as minimum standards.

1. Netting schemes should have a well-founded legal basis under all relevant jurisdictions.
2. Netting scheme participants should have a clear understanding of the impact of the particular scheme on each of the financial risks affected by the netting process.
3. Multilateral netting systems should have clearly defined procedures for the management of credit risks and liquidity risks which specify the respective responsibilities of the netting provider and the participants. These procedures should also ensure that all parties have both the incentives and the capabilities to manage and contain each of the risks they bear and that limits are placed on the maximum level of credit exposure that can be produced by each participant.
4. Multilateral netting systems should, at a minimum, be capable of ensuring the timely completion of daily settlements in the event of an inability to settle by the participant with the largest single net debit position.
5. Multilateral netting systems should have objective and publicly disclosed criteria for admission which permit fair and open access.
6. All netting schemes should ensure the operational reliability of technical systems and the availability of backup facilities capable of completing daily processing requirements.

Mutual funds

The Inquiry proposes that mutual fund companies be enabled to use the rules of the Share Accounts Act. This can be done by resorting for this purpose to VPC or possibly another separate entity with the appropriate permit. An alternative would be for depositories as well as mutual fund management companies to obtain a permit to register mutual fund holdings in accordance with the Share Accounts Act. In both these cases the Share Accounts Act would be generally applicable to mutual fund holdings, giving a rule system that is unambiguous as regards property law. In the event of a mutual fund company not wishing to switch to procedures under the Share Accounts Act, the Inquiry proposes an amendment to *the Mutual Funds Act (1990:1114)* that expressly refers to the provisions of the Promissory Notes Act concerning registred securities; in that way the present legal situation - as perceived by the Inquiry - would be retained.

The Inquiry also proposes that it should be possible for mutual fund holdings to be registered by nominees. If the rule system of the Share Accounts Act is made applicable to securities funds, this will include the provisions concerning nominee registration. For mutual fund companies that prefer to refrain from applying the rules in the Share Accounts Act, the Inquiry proposes that rules on nominee registration are incorporated in the Mutual Funds Act.

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