

**THE FINALITY DIRECTIVE 98/26/EC of the EUROPEAN PARLIAMENT,  
WITHIN THE PORTUGUESE LEGAL SYSTEM**

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THE PRINCIPAL OF THE RELEVANT INTERMEDIARY APPROACH (PRIMA) consecrated in EU Directive 98/26/EC of European Parliament and of the Council of 19 May 1998, ARTICLE 9 NUMBER 2, was introduced to Portuguese legislation by Decree-Law 486/99 13th November that enacted the new Securities Code. Decree-Law 221/2000 adopts the contents of the same Directive where it disposes about the definitive character of the financial transactions carried out within the securities settlement and payment systems. Bank of Portugal Internal regulation 8/2000 stipulates, within the scope of the same Directive, article 10, which will be the securities settlement and payment systems that will benefit from irrevocability of transfer orders and enforceability of guarantees posted to participants of the European System of Central Banks, in case of systemic risk.

The legal risks associated with the taking of securities as collateral, mostly when these securities are held through several layers of intermediaries, crossing a few borders, led to the making of arrangements within the financial services industry. The amount of securities provided as collateral under these arrangements are very high, and so is the risk associated with these transactions. Collateral takers need to be sure that they have enforceable rights to the securities posted as collateral, and that these rights are good against not only the providers, but also against third parties. For that, collateral takers have to be certain which law (of which jurisdiction) is applicable. The interests over securities are credited to an account in the books of an intermediary and these interests are provided as collateral to the intermediary, who will, probably, provide these interests to his customers, and most of the time, in cross border operations. Directive 98/26/EC of the European

Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems, the so-called Finality Directive, intended to reduce the risk associated with participation in securities settlement systems and enforceability of collateral securities. By collateral securities the Directive comprises all means provided by a participant to other participants in the payment and/or securities settlement systems to secure rights and obligations. PRIMA helps determine the applicable law and gives certainty to transactions.

PRIMA is consecrated in Article 9 number 2 of the Finality Directive in terms that whenever securities (including rights in securities) are held as collateral security to participants, Central Banks of the Member States or to the European Central bank, the law governing such rights will be the one where such rights are recorded in a register, account or centralised deposit system located in a Member State,. Under PRIMA, only the requirements of one law need to be satisfied, to obtain valid legal entitlement to the collateral. Collateral takers can determine the validity and priority of the collateral taker entitlement by looking at the law of the relevant intermediary. Under PRIMA one can determine the law territorially applicable to the securities put up as collateral.

PRIMA was implemented in Portugal through articles 41-b) and 284 number 4 of the new Securities Code (Decree-Law 486/99 of 13th November 1999). Under the provisions of article 41-b), transmission of rights and the establishment of collateral on securities that are registered or deposited, but which are not integrated into a E.U. centralised system, will also be regulated in accordance with PRIMA, by the laws of the state where those securities are registered or deposited. In applying PRIMA, article 284 number 4 stipulates that in the event securities given as collateral are registered or deposited in a centralised system, which is located or operating in a Member state of the EU, the determination of the guarantee's beneficiaries is governed by the legislation of the Member State, where the guarantee is registered or deposited.

Through Decree-Law 221/2000 of 9 September the Portuguese Legal system adopted the Finality Directive with regard to settlement payment systems, in terms that, transfer orders and netting are legally enforceable and, even in the event of insolvency proceedings against a participant, binding on third parties, provided that transfer orders enter into a system before the moment of the opening of such insolvency proceedings. The moment of entry of a transfer order into a system is defined by the rules of that system.

Article 13° of the same Decree-Law 221/2000 stipulates that whenever systemic risk is justified, Bank of Portugal must determine which settlement systems will benefit from the irrevocability of transfer orders and the enforceability of the collateral posted to participants or to banks that are aggregated in the European System of Central banks(SEBC).

Bank of Portugal Internal regulation number 8/2000 indicates these settlement systems, which are the following: i) Large Transactions Payment Systems (Sistema de pagamentos de grandes transacções) (SGPT); ii) Netting between Banks Systems (Sistema de compensação interbancária)(SICOI); and, iii) Other Depositors Settlement System (Sistema de liquidação de outros depositantes)(SLOD).

The finality directive intending to reduce the risk associated with participation in securities settlement systems, ensures the reduction of systemic risk and guarantees irreversibility of clearance and enforceability of guarantees constituted by their participants within the scope of their participation within the system. "