

# Legally required participant disclosure

---

## 1 Introduction<sup>1</sup>

The purpose of this document is to disclose the levels of protection associated with the different levels of segregation in respect of securities held directly for clients with Central Securities Depositories (CSDs) within the European Union (EU), including a description of the main legal implications of the respective levels of segregation offered and information on the insolvency law applicable.

This disclosure is required under Art. 38(6) of the Central Securities Depositories Regulation (CSDR) in relation to CSDs domiciled in the EU.

This document is not intended to constitute legal or other advice and should not be relied upon as such. You should seek your own legal advice if you require any guidance on the matters stated herein.

---

## 2 Background

In our own books and records, we record each client's individual entitlement to securities that we hold for that client in a separate client account. We also open accounts with a CSD in our own name (or in our nominee's name) in which we hold clients' securities. As a general rule, we currently make two types of accounts with CSDs available to clients: Individual Client Segregated Accounts (ISAs) and Omnibus Client Segregated Accounts (OSAs).

An ISA is used to hold the securities of a single client and therefore the client's securities are held separately from the securities of other clients and our own proprietary securities. An OSA is used to hold the securities of a number of clients on a collective basis. However, we do not hold our own proprietary securities in OSAs.

---

## 3 Main legal implications of levels of segregation

### Insolvency (bankruptcy)

If a Swiss bank were to become insolvent, the insolvency proceedings would take place in Switzerland and be governed by Swiss insolvency law. Nevertheless, non-Swiss branches of a Swiss bank may also be subject to insolvency proceedings in the

foreign location in question governed by local insolvency law. Were we to become insolvent, insolvency proceedings relating to our Guernsey branch may also take place in Guernsey and be governed by Guernsey insolvency law.

Clients' legal entitlement to the securities that a Swiss bank holds for them directly with a CSD would generally (except in specific circumstances, some of which are discussed below) not be affected by the bank's insolvency (bankruptcy), regardless of whether those securities were held in ISAs or OSAs.

In practice, the exclusion of securities from a Swiss bank's bankruptcy estate would further depend on a number of additional factors, the most relevant of which are discussed below.

### Exclusion from our bankruptcy estate

#### Swiss law

Under Swiss insolvency laws, intermediated securities and certain other safe custody assets within the meaning of the Banking Act booked on safekeeping accounts held by clients with a Swiss bank, as well as certain readily available claims of the bank to receive delivery of securities from third parties, do not form part of the bankruptcy estate. Instead, in an insolvency (bankruptcy) of a bank, they are designated to be excluded in favour of the relevant client, subject to any claims the bank has against the client.

According to Art. 11 FISA, a Swiss bank must hold with itself or with a sub-custodian or a CSD intermediated securities (available securities) in a quantity and of a kind at least equal to, the total of intermediated securities credited to the securities accounts maintained by the bank for its clients<sup>2</sup>. A bank is also subject to strict requirements as to maintenance of accurate books and records and as to reconciliation of its records against those of the CSDs and sub-custodians with which the intermediated securities are held.

1. At the end of this documents is a glossary explaining some of the technical terms used in the document.

2. Available securities also include the bank's readily available rights to delivery of intermediate securities from other custodians during the regulatory or customary settlement period for the corresponding market, provided that this period does not exceed eight days.

Accordingly, as long as a bank maintains sufficient holdings of intermediated securities in accordance with its statutory obligations, clients should receive the same level of protection in the bank's insolvency, regardless of whether the intermediated securities are held in an ISA or an OSA. However, ISA could contribute to swifter identification of client assets in a default scenario.

### **Guernsey law**

Under Guernsey insolvency law, securities that we held on behalf of clients would not form part of our estate on insolvency for distribution to creditors, provided that they remained the property of the clients. Rather, they would be deliverable to clients in accordance with each client's proprietary interests in the securities.

As a result, it would not be necessary for clients to make a claim in our insolvency as a general unsecured creditor in respect of those securities. Securities that we held on behalf of clients would also not be subject to any bail-in process (see glossary), which may be applied to us if we were to become subject to resolution proceedings (see glossary).

Accordingly, where we hold securities in custody for clients and those securities are considered the property of those clients rather than our own property, they should be protected on our insolvency or resolution. This applies whether the securities are held in an OSA or an ISA."

### **Nature of clients' interests**

Although client's securities are held in Bank's name at CSDs, Bank holds them on behalf of Bank's clients.

For securities that are held in a CSD, the nature of the entitlement embodied in a security also depends on the law, regulations and contractual framework applicable to such other CSDs and further parties involved in the custody chain. In such a case, entitlements that are available for exclusion may be limited to contractual claims against a CSD involved. Moreover, the ability of the client to exclude securities in the case of insolvency may depend on whether a CSD or any custodian in the custody chain could assert any right to set-off, retention right, security interest or similar right with respect to the securities (see also "Security interests" below).

### **Shortfalls**

As described above, the statutory requirements are designed to ensure that a Swiss bank holds intermediated securities in a quantity and a kind at least equal to the intermediated securities credited to client accounts. If notwithstanding these requirements there were a shortfall between the number of intermediated securities that a bank is obliged to deliver to clients and the number of intermediated securities that the bank holds on their behalf in either an ISA or an OSA, this could result in fewer intermediated securities than clients are entitled to being returned to them on the bank's insolvency. The way in which a shortfall could arise and would be treated may be different as between ISAs and OSAs.

### **How a shortfall may arise**

A shortfall could arise for a number of reasons including as a result of administrative error, intraday movements or counterparty default. In most cases a shortfall occurs as a result of a mismatch between the time when a bank receives intermediated securities and the earlier time when the delivery is booked to the account of the receiving account holder. In Switzerland, typically for exchange traded transaction, banks credit the client accounts immediately on trade date while the effective delivery may not occur intraday but later (most markets have settlement cycles of 2 or 3 days). As a result, a recipient client could dispose of its intermediated securities as soon as they are credited to its securities account, irrespective of whether the bank has actually already received the intermediated securities. This process is referred to as contractual settlement. Contractual settlement may therefore cause a difference between the bank's number of intermediated securities at the CSD and the clients' higher number of aggregated securities credited to their securities accounts. In the normal course of the settlement this process-immanent difference disappears at the end of the settlement cycle. Contractual settlement increases market liquidity, accelerates deliveries and settlement, and is based on the fact that a failed settlement of an exchange traded transaction (and the risk that, as a result, a bank does not hold sufficient available securities) is rare. The risk involved with shortfalls is further mitigated by the fact that, if a shortfall arises, a bank is obliged to acquire without delay securities if and to the extent the total number of available securities is less than the total number of securities credited to clients' accounts (see below). In the case of an ISA, the securities held in the ISA can only be delivered out for the settlement of transactions made by the ISA client. As a matter of principle, this may reduce the risk of a shortfall in that account, but also increases the risk of settlement failure which, in turn, may incur additional costs (e.g. buy-in costs) and/or delay in settlements.

### **Treatment of a shortfall**

In the case of an ISA, although arguments could be made that the relevant client should not be exposed to a shortfall that is clearly attributable to an account held for another client or clients, it cannot be excluded that a shortfall on any other (ISA or OSA) account would be shared rateably among clients, including clients who do not have an interest in the relevant account<sup>3</sup>. Accordingly, a client holding whose securities are held in an ISA may still be exposed to a shortfall on an account held for another client or clients.

In the case of an OSA, a shortfall attributable to the OSA would be shared rateably among the clients with an interest in the OSA (and potentially other clients). Therefore, a client may be exposed to a shortfall even where securities have been lost in circumstances which are completely unrelated to that client.

3. Cf. Art. 19 FISA.

If a shortfall arises, the bank has the obligation under Swiss law to acquire without delay securities if and to the extent the total number of available securities is less than the total number of securities credited to clients' accounts. If a shortfall arose and was not so covered, clients may have a claim for compensation against a Swiss bank. Furthermore, if the securities that may be excluded from the bank's bankruptcy estate (see above) are not sufficient to satisfy the claims relating to client accounts in full, securities of the same kind held by the bank for its own account will also be excluded for the benefit of the relevant clients.

If a Swiss bank were to become insolvent prior to covering a shortfall, clients would rank as general unsecured creditors for any amounts owing to them in connection with such a claim. Clients would therefore be exposed to the risks of a Swiss bank's insolvency, including the risk that they may not be able to recover all or part of any compensation claimed. In order to calculate clients' shares of any shortfall in respect of an OSA, each client's entitlement to securities held within that account would need to be established as a matter of law and fact based on the bank's books and records. The shortfall would then be allocated among the clients as described above. It may therefore be a time-consuming process to confirm each client's entitlement and establish the securities available for exclusion. This could give rise to delays in returning securities and initial uncertainty for a client as to its actual entitlement on an insolvency.

---

## 4 Security interests

### Security interest granted to a CSD

Where a CSD benefits from a security interest (either it benefits from a statutory right or a contractual right based on its terms and conditions) over securities held by the bank with it (including securities held for clients), there could be a delay in the return of securities to a client (and a possible shortfall) in the event that the bank failed to satisfy its obligations to a CSD and the security interest was enforced. This applies regardless of whether the securities are held in an ISA or an OSA. However, in practice, we would expect that a CSD would first seek recourse to any securities held in the Bank's proprietary accounts to satisfy the bank's obligations and only then make use of securities in client accounts. We would also expect a CSD to enforce its security rateably across client accounts held with it. Furthermore, Swiss law requires the liquidator to satisfy claims of the CSD arising out of the custody of intermediated securities or the financing of their acquisition.

### Security interest granted to third party

Where a client purported to grant a security interest over its interest in securities held in an OSA and the security interest was asserted against the CSD with which the account was held, there could be a delay in the return of securities to all clients holding securities in the relevant account (and a possible shortfall in the account). However, in practice, Bank would expect that the beneficiary of a security interest (pledgee) over a client's securities would perfect its security by notifying Bank rather than a CSD and would seek to enforce the security against Bank rather than against the CSD, with which it had no relationship.

## CSD disclosures

Set out below are links to the disclosures made by CSDs in the EU in which Bank is a Participant:

<https://my.euroclear.com/eb/en/reference/csdr---euroclear-bank.html>

If you click on this link, you leave this information/website. These disclosures have been provided by relevant CSD. Bank has not investigated or performed due diligence on the disclosures and websites and clients rely on the CSD disclosures and websites at their own risk.

## Glossary

<b>Central Securities Depository (CSD)</b>	Is an entity within the European Union which records legal entitlements to dematerialised securities and operates a system for the settlement of transactions in those securities.
<b>Central Securities Depositories Regulation (CSDR)</b>	Refers to EU Regulation No 909/2014 on improving securities settlement in the European Union and on central securities depositories, which sets out rules applicable to CSDs and their participants. The CSDR is relevant for the European Economic Area (EEA) and is under scrutiny for incorporation into the EEA Agreement. Upon completion of the adoption process it will also be in force in the EEA.
<b>Federal Act on Banks and Savings Banks (Banking Act or BA)</b>	A Swiss law which sets out the financial market legislation governing banks, private bankers and savings banks, dealing, amongst others, with operating licences and specifying rules for business conduct.
<b>Federal Act on Intermediated Securities (FISA)</b>	A Swiss law which regulates the custody of certificated and uncertificated securities by custodians and their transfer.
<b>Individual Client Segregated Account (ISA)</b>	Is used to hold the securities of a single client.
<b>Omnibus Client Segregated Account (OSA)</b>	Is used to hold the securities of a number of clients on a collective basis.
<b>Participant</b>	Means an entity that holds securities in an account with a CSD and is responsible for settling transactions in securities that take place within a CSD.

## Graphic representation of OSA and ISA

OSA (example with three clients  $C_1 - C_3$ )



ISA (example with client  $C_1$ )



### CREDIT SUISSE AG GUERNSEY BRANCH

Helvetia Court  
Les Echelons  
St Peter Port  
Guernsey GY1 3YJ  
**credit-suisse.com**

The information presented in this document is provided for informational purposes only. Nothing contained in this document is intended and should not be construed as tax, accounting or legal advice. The information provided was produced by Credit Suisse AG Guernsey Branch ("Credit Suisse") with due care and to the best of its knowledge and belief. Any information including facts, opinions or quotations, may be condensed or summarised and is expressed as of the date of writing. The information may change without notice. Credit Suisse does not accept any responsibility or liability (whether in contract, tort or otherwise) for any loss or damage, which may arise directly or indirectly from use of or reliance on such information presented in this document. Your personal data will be processed in accordance with the Credit Suisse Privacy Policy published at <https://www.credit-suisse.com/gg/en/legal/privacy-statement.html>. Credit Suisse AG Guernsey Branch is authorised and regulated by the Guernsey Financial Services Commission. If you have any questions, please contact your Relationship Manager.

© 2019, CREDIT SUISSE AG GUERNSEY BRANCH

DES 000344 | December 2019