

Modernising the settlement of Money Market Instruments

Consultation Document

September 2002



HM TREASURY

**MODERNISING THE SETTLEMENT OF MONEY MARKET
INSTRUMENTS**

Part 1 - The Issue

Introduction

This consultation paper introduces and seeks views on new draft changes that the Government proposes to make to the Uncertificated Securities Regulations 2001 (the USRs – attached at Annex A)¹ in order to permit the evidencing and transfer of title of dematerialised equivalents of Money Market Instruments (MMIs) (to be known as “eligible debt securities” (EDSs))² through the CREST system³. A comprehensive and strong legal framework in relation to uncertificated securities helps financial stability, improves the competitiveness of the UK’s financial sector, and ultimately, helps lower the cost of capital for companies (and Government) in the United Kingdom.

2. To this end, there has been a rolling programme of amendment of the USRs. They were first introduced in 1995 for the commencement of settlement in CREST of equities and corporate bonds and extended to include gilts in 2000. The 2001 Regulations provided for Electronic Transfer of Title (ETT) and facilitated full real-time Delivery versus Payment (DvP) in central bank money. Wholesale changes to the current regulations are not considered necessary in order to integrate eligible debt securities, but some amendments are essential if the UK securities settlement infrastructure is to continue to compete and take advantage of the opportunities for market developments over the next few years.

¹ SI 2001/3755

² Previous consultations have referred to money market instruments: however to help make a distinction between money market instruments and their dematerialised equivalents the draft regulations avoid the words “money market instrument” preferring “eligible debt security”.

³ The USRs refer to a “relevant system”: CREST is the only system approved at present but there might be others in the future.

Securities Settlement Priorities Review

3. The Government's proposals are being published in the light of the Bank of England's Securities Settlement Priorities Review (SSPR)⁴ and the programme that it set out for the development of the UK securities settlement infrastructure in the medium to longer term. The key strategic recommendations of the SSPR were:

- a) that the Central Gilts Office (CGO) and CREST should merge, and that full merger should be preceded by CRESTCo assuming responsibility for operating CGO and the Central Moneymarkets Office (CMO);
- b) that the introduction of full scale DvP with payment effected in real time central bank money, was a desirable and important development;
- c) that money market settlement arrangements should be further developed and should as far as possible be integrated with gilt and equity settlement arrangements.

4. The first two of these objectives have been accomplished. Responsibility for the CGO was transferred from the Bank of England to CRESTCo on 24 May 1999, responsibility for the CMO transferred on 20 September 1999 and the integration of the CGO into the CREST system took place on 3 July 2000. ETT and DvP in central bank money were introduced into CREST on 26 November 2001.

5. The three Bank of England publications on "The Future of Money Market Instruments" (November 1999, March 2000 and January 2001) and CRESTCo's consultation paper on "Money Market Instruments in CREST" of January 2001⁵ have produced positive responses from market participants in favour of allowing these securities to be issued in electronic form, title to be evidenced by names on an electronic register and their integration into the CREST settlement system. In the light of this the Treasury has held discussions with the Bank of England, the UK Debt Management Office and CRESTCo and the new draft Regulations reflect their comments. The Treasury is very grateful to those who have contributed to these discussions.

⁴ Securities Settlement Priorities Review: Bank of England, 18 September 1998

⁵ Available on the Bank and CRESTCo's website.

6. On 4 July 2002, CRESTCo announced its intention to merge with Euroclear plc, the International Central Securities Depository based in Brussels. This was confirmed at Extraordinary General Meetings of CRESTCo and Euroclear shareholders on 16 August. The merger is expected to take effect on 23 September 2002. The merger proposals recognised the critical importance of the dematerialisation of MMIs into CREST which will be unaffected by these changes to CRESTCo's corporate structure.

Legislative Route

7. The Treasury has the powers to:

‘... make provision by regulations for enabling title to securities to be evidenced and transferred without a written instrument.’

This provision is contained in section 207 of the Companies Act 1989 (as amended by the Bank of England Act 1998).⁶ This power is subject to the constraint that, as far as is practicable, the rights and obligations relating to securities to which title is evidenced and transferred without a written instrument should correspond with those that would arise if the security were (in the present context) a negotiable paper instrument. In keeping with this restriction, other legislation, principally the Treasury Bills Act 1877 and The Local Authority and Housing Act 1989 (and regulations made under them) will need to be applied (in modified form) to the dematerialised versions of money market instruments issued by the Treasury, and by local authorities respectively.

8. As currently drafted, the amended regulations will come into force the day after the day on which they are made⁷. Depending on the responses to this consultation we hope to lay the regulations before Parliament in the first half of 2003.

⁶ Section 35, The Bank of England Act 1998: “Section 207 of the Companies Act 1989: bearer securities, 35. In section 207 of the Companies Act 1989 (power to make regulations enabling title to securities to be evidenced and transferred without a written instrument), there is inserted at the end – “(10) In subsection (1), the reference to transfer without a written instrument includes, in relation to bearer securities, transfer without delivery.””

⁷ i.e. signed by Lords Commissioners of HM Treasury. Before the regulations can be made they have to be approved by a resolution of both Houses of Parliament (see section 207(9) of the Companies Act 1989)

Next Steps

9. Comments on the proposals generally or on any particular aspect of them would be welcomed. When commenting, respondents should give details of any organisation whose views they represent. It will be assumed unless indicated to the contrary, that respondents have no objection to their response being shared with CRESTCo, the Bank and the DMO and made public. Responses should be submitted by 6 December 2002 to:

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10. Further copies of the consultation document may be obtained from Sue Cook on 020 7270 4345 or by email at sue.cook@hm-treasury.gsi.gov.uk. This consultation document may also be viewed on the Treasury's website at <http://www.hm-treasury.gov.uk>.

Part II – A proposal for modernising the settlement of MMIs

Background

11. Money Market Instruments⁸ are debt securities most of which have an original maturity of less than one year (although some securities regarded as MMIs such as some CDs, do have a maturity of over a year)⁹. They are transferable, marketable instruments creating or evidencing debt and issued by the borrower. Given the short maturities of the instruments many of them are discount securities, issued at a discount to par, rather than carrying a coupon (although the majority of certificates of deposit (CDs) are issued with a coupon). A key characteristic is that they are negotiable bearer instruments i.e. paper instruments whose title passes by physical delivery. (However, some are already dematerialised in the CMO by deed of covenant and contractual agreement). Unlike gilts (bearer gilts apart) or other bonds (bearer and other negotiable bonds apart) they are not registered instruments, and their transfer does not require a written instruction.

12. MMIs are used to meet the short term funding needs of the Government, financial institutions and companies as well as to assist banks and investment firms to manage their liquidity by holding suitable short-term assets. MMIs, in particular CDs, are also sought after as collateral for stock or cash lending.

13. The transfer and settlement of most MMIs currently takes place through the Central Moneymarkets Office (CMO) system run by CRESTCo, with the paper instruments held immobilised with the Bank of England acting as CMO depository under arrangements made between the Bank of England and CRESTCo. Other paper instruments are transferred outside the CMO system through other settlement arrangements or bilaterally, or alternatively held securely until maturity. This paper

⁸ Money Market Instruments include: Treasury Bills; Certificates of Deposit; Commercial Paper; Bankers' Acceptances and Local Authority Bills (it is proposed that Trade Bills, as with Letters of Credit, will not be available in dematerialised form in CREST).

⁹ It should also be noted that the dematerialisation proposals are concerned with money market instruments and other negotiable instruments with a longer maturity, which are also securities in terms of section 207 of the Companies Act 1989, including potentially such negotiable bonds as Medium-Term Notes (on the assumption that they otherwise satisfy the requirements of an "eligible debt security").

based system involves considerable printing costs as well as costs of storing paper securely for issuers.

14. Payment for transfers of MMIs are made by the CREST settlement banks on behalf of their CMO member customers. Such payments by settlement banks are not assured and the CMO does not offer full DvP in central bank money. This entails an additional risk with large intraday credit exposures being run by members.

Eligible Debt Securities

15. Against this background, the Government supports changes to allow EDSs (eligible debt securities), MMI equivalents, to be issued in dematerialised form and settled in CREST with CREST keeping an electronic register of title.

16. EDSs held within CREST would serve the same economic functions as their MMI equivalents, but would be distinct in several important respects. MMIs are paper, negotiable securities (see paragraph 19); EDSs will be electronic, registered instruments. MMIs are non-fungible (see paragraph 20); EDSs will be fungible where they are part of the same issue. There will also be a distinction in respect of the terms of issuance. For example, the electronic equivalents of Bankers' Acceptances, Certificates of Deposit and Commercial Paper will need issuance terms to be set out, probably in a deed. It is envisaged that in principle all issues of EDSs by an issuer could be under a single deed, albeit with specific notices of issue for particular issues. These would specify the issuer's obligation to the holder, the amount, maturity date, coupon, if any, and other terms of issue, any guarantee arrangements and state the type of EDS. The Bank of England will shortly be issuing for consultation some draft standard issuance terms for the main types of EDS.

17. The Government supports settlement of EDSs in CREST as it would provide full DvP in central bank money both in sterling and euros against simultaneous transfer of legal title and reduce the current large intraday exposures of the settlement banks to each other, further minimising settlement risks. It would also ensure that settlement of eligible debt securities was consistent with CPSS-IOSCO¹⁰ recommendations on

¹⁰ The Committee on Payment and Settlement Systems (CPSS) of the Group of Ten central banks and The Technical Committee of the International Organization of Securities Commissions (IOSCO)

securities settlement systems. Settlement in CREST would also generate substantial efficiencies and cost savings by creating a single settlement platform for EDSs, gilts and equities.

18. Currently most MMIs are issued in paper form (apart from some CDs). Consultation has indicated that given the wholesale nature of MMIs there is no market demand for an interface in CREST between paper holdings and registered CREST holdings. Therefore, CREST will not provide a paper interface. The only way in which an EDS will be able to be converted to a paper MMI will be if the particular issuer (through its Issuing and Paying Agent (IPA)) was willing to provide the service of withdrawing it from CREST and issuing a new paper instrument. Unlike non-material gilts and their paper equivalents, non-material EDSs will have different legal characteristics from their paper MMI equivalents.

19. Currently MMIs are negotiable. (Negotiability confers property rights on transferee holders that are superior to those conferred only by contract, in particular the right to take title free of any preceding equities). But this concept would no longer be relevant once MMIs are registered securities in CREST. Instead legal title to EDSs will be provided to the holder by the entry of his name on the “Operator register of eligible debt securities” operated by CREST. Like equities and gilts a change in the register would represent a change in legal title i.e. Electronic Transfer of Title (ETT). The advice given by Counsel in November 1999 confirms that the quality of title given to securities transferred through CREST is as good as the title given on delivery of a negotiable instrument.¹¹

20. Currently MMIs are not fungible (i.e. each unit is unique and cannot be used interchangeably) because each MMI is a separately identifiable bearer instrument. EDSs would not be unique, negotiable instruments and would be issued as fungible units of a registered security. The Government supports the view that fungibility could increase the flexibility for the issuer of the securities and so allow better tailoring to the needs of both investors and issuers.

¹¹ See Appendix II of the Bank of England’s paper on the Future of Money Market Instruments: November 1999: “A person taking a transfer of a security through the CREST system was therefore in at least as good a position as regards notice of defects in title as a person to whom a paper negotiable instrument was negotiated ...”

21. The new EDSs will be similar to debt securities already issued into CREST except that there will be no legislative provision for the possibility of their being registered outside CREST, and many will not carry coupons but instead will be discount securities. Currently paper bankers' acceptances are "two-name paper" with obligations (set out in the Bills of Exchange Act 1887) such that the acceptor has the primary obligation to pay the holder on maturity, but if the acceptor defaults, the drawer has the secondary obligation to pay the holder. Since there will be no paper bankers' acceptances in CREST, the draft Regulations set out corresponding obligations in respect of the relevant type of EDSs.

22. As part of the new payment arrangements for EDSs the Government expects that the provisions of the Financial Markets and Insolvency Regulations 1996 (SI 1996/1469 as amended) and the "collateral security charge" provisions of the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 will apply to EDSs. Once valuation arrangements are finalised, this should allow the CREST settlement banks to take floating charges over EDSs held by their customer CREST members, to support further the provision of DvP in central bank money. This should allow the possibility of the extension of the automatic self-collateralisation arrangements to these securities, although the Bank of England will make the decision on which securities are eligible for self-collateralisation.

Transition Period

23. It is envisaged that following the introduction of the new regulations EDSs will be issued before all existing MMIs have matured. Therefore, some paper (legacy) MMIs will run off in the CMO with an early maturity process for others, before its closure at end 2003. This would mean that any remaining paper MMIs could no longer be held or transferred in that system. Issuers could then choose to cancel outstanding legacy MMIs and issue non-material equivalent EDSs in their place. Alternatively, paper MMIs could be held in (holders' own) safe custody until their maturity with issuers making their own arrangements for redemption on maturity.

Part III – The main provisions

24. A limited number of amendments are needed to the USRs in order to achieve the objective of allowing electronic equivalents of MMIs to be eligible to be settled in an electronic settlement system and to be evidenced and transferred electronically. The key amendments are focused on defining EDSs and allowing title to be evidenced by the electronic register of holders of EDSs maintained by CRESTCo (which is currently the only Operator of a ‘relevant system’ of securities settlement under the USRs).

Regulation 3

25. Regulation 3 amends regulation 3 of the 2001 USRs, which provides definitions of references that appear elsewhere in the regulations. In so doing it defines the types of securities that can be evidenced and transferred electronically and settled in CREST. The amendments include a definition of an ‘eligible debt security’ the electronic equivalent of an MMI, and definitions of a ‘dematerialised Treasury bill’ and an ‘eligible dematerialised loan instrument’, both of which are specific types of ‘eligible debt security’ which have a basis in other legislation. The definition of an ‘eligible debt security’ is cast in fairly broad terms, without, for example a specific limitation on the maturity date for the securities in question. The breadth of the definition is intended to maintain sufficient flexibility to allow for the development of new kinds of securities in the future. We would welcome comments both on the detail of the definition, and its potential scope.

Regulation 4

26. Regulation 4 inserts a new interpretation provision defining a ‘participating issuer’ in relation to an eligible debt security and distinguishes between a principal (“P”) performing the payment obligation and another principal performing that obligation when P fails to do so (which is relevant in the context of EDS corresponding to bankers’ acceptances). Further consideration is required as to whether there are provisions of the USRs which should be disapplied in relation to the second principal (corresponding to the drawer of a bill).

Regulation 5

27. This regulation makes provision for updating references to registrars of local authority securities. It has no specific application in respect of EDSs.

Regulation 6

28. This regulation amends regulation 22(3) of the 2001 USRs, which is about registers and records kept of the holders of securities other than shares. It obliges the Operator to maintain a register of holders, their names and addresses, and how many units they hold, of participating securities. The amendments oblige the Operator to maintain a register of eligible debt securities. But there is no obligation on a participating issuer to maintain a record of uncertificated holders, as there is for other CREST securities.

Regulation 7

29. Regulation 7 amends regulation 24 of the 2001 USRs under which the register of holders of securities maintained by the Operator provides evidence of title to those securities. The Operator register provides prima facie evidence of title to eligible debt securities.

Regulation 9

30. Regulation 9 relates to legislation covering Treasury Bills and Local Authority Bills principally the National Loans Act 1968, the Treasury Bills Act 1877, and the Local Government and Housing Act 1989. The effect of the amendments is to apply to EDSs (with appropriate modifications) certain provisions that relate to paper money market instruments issued by the Treasury and local authorities.

DRAFT REGULATORY IMPACT ASSESSMENT

1. (i) Title of proposed measure:

“The Uncertificated Securities (Amendment) (Eligible Debt Securities) Regulations 2003”

2. (i) The issue and objective:

Issue: The legal framework for CREST’s operations is provided by the Uncertificated Securities Regulations. There has been a rolling programme of amendment of the USRs to ensure that there is a strong legal framework for securities settlement systems aiding financial stability, improving the competitiveness of the UK financial sector and helping to lower the cost of capital for companies (and Government) in the UK. The USRs were first introduced in 1995, extended to include gilts in 2000 and provided for Electronic Transfer of Title and Delivery versus Payment in central bank money in 2001.

Objective: The purpose of the draft amendment regulations is to change the USRs once again in order to allow the use of electronic equivalents of Money Market Instruments and for their transfer through the CREST system.

2. (ii) Risk assessment

In the context of these Regulations, there is no perceived situation that would lead to any harm or detriment to any individual or organisation.

3. (i) Identification of options

There are two options:

Option 1. – do nothing;

Option 2. – implement the draft amendment regulations.

3. (ii) Issues of equity and fairness

It is perceived that the proposed measure should impact equally across the entire wholesale market. Indeed it is at the behest of the market that the proposal for the modernisation of the settlement of MMIs arose.

There will not be any burden on the retail investor. There are no significant retail holdings of MMIs because they tend to have a high minimum denomination (£100,000 or more) and they are backed up by regulatory regimes mainly excluding the retail investor from this market.

4. (i) Identification of the benefits

Option 1. - No perceived benefits. The current paper based system involves considerable printing costs as well as costs of storing paper securely.

Option 2. - It would improve financial stability by offering DvP in central bank money in sterling and euros against simultaneous transfer of legal title for Eligible Debt Securities; create a single settlement platform for EDSs, gilts, bonds and equities; reduce infrastructure and maintenance costs for Treasury Bill investors; increase the flexibility for the DMO and commercial issuers so allowing better tailoring to the needs of both investors and issuers and reduce the Government costs of financing.

4. (ii) Quantifying and valuing the benefits

Option 1. – No benefits to quantify.

Option 2. - The DMO would benefit from the fungibility of bills and ease of use of collateral. There would be a reduction in the Government's debt interest bill insofar as Treasury bills become more attractive instruments in the market. The extent of this reduction is highly uncertain; however, for each basis point reduction in the average yield of Treasury bills at issue (which is a not unreasonable and probably cautious estimate of the impact), there would be a debt interest saving of £1-1.5 million a year. There would also be savings to the Treasury from reduced paper handling and printing costs; these would initially be at least £250,000 a year, and might be expected to rise over time.

Savings to the market would be at least £1.3 million for no longer meeting the costs of the CMO Depository and there would also be significant savings for the market from the saving of printing and paper handling costs. There are also likely to be substantial savings resulting from the fungibility and ease of use as collateral of CDs.

5. (i) Compliance costs for business, charities and voluntary organisations

Option 1. - Unlikely.

Option 2. – Unlikely.

5. (ii) Compliance costs for a typical business

Option 1. – Unlikely.

Option 2. – Unlikely.

5. (iii) Policy Costs

None.

5. (iv) Implementation Costs

There would be a one-off investment cost in new system for CREST estimated by them to be approximately £3 million maximum (for design, development and testing of the technical changes to CREST plus legal costs). We have no figures for the costs of preparation for the market, though given their strong support for modernisation it is assumed that the costs are seen as small compared with the advantages.

CREST is a highly integrated system and CRESTCo do not believe that there will be any significant additional costs once MMIs have been migrated. However, it will allow the cost of the CREST system to be shared over the wider activity base with greater economies of scale.

6. (i) Consultation with small businesses

A first public consultation is being conducted on the draft amendment regulations.

7. (i) Identification of any other costs

Option 1. – The CMO has a limited life. Its physical infrastructure is quite old, indeed largely obsolescent technology that is likely to need replacement in 2003. Although not quantified, it is thought that there will be significant costs and operational risk for the market and HM Treasury as an issuer if measures had to be taken to extend the life of the CMO.

Option 2. – None.

8. Results of consultation

This is the first consultation on the draft amendment regulations themselves, but the Bank and CRESTCo have consulted the market on the policy behind the proposal in 1999, 2000 and 2001 resulting in strong and wide market support for the policy.

9. Summary and recommendation

Option 2. is recommended as it will provide substantial efficiencies, risk reductions and cost savings generated by creating a single settlement platform for EDSs, gilts, bonds and equities plus allowing members to enjoy the benefits/savings of using a common network and functionality due to straight through processing. The creation of fungible issues would also make the markets deeper and more liquid and so help reduce issuance costs – an advantage to both issuers and investors. Failure to modernise the settlement of MMIs would also have reputational costs for the UK as a lack of DvP has meant that the CMO has not been consistent with certain of the CPSS- IOSCO recommendations on securities settlements systems.

10. Enforcement, sanctions, monitoring and review

None.

D R A F T S T A T U T O R Y I N S T R U M E N T S

2003 No.

COMPANIES

The Uncertificated Securities (Amendment) (Eligible Debt Securities) Regulations 2003

Made - - - - 2003
Coming into force - - 2003

Whereas a draft of these Regulations has been approved by a resolution of each House of Parliament;

Now, therefore, the Treasury, in exercise of the powers conferred by section 207 of the Companies Act 1989⁽¹²⁾, hereby make the following Regulations:

Citation, commencement and interpretation

1. —(1) These Regulations may be cited as the Uncertificated Securities (Amendment) (Eligible Debt Securities) Regulations 2003, and come into force on [the day after the day on which they are made][a date to be specified].

(2) In these Regulations “the Principal Regulations” means the Uncertificated Securities Regulations 2001⁽¹³⁾.

Amendment of the Principal Regulations

2. The Principal Regulations are amended as set out in regulations 3 to 12 of these Regulations.

Eligible debt securities - interpretation

3. In regulation 3(1)-

(a) after the definition of “the 1986 Act”, insert-

““the 1989 Act” means the Local Government and Housing Act 1989⁽¹⁴⁾”;

(b) in the definition of “the 1974 Regulations”, omit the words from “and” to the end;

(c) after the definition of “the 1974 Regulations” insert-

“the 1990 Regulations” means the Local Authorities (Borrowing) Regulations 1990⁽¹⁵⁾”;

⁽¹²⁾ 1989 c. 40. Section 207 was amended by the Bank of England Act 1998 (c. 11), section 35, and by S.I. 2001/3649, article 90.

⁽¹³⁾ S.I. 2001/3755.

⁽¹⁴⁾ 1989 c. 42.

⁽¹⁵⁾ S.I. 1990/767, amended by the Audit Commission Act 1998 (c. 18), section 54 and by S.I. 1991/551, S.I. 1991/1091, S.I. 1991/2000 and S.I. 2001/3469.

- (d) after the definition of “dematerialised instruction”, insert-
 ““dematerialised Treasury bill” means an uncertificated unit issued by the Treasury (either directly, or through such agent as they think fit)-
 (a) which is-
 (i) a unit of an eligible debt security issued by them;
 (ii) issued in circumstances where the current terms of issue of that security satisfy the requirements of regulation 3 of the Treasury Bills Regulations 1968 as substituted by regulation 49A of these Regulations;
 (iii) for the payment of a principal sum determined in accordance with those terms on a date (not more than twelve months from the date of issue of the unit) and in a manner so determined; and
 (b) in respect of which interest is payable at such rate and in such manner as they direct;”;
- (e) after the definition of “designated agency”, insert-
 ““eligible debt security” means a security-
 (a) which is constituted by an order, promise, engagement or acknowledgement to pay on demand, or at a fixed or determinable future time, a sum in money to, or to the order of, a person who holds one or more units of the security irrespective of whether, before the obligation to pay the sum becomes due, the identity of that person is known to, or can be established by, the person who will or may be obliged to pay the sum;
 (b) which is, or is capable of being, traded in a market for securities of the same or like kind;
 (c) whose current terms of issue provide that units of the security may only be held in uncertificated form and shall be transferable in no other manner than by means of a relevant system in accordance with these Regulations;”;
- “eligible dematerialised loan instrument” means an uncertificated unit issued by a local authority which-
 (a) is a unit of an eligible debt security issued by them;
 (b) is issued in circumstances where the current terms of issue of that security-
 (i) state that the issue of units of the security is an acknowledgement (by the borrower, the lender or both) that a loan has been made to the local authority concerned or that, in connection with the provision of funds to the authority, a payment or repayment is due from the authority;
 (ii) state, or provide a means for determining-
 (aa) the dates on which the authority are to make payments or repayments; and
 (bb) the amount of each of those payments or repayments; and
 (iii) in the case of a security issued by two or more local authorities acting jointly, state what proportion of the payments or repayments due are the responsibility of each of the authorities concerned; and
 (c) at the time it is issued does not contravene regulations 3, 4 (if applicable), 6 or 7 of the 1990 Regulations as modified by regulation 49B of these Regulations;”;
- (f) for paragraph (b) of the definition of “issuer register of securities”, substitute-
 “(b) in relation to units of securities other than-
 (i) shares,
 (ii) securities falling within regulation 22(3), or
 (iii) eligible debt securities
 means a register of persons holding the units, maintained by or on behalf of the issuer or, in the case of public sector securities, by or on behalf of the person specified in regulation 21(3);”;
- (g) after the definition of “issuer register of securities”, insert-
 ““local authority”-

- (a) in relation to a security referred to in paragraph (a) of the definition of “local authority security” has the same meaning as in the 1974 Regulations;
 - (b) in relation to a security referred to in paragraph (b) of the definition of “local authority security” or an eligible dematerialised loan instrument, has the same meaning as in the 1989 Act;”;
- (h) for the definition of “local authority security”, substitute-
 ““local authority security” means a security (other than an eligible debt security) which, when held in certificated form-
- (a) is transferable in accordance with regulation 7(1) of the 1974 Regulations and title to which must be registered in accordance with regulation 5 of those Regulations; or
 - (b) is a loan instrument within the meaning of section 43(4) of the 1989 Act, and is transferable in accordance with regulation 5(1) of the 1990 Regulations;”;
- (i) after the definition of “Operator register of corporate securities”, insert-
 ““Operator register of eligible debt securities” has the meaning given by regulation 22(3A)(a);”;
- (j) in paragraph (b) of the definition of “Operator register of securities”, after “public sector securities”, insert, “, an Operator register of eligible debt securities”;
- (k) in the definition of “UK Government security”, after “a security”, insert, “(other than an eligible debt security)”.
- 4.**—(1) In regulation 3(3)(a), after “appointed”, where second occurring, insert-
 “; or
 (iii) if the security falls within paragraph (b) of the definition of “local authority security” in regulation 3(1) and the local authority has appointed a person who is neither an officer nor any other employee of the authority for all of the purposes of the register required to be maintained under section 46(1) of the 1989 Act, to the person so appointed”.
- (2) After regulation 3(3), insert-
 “(4) In respect of a participating security which is an eligible debt security, references in these regulations to-
- (a) the issuer or participating issuer of that security (or units of that security) shall be taken to be references to-
 - (i) a person (“P”) who undertakes as principal to perform the payment obligation constituted by the security in accordance with its current terms of issue; and
 - (ii) any other person who undertakes as principal to perform that obligation other than by way of guarantee or surety in accordance with those terms in the event that P fails to do so;
 - (b) the issue of that security (or units of that security) shall be taken to include references to a procedure by which a person assumes an obligation of a kind referred to in paragraph (a).”.

Entries on registers and records in respect of local authority securities

- 5.**—(1) In regulation 21(3), after “appointed”, where second occurring, insert-
 “; or
 (c) if the security falls within paragraph (b) of the definition of “local authority security” in regulation 3(1) and the local authority has appointed a person who is neither an officer nor any other employee of the authority for all of the purposes of the register required to be maintained under section 46(1) of the 1989 Act, to the person so appointed”.
- (2) For regulation 21(5), substitute-
 “(5) Such sanctions as apply to-
- (a) the registrar within the meaning of the 1974 Regulations in the event of a default in complying with regulation 5 of those Regulations; or

(b) a person appointed as registrar under section 46(1) of the 1989 Act in the event of a default in complying with his obligations under that section or under the 1990 Regulations with respect to the keeping of a register

shall apply to a participating issuer and his officers in the event of a default in complying with paragraph (2)(a) in respect of a local authority security falling within paragraphs (a) or (b) respectively of the definition of “local authority security” in regulation 3(1).”.

(3) For paragraph 19(2) of Schedule 4, substitute-

“(2) Such sanctions as apply to-

(a) the registrar within the meaning of the 1974 Regulations in the event of a default in complying with regulation 5 of those Regulations; or

(b) a person appointed as registrar under section 46(1) of the 1989 Act in the event of a default in complying with his obligations under that section or under the 1990 Regulations with respect to the keeping of a register

shall apply to a participating issuer and his officers in the event of a default in complying with paragraph 13 in respect of a local authority security falling within paragraphs (a) or (b) respectively of the definition of “local authority security” in regulation 3(1).”.

Entries on registers and records in respect of eligible debt securities

6.—(1) In regulation 22(3), after “participating security”, where first occurring, insert “(other than an eligible debt security)”.

(2) After regulation 22(3), insert-

“(3A) In respect of every participating security which is an eligible debt security, the Operator shall-

(a) maintain a register, and such a register is referred to in these Regulations as an “Operator register of eligible debt securities”; and

(b) record in that register-

(i) the names and addresses of the persons holding units of that security; and

(ii) how many units of that security each such person holds.”.

(3) In regulation 22(4), for “(2)(a)(i) or (3)”, substitute, “(2)(a)(i), (3) or (3A)”.

Effect of entries on registers

7. In regulation 24, at the end, insert-

“(8) Subject to regulation 29, an entry on an Operator register of eligible debt securities shall be prima facie evidence, and in Scotland sufficient evidence unless the contrary is shown, of any matters which are by these Regulations directed or authorised to be inserted in it.”.

Registration by an Operator of transfers of securities

8. In regulation 27-

(a) for “Immediately upon”, substitute, “Subject to paragraph (7A), immediately upon”;

(b) after paragraph (7), insert-

“(7A) Paragraph (7) does not apply in relation to units of an eligible debt security.”.

Dematerialised Treasury bills and dematerialised loan instruments

9. After regulation 49, insert-

“APPLICATION OF THE TREASURY BILLS ACT 1877 ETC

Dematerialised Treasury bills

49A. –(1) The Treasury Bills Act 1877⁽¹⁶⁾, section 5 of the National Debt Act 1889⁽¹⁷⁾ and the Treasury Bills Regulations 1968⁽¹⁸⁾ apply to dematerialised Treasury bills with the modifications set out in paragraph (2) and in Part 1 of Schedule 5A to these Regulations.

(2) A reference in an enactment referred to in paragraph (1) to a Treasury bill is to be taken to include a reference to a dematerialised Treasury bill.

(3) A reference in the National Loans Act 1968⁽¹⁹⁾ to-

(a) a Treasury bill includes a reference to a dematerialised Treasury bill;

(b) the issue of securities includes a reference to the issue of uncertificated units of eligible debt securities.

Eligible dematerialised loan instruments

49B. –(1) Part IV of the 1989 Act and the 1990 Regulations apply in respect of eligible dematerialised loan instruments with the modifications set out in this regulation and in Part 2 of Schedule 5A to these Regulations.

(2) A reference in Part IV of the 1989 Act or the 1990 Regulations to-

(a) a loan instrument includes a reference to an eligible dematerialised loan instrument;

(b) borrowing money by means of a loan instrument includes a reference to borrowing money by means of the issue of an eligible dematerialised loan instrument;

(c) a payment made under an instrument includes a reference to a payment made in respect of an eligible dematerialised loan instrument in accordance with the current terms of issue of the eligible debt security of which that instrument is a unit (and references to payments which fall to be made, or are due to be made, under an instrument shall be construed accordingly);

(d) a matter or thing specified in an instrument includes a reference to a matter or thing specified in, or in accordance with the current terms of issue of the eligible debt security of which that instrument is a unit.

(3) The reference in regulation 7(4) of the 1990 Regulations to all bills issued by a local authority includes a reference to all eligible dematerialised loan instruments issued by the authority in circumstances where the issue of the instrument amounts to the issue of a bill for the purposes of those Regulations.

(4) In this Regulation, “local authority” has the same meaning as in section 39 of the 1989 Act.

Requirements for approval of a person as Operator

10. In paragraphs 12 and 25(e)(ii) of Schedule 1, after “Operator register of securities”, insert “(other than an Operator register of eligible debt securities)”.

Keeping of registers and records of participating securities

11. In Schedule 4-

(a) after paragraph 12(3), insert-

“(4) Regulations 5 and 7 of the 1990 Regulations shall not apply in respect of units of local authority securities held in uncertificated form.”;

(b) in paragraph 16(2), after “such register”, insert “(other than an Operator register of eligible debt securities)”.

⁽¹⁶⁾ 1877 c. 2.

⁽¹⁷⁾ 1889 c. 6.

⁽¹⁸⁾ S.I. 1968/414, amended by S.I. 1988/1603, S.I. 1991/1667, S.I. 1998/1450, and S.I. 1999/2907.

⁽¹⁹⁾ 1968 c. 13.

Modification of other enactments

12. After Schedule 5, insert-

“SCHEDULE 5A

Regulations 49A and 49B

PART 1

DEMATERIALIZED TREASURY BILLS

Modification of the Treasury Bills Act 1877

1. Omit section 4.
2. In section 8(2), at the end insert “in accordance with the current terms of issue of the bill”.
3. In section 9-
 - (a) omit subsections (1), (2) and (4);
 - (b) in subsection (3), omit the words from “, by the use” to “otherwise,”.

Modification of the National Debt Act 1889

4. In section 5, at the beginning, insert “Documents containing the current terms of issue of”.

Modification of the Treasury Bills Regulations 1968

5. For regulation 3, substitute-

“3. –(1) The current terms of issue of an eligible debt security, the units of which are dematerialised Treasury bills shall include a term to the effect that each uncertificated unit of the security-

 - (a) is issued subject to-
 - (i) the Treasury Bills Act 1877; and
 - (ii) these Regulationsas modified by the Uncertificated Securities (Amendment) (Eligible Debt Securities) Regulations 2003;
 - (b) is issued to raise money for-
 - (i) the National Loans Fund (“NLF”) under section 12 of the National Loans Fund 1968; or
 - (ii) the Debt Management Account (“DMA”) under paragraph 4 of Schedule 5A to the National Loans Act 1968; and
 - (c) entitles the holder of the unit to payment of a defined sum out of the NLF or the DMA (as the case may be) on redemption of the unit in accordance with the current terms of issue of the security.

(2) Where the value of a dematerialised Treasury bill is denominated in a currency other than sterling, the current terms of issue of the eligible debt security of which it is a unit shall include a term indicating the circumstances in which, and the conditions subject to which, the unit may be exchanged for a unit whose value is denominated in sterling.”.
6. In regulation 4-
 - (a) omit paragraph (1);
 - (b) for paragraph (2), substitute-

“(2) The Treasury may from time to time issue dematerialised Treasury bills to the order of the persons entitled to them and shall transfer such bills by means of a relevant system to those persons in consideration of the sums payable to the Treasury (or its duly appointed agent in that behalf) in respect of those bills”;
 - (c) in paragraph (3)-
 - (i) omit “a Treasury bill is ready for issue and”;

- (ii) for “that bill”, substitute “a dematerialised Treasury bill”;
 - (iii) for the words from “no delivery” to the end, substitute “the Treasury shall arrange for the bill to be transferred to them by means of a relevant system”.
7. In regulation 6-
- (a) in paragraph (1)-
 - (i) before “the bill”, insert “the value of”;
 - (ii) at the end, after “Bank of England”, substitute-
“; or
 - (c) by means of the relevant system in which title to the bill is recorded.”.
 - (b) in paragraph (1M)-
 - (i) for “mentioned in”, substitute “determined in accordance with the current terms of issue of a dematerialised Treasury bill”;
 - (ii) for “mentioned therein”, substitute “so determined”;
 - (iii) after “date of” wherever occurring, insert “issue of”.
 - (c) omit paragraph (2).
8. Omit regulations 7 and 8.
9. In regulation 9, after the definitions of “NLF bill” and “NLF Treasury bill”, insert-
““dematerialised Treasury bill”, “eligible debt security”, “issue”, “relevant system”, “uncertificated” and “units” have the same meaning as in the Uncertificated Securities Regulations 2001⁽²⁰⁾, as amended from time to time.”.

PART 2 DEMATERIALIZED LOAN INSTRUMENTS

Modification of Part IV of the Local Government and Housing Act 1989

1. In section 43(5)(a), omit the words from “and” to “redemption”.
2. In section 46-
 - (a) in subsection (4)(a), for the words from “an instrument” to “delivery”, substitute “an eligible dematerialised loan instrument”;
 - (b) omit subsection (8).
3. In section 66(1), after paragraph (a), insert-
“(aa) “dematerialised loan instrument”, “eligible dematerialised loan instrument”, “issue”, “uncertificated” and “unit” have the same meanings as in the Uncertificated Securities Regulations 2001⁽²¹⁾.”.

Modification of the Local Authorities (Borrowing) Regulations 1990

4. In regulation 2-
 - (a) after the definition of “the Act”, insert-
““dematerialised loan instrument”, “eligible debt security”, “eligible dematerialised loan instrument”, “issue”, “Operator”, “relevant system”, “uncertificated” and “unit” have the same meanings as in the Uncertificated Securities Regulations 2001;”;
 - (b) in the definition of “loan instrument”, for “instruments which are transferable by delivery, substitute “eligible dematerialised loan instruments”.
5. In regulation 3-

⁽²⁰⁾ S.I. 2001/3755.
⁽²¹⁾ S.I. 2001/3755.

(a) in paragraph (1), for “The terms of a loan instrument”, substitute “The current terms of issue of an eligible debt security whose units are eligible dematerialised loan instruments”.

(b) omit paragraphs (6) to (8).

6. For regulation 5, substitute-

“5. Units of a loan instrument which are recorded on a register kept by the Operator of a relevant system under the Uncertificated Securities Regulations 2001 shall be transferable in no other manner than by means of that system in accordance with those Regulations.”.

7. In regulation 7-

(a) in paragraph (1), for “a loan instrument which is transferable by delivery”, substitute “an eligible dematerialised loan instrument”;

(b) for paragraph (2)(b)(iv), substitute-

“(iv) the authority provides the holder of the instrument with a statement in accordance with paragraph (9)”;

(c) in paragraph (8), a reference to “paper” or a “note” includes a reference to an eligible dematerialised loan instrument which is sterling commercial paper or a sterling medium term note (as the case may be) for the purposes of paragraph (2)(b) or (c);

(d) in regulation 7(9)-

(i) after “local authority shall”, insert “be accompanied by”;

(ii) in sub-paragraph (a), omit “contain”;

(iii) in sub-paragraphs (b) and (c), for “state”, substitute “a statement”;

(v) omit sub-paragraph (d);

(vi) in sub-paragraph (e), omit “contain”;

8. Omit regulation 8.

9. In regulation 9-

(a) in paragraph (3)(a), for “and”, substitute “or”;

(b) in paragraph (4), after “regulation 5”, insert “, the transfer of title to an eligible dematerialised loan instrument by means of a relevant system”.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Uncertificated Securities Regulations 2001 (S.I. 2001/3755) (“the Principal Regulations”) to allow for the evidencing and transfer of title to “eligible debt securities” by means of a “relevant system” as defined in the Principal Regulations.

A new definition of “eligible debt securities” is inserted into the Principal Regulations by regulation 3(e). “Dematerialised Treasury bills” and “eligible dematerialised loan instruments” (as defined in regulation 3(d) and (e)) are special cases of “eligible debt securities”, in respect of which consequential modifications of other legislation are made by new regulations 49A and 49B and Schedule 5A (inserted into the Principal Regulations by regulations 9 and 11).

Regulation 4(2) inserts interpretation provisions into the Principal Regulations, in relation to the persons who are “participating issuers” of eligible debt securities, and the “issue” of such securities.

By virtue of provisions inserted into the Principal Regulations by regulation 6, an Operator of a relevant system must maintain an “Operator register of eligible debt securities” in relation to each such security which is a participating security. Such a register must contain entries indicating the names and addresses of persons holding units of the security, and how many such units each person holds. Such entries are prima facie evidence, and in Scotland sufficient evidence (unless the contrary is shown) of the matters to which they relate (regulation 7, which inserts a new paragraph (8) into regulation 24 of the Principal Regulations).

Regulation 8 disapplies regulation 27(7) of the Principal Regulations in the case of eligible debt securities, in view of the nature of those securities. Regulation 11 modifies the existing provisions as to the location of registers in relation to such securities.

Eligible debt securities that constitute “dematerialised Treasury bills” or “eligible dematerialised loan instruments” (as defined in regulation 3(d) and (e)) are subject to new regulations 49A and 49B (inserted by regulation 9 of these Regulations) which, in combination with new Schedule 5A (inserted by regulation 12) apply, with modifications, provisions of the Treasury Bills Act 1877, Part IV of the Local Government and Housing Act 1989 and other legislation to those securities.

Regulation 10 amends paragraphs 12 and 25(e)(ii) of Schedule 1 to the Principal Regulations with the effect that issuers of eligible debt securities have no statutory right to inspect an Operator register of eligible debt securities. This is in keeping with the nature of “eligible debt securities” as uncertificated counterparts of bearer securities, in relation to which the identity of the bearer need not be known to the issuer of the security.

Regulation 11 amends Schedule 4 to the Principal Regulations with the effect that certain provisions of the Local Authorities (Borrowing) Regulations do not apply in respect of units of local authority securities held in uncertificated form, and that the provisions concerning the location of registers in paragraph 16(2) of that Schedule do not apply in respect of Operator registers of eligible debt securities.