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For the attention of Daniel Jones
HM Treasury
1 Horse Guards Road
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Dear Daniel Jones

Issues of legal uncertainty in relation to security-based collateral structures under the Financial Collateral Arrangements (No. 2) Regulations 2003 ("FCARs")

The role of the Financial Markets Law Committee (the "**FMLC**" or the "**Committee**") is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

The interpretation of certain elements of the FCARs has remained an area of legal uncertainty for a number of years, the Committee having previously written about these topics on several occasions.[1]

The FCARs are listed in Schedule 1 of the Financial Services and Markets Act 2023 ("**FSMA 2023**") and will therefore be revoked[2] in due course.[3] The Committee asks the Government to use this opportunity to ensure that the replacement legislation for the FCARs clarifies the areas of uncertainty discussed in this letter.

The main issue with the FCARs relates to a lack of comfort that structures not involving title transfer (e.g. pledges, mortgages, other security interests) fall within the scope of the FCARs and are therefore subject to its protections.

The FMLC understands that addressing these issues could potentially free up large amounts of bank capital, whilst also allowing users of financial services to adopt structures which involve reduced counterparty risk, potentially providing a considerable boost to the UK economy.

1 Including, in relation to the FCARs, (i) the report on *Gray v G-T-P Group Ltd* dated December 2010 (available here: http://fmlc.org/wp-content/uploads/2018/02/Issue-87-Control-Gray.pdf), (ii) the report on the FCARs dated 1 December 2012 (available here: https://fmlc.org/publications/report-collateral-directive-1-december-2012/), (iii) the letter to Richard Knox dated 13 April 2015 (available here: http://fmlc.org/wp-content/uploads/2018/03/letter_to_mr_richard_knox_hmt_regarding_fcars.pdf), and (iv) the letter to the Directorate-General for Financial Stability, Financial Services and Capital Markets Union dated 7 May 2021 (available here: https://fmlc.org/wp-content/uploads/2021/05/FCD-Review.pdf).

2 Section 1(4) of FSMA 2023 provides that the revocation of any legislation in accordance with that section will not affect the continued effect of any amendments to other legislation made by that revoked legislation (as those amendments had effect immediately before the revocation).

3 We note that the commencement for the revocation of the FCARs are not included in the Financial Services and Markets Act 2023 (Commencement No. 1) Regulations 2023 and that no timetable for their revocation and replacement has yet been announced.

This letter sets out the areas of uncertainty, their impact on the market and suggested drafting to mitigate such identified uncertainties amending the current FCARs[4] for ease of implementation.

1. Issues of Legal Uncertainty

1.1. The intention of the FCARs is to improve the legal certainty of financial collateral arrangements by affording certain protections (including, amongst others, the disapplication of various rules on formalities and the registration of security, and the disapplication and modification of certain parts of insolvency legislation). There are two forms of acceptable "financial collateral arrangements" for these purposes: (i) "title transfer financial collateral arrangements" and (ii) "security financial collateral arrangements". Title transfer collateral arrangements involve the full transfer of relevant assets to the collateral-taker; such arrangements are easy to identify and are widely used in the market. Security financial collateral arrangements are a form of security arrangement where the collateral-taker receives a security interest in the assets, but the collateral-provider retains an ownership interest in the collateral.

1.2. The term "security financial collateral arrangement" is defined in regulation 3(1) of the FCARs as an arrangement or agreement:

1.2.1. evidenced in writing;

1.2.2. under which a security interest is created or arises over financial collateral to secure "relevant financial obligations" owed to the collateral-taker;

1.2.3. where the collateral-provider and the collateral-taker are non-natural persons; and

1.2.4. where the financial collateral is delivered, transferred, held, registered or otherwise designated so as to be in the possession or under the control of the collateral-taker or a person acting on its behalf.

1.3. The first three of these requirements are usually straightforward and do not require further analysis or discussion. However, the scope and interpretation of the latter requirement for "possession" or "control" has proved particularly troublesome in case law and in practice, as discussed further below. The Committee is of the view that replacement legislation for the FCARs should provide clarity and certainty as to the separate meanings of "possession" and "control".[5] We have set out some proposed drafting in this regard in the Annex to this letter on the basis of the current FCARs.

2. "Possession" and "control"

2.1. Per the definition in regulation 3(2) of the FCARs, the "possession" of financial collateral in the form of cash or financial instruments *"includes the case where financial collateral has been credited to an account in the name of the collateral-*

[4] We note that in its final report on digital assets dated 27 June 2023 (available here: https://s3-eu-west-2.amazonaws.com/lawcom-prod-storage-11jsxou24uy7q/uploads/2023/06/Final-digital-assets-report-FOR-WEBSITE-2.pdf), the Law Commission recommended the development of a distinct financial collateral regime for digital assets. This letter considers the broader financial collateral regime but does not specifically consider how it should apply to digital assets in any such separate regime.

[5] A more extensive redraft of the existing framework could seek to remove the concept of "possession" altogether, and instead focus purely on a broader concept of "control" which includes elements currently under the "possession" definition.

taker or a person acting on his behalf (whether or not the collateral-taker, or person acting on his behalf, has credited the financial collateral to an account in the name of the collateral-provider on his, or that person's, books) provided that any rights the collateral-provider may have in relation to that financial collateral are limited to the right to substitute financial collateral of the same or greater value or to withdraw excess financial collateral". There is no guidance on what constitutes "possession" of financial collateral in the form of credit claims.

2.2. There is also no definition or specific guidance as to the meaning of "control" in the FCARs. However, within the definition of "security financial collateral arrangement" in regulation 3(1) of the FCARs, it is stated that *"any right of the collateral-provider to substitute financial collateral of the same or greater value or withdraw excess financial collateral or to collect the proceeds of credit claims until further notice shall not prevent the financial collateral being in the possession or under the control of the collateral-taker"*.

2.3. There is uncertainty as to whether this wording precludes a collateral-provider from having any rights that go beyond a right to substitute financial collateral of the same or greater value or to withdraw excess financial collateral for the collateral-taker to still have "possession" or "control" of the collateral. This is particularly acute where collateral continues to be held in an account in the name of the collateral-provider, such as under tripartite arrangements between a collateral-provider, collateral-taker and custodian, where the collateral-taker is granted a security interest over the account. In such a situation, the collateral-taker does not have possession of the collateral, so it will need to show it has control, notwithstanding additional rights granted to the collateral-provider. Such additional rights are customary and often include:

2.3.1. the right to withdraw any income that accrues on the collateral on the basis that the security interest does not extend to such income;

2.3.2. the right to be able to continue to receive notices or to exercise voting rights in respect of the collateral (where relevant to the type of collateral);

2.3.3. the right (or responsibility) for determining the value of the collateral (e.g. in respect of collateral consisting of derivatives); and

2.3.4. the right to be returned the collateral in the event of the insolvency of the collateral-taker, or on satisfaction of the secured obligations.

2.4. It is also unclear where the law stands when a collateral-taker exercises a right of use over the collateral, including with the client's consent, and for example delivers up the collateral to meet an obligation arising as a result of business for its client (e.g. using it as collateral in respect of a client transaction, where the collateral-taker acts as an intermediary facing another institution such as a swap counterparty, settlement agent, custodian or CCP). In such circumstances, the collateral will not be in the possession of the collateral-taker, but it is uncertain whether the collateral remains in its control. Similarly, it is not clear whether there can be two parties with control over the same collateral at any one time. For example, in the tripartite example mentioned above, the custodian may have certain rights that demonstrate "control", in addition to those of the collateral-taker that also demonstrate "control". This could usefully be clarified in the replacement legislation.

2.5. The requirement for "possession" or "control" in security financial collateral arrangements has been the subject of detailed judicial scrutiny and commentary in two decided cases in the English courts – the so-called *Lehman "Extended Liens"*

case[6] and *Gray*[7] – and one decided case in the ECJ, *Swedbank*,[8] which resulted from a referral from the Latvian courts. It is worth noting that in the *Lehman "Extended Liens"* and *Gray* cases, a purported security financial collateral arrangement was challenged by insolvency office-holders and held not to exist.

2.6. The state of the current case law is that the collateral-taker (or its agent) must have a level of "possession" or "control" sufficient that the collateral-provider can be properly described as "dispossessed" of the collateral and the collateral can properly be described as having been "provided" to the collateral-taker. The collateral-taker (or its agent) must not only have practical control over the account to which the collateral relates, but also the right to prevent the withdrawal of cash by the collateral-provider in so far as is necessary to guarantee the relevant obligations.[9] Importantly, the collateral-taker must have the right to prohibit the withdrawal of collateral where the value of the remaining collateral would thereby be or fall below the value of the liabilities secured by that collateral.[10] Beyond this, there is other guidance on what is insufficient for a security financial collateral arrangement,[11] but little in the way of helpful guidance as to what might qualify. In addition, the courts have held that the question of possession or control is a factual matter to be assessed in the specific circumstances.[12] These tests might be appropriate in the context of a very fixed collateral arrangement, e.g. where there is a single-payment or so-called "bullet" loan, and a bank takes security over physical share certificates which are held in its vault and not released until full repayment of the loan. However, these definitions and concepts do not work at all in the more usual modern situation of an active portfolio where a client transacts in and out of exposures on a regular basis. Where a client reduces their exposures, by closing out or terminating contracts, they would typically be entitled then to withdraw any excess collateral. Arrangements which do not allow for the withdrawal of excess collateral are uncommercial. The way in which these concepts have been interpreted by the Courts makes it difficult for market participants to have any certainty that the "possession" or "control" test has been met for any purported security financial collateral arrangement, with clarity only coming upon enforcement.

2.7. The situation can be contrasted with that of the U.S. and certain other jurisdictions, where security collateral arrangements are commonplace. In the U.S. (pursuant to the Uniform Commercial Code adopted in all states), the concept of "control" (which is a basis of perfection of security interests in securities and certain other financial assets) is considerably more flexible. The key to control from a U.S. perspective is that the collateral-taker has the right to have the collateral transferred without need for action or consent by the collateral-provider. This right need not be exclusive (and often is not), such that the debtor may also retain the right to make substitutions, to instruct any custodian or otherwise deal with the pledged security. It is frequently the case that any such rights of the collateral-provider can be terminated by the collateral-taker upon a default by the collateral-provider, following which the collateral-taker would have exclusive control. Once the collateral-taker has control over securities collateral, its security

6 *Re Lehman Brothers International (Europe) in administration and others* [2012] EWHC 2997 (Ch).

7 *Re F2G Realisation Ltd: Gray v GTP Group Ltd* [2010] EWHC 1772 (CH), [2011] 1 BCLC 313.

8 *Private Equity Insurance Group SIA v Swedbank AS* [2016] EUECJ C-156/15 (10 November 2016).

9 Opinion of Advocate General Szpunar, *Private Equity Insurance Group SIA v Swedbank AS*, Case C-156/15, 21 July 2016, available here: https://curia.europa.eu/juris/document/document.jsf?text=&docid=181931&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=287546. This opinion was adopted by the ECJ in its decision.

10 See paragraphs 131 to 151 of the *Lehman "Extended Liens"* case.

11 See, in particular, paragraphs 131 to 133 and 143 to 147 of the *Lehman "Extended Liens"* case.

12 See paragraph 136 of the *Lehman "Extended Liens"* case

interest will generally remain perfected until it both ceases to have control and the debtor again becomes the holder of the securities. U.S. law also is generally more flexible with respect to repledges or reuse of collateral by the collateral-taker without risk of losing its perfected security interest. Furthermore, in the context of a U.S. bankruptcy proceeding, it is necessary essentially for the secured party to show that it is perfected at the point of enforcement. There is no need as in the UK for a collateral-taker to show an ongoing relationship of possession or control. We understand that other common law-based jurisdictions (including Canada and Australia) follow an approach similar to that of the U.S. with respect to control of financial collateral.

2.8. To remove this uncertainty, the replacement legislation for the FCARs could move towards the U.S. approach of abandoning reference to the pre-default situation and instead only require a later perfection of control, i.e. at the point of enforcement. This would enhance legal certainty by looking at the situation at the most relevant point in time. Alternatively, it could still look to the pre-default situation but more clearly define what constitutes "possession" and "control" by setting out certain permissible features of security financial collateral arrangements. We have set out in the Annex to this letter our proposals regarding how the existing provisions in the FCARs could be amended in replacement legislation. Broadly these changes would make clear that:

2.8.1. any right of the collateral-provider to substitute collateral of the same or greater value or to withdraw excess collateral will not be deemed to cause the collateral-taker not to have "possession" or "control" of the collateral (i.e. a broadening of the existing wording which currently just limits the rights of a collateral-provider to such a right);

2.8.2. certain additional rights of the collateral-provider (such as those set out at paragraph 2.3 above) will not cause the collateral-taker to be treated as not having "control" of the collateral, subject to certain conditions in respect of certain of those rights;

2.8.3. collateral being held in an account in the name of the collateral-provider (such as under a tripartite arrangement described above) would not cause the collateral-taker to be treated as not having "control" of the collateral; and

2.8.4. exercise of a right of use by the collateral-taker would not cause the collateral-taker to be treated as not having "control" of the collateral.

3. "**Excess Financial Collateral**"

3.1. A secondary issue arises in respect of what constitutes "excess financial collateral" for the purposes of the definition of "security financial collateral arrangement" in regulation 3(1) of the FCARs. The phrase is not defined in the FCARs, and there is currently no specific guidance in case law as to what would constitute an "excess" of collateral permitting withdrawal. For a loan obligation secured by a government bond, the concept may be clear. However, the collateral required for derivatives exposures is calculated using a complex model based upon previously observed historical price variations, a holding period (say, 2 to 5 days' worth of such historical variations) and a confidence interval (say, 95% or 99% confidence). It is not clear how the amount of "excess" is to be determined when an asset's price may vary and is risk-weighted using models. It is also unclear whether the collateral-taker is free to specify the amount of collateral that must be held under such models, so that there is an "excess" if the value of the collateral exceeds that agreed amount. The judgment in the *Lehman "Extended Liens"* case assumes the

former, i.e. that an excess would only arise where the value of the collateral exceeded the liabilities to be secured by it. However, there is often no such objective value.

3.2. As such, in our view it could be clarified in the replacement legislation for the FCARs that an "excess" of collateral arises where the value (or estimated value) of the collateral exceeds the amount of collateral required to be posted from time to time by the collateral-taker. We have proposed some drafting to reflect this position in the Annex to this letter.

4. Use of collateral received after insolvency

4.1. Another area of uncertainty arises in connection with the receipt of assets by a collateral-taker after the insolvency of the relevant collateral-provider, due to a lack of clarity regarding the relationship between two overlapping pieces of UK legislation, the FCARs and the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (the "**SFRs**").

4.2. Where financial collateral comes to be in the possession or under the control of a collateral-taker after the commencement of, insolvency proceedings in respect of the collateral-provider, the collateral will generally not be protected by the FCARs. However, under regulation 13(1) of the FCARs, for security collateral, the collateral is still protected if received on the same day as the onset of proceedings if the collateral-taker was not aware, nor should have been aware, of the commencement of such proceedings. The provision is silent as to whether any receipt of collateral after that time or which occurs following the collateral-receiver's awareness is protected. There is therefore uncertainty regarding the extent of protections in such situations.

4.3. The speed of communications around the market in respect of insolvencies has increased as a result of usage of the internet, email and other developments since 2003. At the same time, settlement times for cash and non-cash assets have reduced. Cash can generally be transferred and settled intra-day and often within a matter of minutes or hours. However, that is not the case for non-cash collateral in the form of securities. Exchange-traded securities are usually settled on a T+2 basis,[13] but for other assets settlement times may be longer – and at the point of receipt, the collateral-taker may have the requisite notice or the transfer may be completed on the following day.

4.4. The SFRs separately apply to so-called "designated systems" such as payment, clearing and settlement systems. These systems are often used by collateral providers and collateral takers for transfers of collateral. Regulation 20 of the SFRs provides that a transfer order that is entered into a designated system and becomes irrevocable on the same day as the start time of the insolvency proceedings of the relevant participant (the "**Insolvency Start Time**") will still be subject to the insolvency law disapplications and modifications set out therein, as long as the operator of the designated system did not have notice of the insolvency at the time the transfer order became irrevocable. There may then be a delay between an order becoming irrevocable under the relevant system rules and its receipt. Unlike the situations specifically provided for in regulation 13 of the FCARs, the SFRs protections are dependent on the date and time of initiation and irrevocability of a transfer of collateral, rather than final settlement. This could create a potential disconnect between the FCARs and SFRs, whereby a transfer of collateral pursuant to an irrevocable transfer order in respect of non-cash securities entered into a designated system after the collateral-provider's insolvency can still be protected under the SFRs and indeed will be processed

[13] Article 5(2) of Regulation (EU) No 909/2014, as it forms part of UK domestic law by virtue of the European Union (Withdrawal) Act 2018.

resulting in a transfer to the collateral-taker, but the FCARs give no assurance that the collateral-taker would be able to afford itself of the protections under the FCARs as regards such assets.

4.5. In practice, instructions for transfer of title transfer collateral and security collateral which are put into and become irrevocable in a designated system:

4.5.1. before the Insolvency Start Time will result in the transfer taking effect, notwithstanding that the transfer may complete after (and perhaps even one or two days after) the Insolvency Start Time. In this case, the recipient of that collateral is protected by the SFRs;

4.5.2. on the day of but after the Insolvency Start Time, so long as the operator of the designated system was not aware nor should have been aware of the insolvency, will result in the transfer taking effect, so long as the transfer completes on the same day. In this case, the recipient of that collateral is protected by the SFRs;

4.5.3. after the Insolvency Start Time, i.e. either on a date after the day of the Insolvency Start Time, or on the day of but after the Insolvency Start time other than in the circumstances set out in 4.5.2, will not result in the transfer taking effect.

There is then typically a delay between a transfer order becoming final and irrevocable and it actually settling, which could be as long as two business days even for listed securities. Receipts of assets under protected SFRs orders could therefore arrive in a collateral-taker's account after the time limit set out in regulation 13 of the FCARs. One possible resolution of this conflict would be if regulation 13 of the FCARs only addressed transfers that do not go through a designated system, which would be a reasonable interpretation of the two provisions. However, this should better be clarified.

4.6. This inconsistency has no policy rationale. It could be fixed by including an additional exception in regulation 13 of the FCARs for collateral transfers which are received by collateral-takers pursuant to an irrevocable transfer order under the rules of a designated system pursuant to the SFRs. We have proposed some drafting to reflect this position in the Annex to this letter. We have also suggested a corresponding amendment that should be made to regulation 13(2)(c) to ensure that the existing provision also applies to title transfer arrangements, which was unclear from the current drafting.

5. Market Impact

Clearing Houses

5.1. For the above reasons, some of the UK's biggest clearing houses do not accept security financial collateral at all; others allow it within limits only.

5.2. Security financial collateral structures have the advantage of making collateral "bankruptcy remote" from the perspective of the collateral-provider. This is because although the collateral is delivered up to the collateral-taker, it is kept in a separate account, usually labelled as a trust account or pledged account, which the collateral-taker is only able to use following a default. In the context of collateral provided to clearing houses, collateral providers are the clearing members, mostly the world's largest banks. If such persons were able to provide collateral on a security basis, this would bring significant capital benefits.

5.3. Under the PRA Rulebook in the UK,[14] title transfer results in a charge of 2% for clearing member exposures to a CCP and 4% for client exposures to a clearing member. However, using security would reduce this to 0%. The exposure of the clearing member to the CCP under a security financial collateral arrangement would also not be counted towards the clearing member's leverage ratio calculations, where applicable. Given the size of cleared exposures of the major banks, and the reduction to capital charges that would result, changes to the FCARs would potentially unlock significant amounts of bank capital, which could be deployed elsewhere.

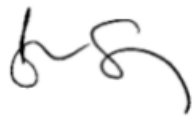
5.4. Additional usage of security financial collateral by clearing houses would likely, in turn, drive more clearing business to the UK, in particular from the U.S. where pledged collateral structures are common in the sector.

Derivatives

5.5. ISDA has obtained a legal opinion stating that there are "good arguments" to suggest that Security Documents entered into in connection with an ISDA Master Agreement "should" each be a "security financial collateral arrangement" for the purposes of the FCARs.[15] The relevant opinion is necessarily heavily qualified and based on a number of assumptions, and we understand has in practice not greatly altered the sentiment of the market. We understand that whilst some banks do offer security financial collateral arrangements on uncleared derivatives, such structures are usually subject to significant haircuts and higher fees. The increased legal certainty that the suggested legislative changes would bring would incentivise banks to offer these structures more readily, reducing their legal risk and freeing up capital from collateral-providers for other purposes.

I and Members of the Committee would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me should you wish to arrange a meeting or if you have any questions.

Yours sincerely,



Brian Gray
Chief Executive[16]

CC: Peter King

[14] Article 306 of Chapter 3 of the Counterparty Credit Risk (CRR) Part of the PRA Rulebook.

[15] See Part II.4 of the opinion, available here: https://www.isda.org/a/6wIEE/England-amp-Wales-ISDA_Collateral_Provider_Opinion_-_13_November_2018__IS.pdfhttps://www.isda.org/a/6wIEE/England-amp-Wales-ISDA_Collateral_Provider_Opinion_-_13_November_2018__IS.pdf.

[16] The FMLC acknowledges the assistance of ICE Clear Europe, Thomas Donegan of Sherman and Sterling LLP and Habib Motani of Clifford Chance LLP in writing this letter.

Annex

Proposed Amendments for the current FCARs to mitigate areas of uncertainty

[…]

3 Interpretation

[…]

(2) For the purposes of these Regulations "possession" of financial collateral in the form of cash or financial instruments includes the case where financial collateral has been credited to an account in the name of the collateral-taker or a person acting on his behalf (whether or not the collateral-taker, or person acting on his behalf, has credited the financial collateral to an account in the name of the collateral-provider on his, or that person's, books) provided that any rights the collateral-provider may have ~~**in relation to that financial collateral are limited to the right**~~ to substitute financial collateral of the same or greater value or to withdraw excess financial collateral **shall not cause the collateral-taker not to have possession or control of the financial collateral**.

(3) In a security financial collateral arrangement, the collateral-taker shall be treated as having "control" of the collateral for the purposes of these Regulations notwithstanding:

(a) its exercise of a right of use as described in regulation 16;

(b) any right of the collateral-provider to substitute collateral of the same or greater value, withdraw excess collateral or collect the proceeds of, or otherwise service, a credit claim until further notice;

(c) any right of the collateral-provider to receive income or notices, or exercise any voting rights, in relation to collateral in the form of securities;

(d) any right or responsibility of the collateral-provider to determine the value of the collateral (or any assets which may be substituted for the collateral), provided that:

(i) the exercise of any right of substitution or withdrawal of excess collateral depends on the collateral-provider's determinations being verified by the collateral-taker or a third party (such as the custodian with which the collateral is held); or

(ii) the collateral-taker has the right to carry out such verification (or procure that it is carried out) and veto any exercise of a right of substitution or withdrawal of excess collateral if the collateral-provider's valuations cannot be confirmed;

(e) any right of the collateral-provider to require release of the collateral from the collateral arrangements if the collateral-taker becomes insolvent upon certification that the secured obligations have been discharged, provided that:

(i) where the certification depends on a valuation that has been carried out by the collateral-provider, the collateral-provider is required to act reasonably and in good faith in undertaking such valuation; and

(ii) the collateral-provider is required to provide its certification to both the collateral-taker and the person with which the relevant account is

held, with the right to withdraw collateral from the account arising only after a specified period has elapsed;

(ii) the collateral-taker has the right to carry out such verification (or procure that it is carried out) and veto any exercise of a right of substitution or withdrawal of excess collateral if the collateral-provider's valuations cannot be confirmed; and

(f) the fact that the collateral may be held in an account in the name of a third party (including the collateral-provider) where the collateral-taker has an agreement with the person with which the account is held that contains the features set out in sub-paragraphs (b) to (e).

(4) For the purposes of paragraphs (2) and (3), "excess financial collateral" arises where the value (or estimated value) of the collateral exceeds the amount of collateral required to be posted from time to time under the agreement between the collateral-provider and the collateral-taker.

[…]

13 Financial collateral arrangements to be enforceable where collateral-taker not aware of commencement of winding-up proceedings or reorganisation measures

(1) Where any of the events specified in paragraph (2) occur on the day of, but after the moment of commencement of, winding-up proceedings or reorganisation measures those events, arrangements and obligations shall be legally enforceable and binding on third parties if the collateral-taker can show that he was not aware, nor should have been aware, of the commencement of such proceedings or measures.

(2) The events referred to in paragraph (1) are–

(a) a financial collateral arrangement coming into existence;

(b) a relevant financial obligation secured by a financial collateral arrangement coming into existence; or

(c) the delivery, transfer, holding, registering or other designation of financial collateral so as to **transfer its legal and beneficial ownership to, or** be in the possession or under the control of**,** the collateral-taker.

(2A) Where, on the day of winding-up proceedings or reorganisation measures–

(a) a transfer order is entered into a designated system and becomes irrevocable in accordance with the Financial Markets and Insolvency (Settlement Finality) Regulations 1999/2979; and

(b) such transfer order meets the conditions set out in regulation 20(2) of the Financial Markets and Insolvency (Settlement Finality) Regulations 1999/2979,

any delivery, transfer, holding, registering or other designation of financial collateral so as to transfer its legal and beneficial ownership to, or be in the possession or under the control of, the collateral-taker pursuant to such transfer order shall be legally enforceable and binding on third parties.

(3) For the purposes of paragraph (1)–

(a) the commencement of winding-up proceedings means the making of a winding-up order or, in the case of a Scottish partnership, the award of sequestration by the court; and

(b) commencement of reorganisation measures means the appointment of an administrator, whether by a court or otherwise or, in the case of a Scottish partnership, the date of registration of a protected trust deed.

[…]

16 Right of use under a security financial collateral arrangement

(1) If a security financial collateral arrangement provides for the collateral-taker to use and dispose of any financial collateral provided under the arrangement, as if it were the owner of it, the collateral-taker may do so in accordance with the terms of the arrangement.

(2) The exercise by a collateral-taker of a right of use as described in paragraph (1) shall not render invalid or unenforceable any right of the collateral-taker under such a collateral arrangement.

[…]