Rome I: Council's Compromise Package, Insurance Contracts, Financial Aspects Relating to Articles 4 and 5

Following our post on the note from the Luxembourg delegation relating to consumer contracts, a number of new interesting documents on the Rome I Proposal have been made publicly available on the Register of the Council.

Here's a brief presentation:

– doc. n. 8022/07 ADD 1 REV 1 of 13 April 2007, containing a **"compromise package" prepared by the German Presidency** for the JHA Council session of 19-20 April 2007 (see our related post on the Council conclusions). The text focuses on Articles 3 (Freedom of choice), 4 (Applicable law in the absence of choice) and 6 (Individual employment contracts). Art. 7 on contracts concluded by an agent is deleted; other important issues, such as contracts of carriage (art. 4a), consumer contracts (art. 5), insurance contracts (art. 5a) and overriding mandatory provisions (art. 8) do not form part of the compromise;

– doc. n. 8935/1/07 REV 1 of 4 May 2007, on **insurance contracts**. The document provides a draft text of Art. 5a, taking into account the comments submitted in March by the Member States delegations (docs. 6847/07 and ADD 1 to 12, not accessible to the public);

– doc. n. 7418/07 of 15 March 2007, from the Services of the Commission to the Council's Committee on Civil Law Matters, dealing with **certain financial aspects relating to the application of Articles 4 and 5**. The document is divided in two parts: the first one addresses the conflict rule on contracts concluded at a financial market (Art. 4(1)(j1)), that was introduced by the Finnish presidency (see doc. n. 16353/06 of 12 December 2006) and confirmed by the German Presidency (see the French text of doc. n. 6953/07 of 2 March 2007), stressing the **importance of a specific provision on stock exchange transactions**:

The reason for including a specific provision for trading systems relates, in particular, to the fact that regulated markets, multilateral trading facilities and other similar trading systems need to operate under a single law. It is essential that all transactions are carried out in accordance with the governing law of the system. The application of a single governing law is an intrinsic feature of organised multilateral trading systems and necessary for legal certainty for the market participants.

These transactions concluded within such a trading system include contracts of buying, selling, lending and other such dealings in financial instruments. Contracts for the provision of services between a financial intermediary and a client are not concluded within these trading systems.

The transactions in question are closely connected to the market concerned and it is appropriate and, indeed, necessary that the same law governs them irrespective of the nature of the parties to the transactions (consumer/professional) and the place where the parties have their habitual residence. Any other result would mean that the systems could not operate.

Problems arising from the **definition of "financial market"** are then addressed, in the light of the Directive 2004/39/EC (MiFID – Markets in Financial Instruments Directive), and an improved draft of the provision is proposed:

[T]he use of the term "financial market" in this provision leads to undesirable uncertainty. There is no definition of this concept in any community instrument. The term is used in the particular context of Article 9 of the Insolvency Regulation but it is not defined. In the framework of a general conflict of law rule in Rome I this expression would lack precision and create legal uncertainty. Given the extreme diversity and complexity of the financial sector activities, there is a need to define all relevant concepts used.

Taking into account the universal scope of application of Rome I (Art. 2), the definition of markets and trading systems by reference to the EU regulatory categories in Directive 2004/39/EC (MiFID) has been avoided. This is because cross-reference to the MiFID concepts would limit the provisions to an EU context. Instead, the proposed draft contains a functional description of multilateral system that uses the common elements of the definitions of regulated market and multilateral trading facility in MiFID, together with the

condition that such systems should be subject to a single governing law. This description will cover all the equivalent non-EU trading facilities that need to be caught.

The second part deals with **possible overlaps between the scope of application of the protective rule on consumer contracts** (Art. 5 of the Rome I Proposal) **and the legal regime of financial instruments** (rights and obligations which comprise a financial instrument, contracts to subscribe for or purchase a new issue of transferable securities, contracts concluded within the type of system falling within the scope of the above mentioned Article 4(1)(j1)):

All these issues are not covered by Art. 5 of the Rome Convention as that Article only applies to contracts for the provision of services and sale of goods. The questions […] only arise due to the enlarged scope of Article 5 of the Rome I proposal.

The proposed text does not exclude contracts for the provision of financial services generally nor does it exclude contracts for the sale of shares and bonds concluded outside the systems referred to in the draft Art. 4(1)(j1).

As regards financial instruments, on the assumption that the exclusion from the scope of the Rome I proposal of financial instrument under Art. 1(2)(d) may not be exhaustive it is absolutely necessary to provide for this exclusion since without it the actual nature of a financial instrument – the rights and obligations that constitute its essence – could change by virtue of the application of Article 5. […]

Without an amendment to this effect, the actual nature of a financial instrument and the rules of law governing it could be various and unpredictable and would depend on the habitual residence of the person holding it. This question should not be confused with contracts for the provision of financial services. For example, when a bank sells to a consumer shares from company x it is providing a financial service. The consumer friendly rule of Article 5 of the proposal will naturally continue to apply to all these contracts that were already covered by Article 5 of the Rome Convention.

As regards the subscription for shares and units in collective investment schemes, and purchase of new issues of debt, it is important that the issuer in

relation to a single issue is not faced with a risk of application of multiple laws depending on the habitual residences of investors. This would effectively prevent cross-border retail offerings of shares, debt, etc. Contractual rights and obligations in relation to the subscription for or purchase of new issues of transferable securities will not necessarily be covered by the narrowly focussed exclusion discussed above for contracts which comprise financial instruments. […]

Thus, on the assumption and to the extent that this issue is not excluded entirely from the scope of the Regulation by virtue of Art. 1(2)(f) (exclusion of contracts governed by company law) it is necessary to ensure in relation to contracts of subscription for or purchase of a new issue of shares, bonds and other transferable securities that Article 5 does not apply.

As a last point, the Services of the Commission point out another **possible inconsistency between Art. 5 of the Rome I Proposal and the MiFID Directive (2004/39/EC)**, **as regards individual investors who act as "professional clients" under Annex II to the Directive**, but may be still considered as consumers for the purposes of the protective conflict rule:

Finally, the Committee may wish to consider an amendment to the text or at least a recital in order to clarify that individuals who 'opt up' to professional status under MiFID should not be treated as consumers for the purposes of Art. 5. Annex II to MiFID allows clients of investment firms, who would otherwise be classified as "retail clients" to be treated as "professional" clients if they meet specified conditions aimed at establishing that that client is financially sophisticated and experienced in investment. However, such clients may be considered to fall within the category of "consumers" for the purposes of Art. 5. The point is important since firms would be most unlikely to let sophisticated individuals opt up to professional status if Art. 5 were to apply to their dealings, and accordingly the objectives of the MiFID in this respect would be thwarted.