

Issues of Electronic Sale of Securities

إشكالات البيع الإلكتروني للقيم المنقولة

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Abstract: The electronic sale of securities represents a prominent success of digital commerce, significantly enhancing stock market investment. To ensure the utmost trust and confidentiality in online securities trading, these instruments have transitioned from physical documents to electronic accounting entries. This shift mandates that ownership transfer occurs not merely upon agreement between buyer and seller, but from the date of account registration. This process incorporates multiple intermediaries who facilitate the contract execution and the securities clearing and settlement, enabling transfer of ownership to the purchaser.

Keywords: Securities; Accounting Entries; Trading, Stock Market; Central Registration; Sale.

JEL Classification Codes : G12 ; G15 ; G19.

ملخص: يعد البيع الإلكتروني للأوراق المالية من أبرز تطبيقات التجارة الرقمية، وعاملاً أساسياً في تعزيز الاستثمار بالبورصة. ولضمان أقصى درجات الثقة والسرية في تداول الأوراق المالية عبر الإنترنت، تحولت هذه الأدوات من شكلها المادي إلى قيود حسابية إلكترونية. وبمقتضى هذا التحول، لم يعد انتقال الملكية يتم بمجرد التراضي بين البائع والمشتري، بل اعتباراً من تاريخ التسجيل في الحساب. تتضمن هذه العملية تدخل عدة وسطاء لتنفيذ العقد، كما تسهل المقاصة والتسوية عملية فرز الأوراق المالية ونقل ملكيتها إلى المشتري. **كلمات مفتاحية:** القيم المنقولة، القيود الحسابية، التداول، البورصة، القيد المركزي، البيع. **تصنيفات JEL :** G12 ; G15 ; G19.

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1. INTRODUCTION

The rapid advancement of digital communication technologies has significantly reshaped the financial market. This transformation has prompted numerous institutions to integrate digital platforms into their operations, adopting e-commerce practices over the internet. The electronic trading of securities is one such successful application, characterized by the digital nature of the e-commerce contract. Indeed, online sales contracts now influence commercial transactions considerably.

The principle of share transferability is foundational to joint-stock companies, since trading inherently involves conveying rights linked to securities from one party to another through legal processes.

The electronic system for trading securities plays a vital role in the success of stock market investments, where precision and prompt execution are critical. To enhance trust and speed in online securities trading, the Algerian legislator has enacted laws and protocols to guarantee the security and efficiency of these transactions. This has led to securities being transformed from their physical state into electronic accounting entries, transferred from seller to buyer through brokerage firms.

In view of the foregoing, the following question arises:

What is the legal nature of an electronic securities sale agreement?

To examine this, the study is organized into the following sections:

The contractual aspects of securities trading

The nature of securities ownership transfer in the stock market under general principles.

2. The contractual nature of securities trading operations

Securities form the fundamental commodities in stock exchange transactions. According to the Algerian Commercial Code, the legislator has defined the types of securities, their associated rights and obligations, and their issuance procedures (Ordinance 75/59, 2022). Specifically, articles 715 bis 30 to 715 bis 132 within Section Eleven of Chapter Three of the Code exhaustively cover securities trading for commercial companies.

The concept of share transferability is a primary feature of joint-stock entities. Essentially, trading refers to the transfer of entitlements linked to a security from one party to another, using legally defined methods. The Algerian legislator, in Article 715 bis 38 of the Algerian Commercial Code,

employs the term "transfer of the security". (Belgoudi, 2016, p. 28).

Hence, securities trading is a process of purchasing and selling that involves the transfer of ownership of a financial instrument through a sales contract.

2.1 Characterization of the Securities Sale Contract

To describe a securities sale contract, it is essential to determine: Is this sale an absolute sale contract, or a barter agreement?

2.1.1 Securities Sale as an Absolute Sale Contract

The sale of securities is recognized as an absolute sale when tangible securities are exchanged for cash. The bulk of trading deals are absolute sales, where assets are transferred in exchange for money (Ordinance 75/59, 2022).

2.1.2 Securities Sale as a Barter Contract

Conversely, securities sales may take the form of a barter arrangement when a security is exchanged for another asset, such as a different security or a tangible good. Here it is a barter transaction (asset-for-asset exchange), although the same legal principles apply as in absolute sales.

Among the various contracts for selling financial assets, the securities sale agreement is one of the most prevalent. A notable aspect is the direct involvement of the buyer and seller as the primary participants. However, in Algeria, securities sales now occur through exchange intermediaries who are direct parties to the contract (Legislative Decree 93/10, 1993), These intermediaries execute the trades registered on the stock exchange (Legislative Decree 93/10, 1993) ,thereby replacing the direct seller or buyer.

2.2 Comparison Between the Sale of Securities on the Stock Exchange and the Sale Contract in General Rules

While both share common characteristics and significant differences exist between the sale of securities on the stock exchange and sales agreements governed by general regulations. Stock exchange transactions are founded upon trading securities using intermediaries via the internet. They are

fundamentally conventional contracts, yet acquire an electronic dimension due to their mode of completion.

2.2.1 Distinguishing the Sale Contract in General Rules from the Sale of Securities on the Stock Exchange

Article 351 of the Algerian Civil Code establishes the definition of a standard sale contract. The standard sale contract diverges from securities sales in specific aspects:

- **Firstly:** A standard sale contract carries reciprocal obligations for both parties, with duties for both the seller and the buyer. However, in securities sales, the contract's direct participants are the intermediaries. These intermediaries act as substitutes for the direct seller and buyer (Al-Haddad, 2012, p. 22)) making the original parties only indirect parties to the agreement. This difference emerges from legal requirements that prohibit the seller and buyer from executing a securities sales agreement listed on the exchange directly; this responsibility is entrusted to financial institutions, and certified firms. (Legislative Decree 93/10, 1993).
- **Secondly:** A standard sale contract is a trade agreement, where the seller receives payment in return for transferring the asset, and the buyer receives the asset for the agreed price. In the case of securities, the asset is a financial instrument.
- **Thirdly:** Standard sales contracts are consensual, requiring only alignment between the seller and the buyer's intent and not requiring specific formats, at least when related to movable items. However, securities trading mandates specific procedures for contract execution, even though they are technically certificates of tangible movables.
- **Fourthly:** The sale contract transfers ownership. A key trait of a sales agreement is its capability to transfer ownership in exchange for payment, but this applies to specifically identified moveable items. In the case of a generically defined asset, the sales agreement only establishes the seller's obligation to transfer ownership, this ownership being transferred through segregation. However, the ownership of securities transfers upon account registration, a specification of the entire account.

2.2.2 Contracting Between the Seller and Buyer on the Stock Exchange

Securities trading on the stock exchange occurs indirectly through brokers representing both the buyer and the seller, utilizing a system of stock exchange orders. Brokers execute trades according to the most favorable prices, matching buy and sell orders.

Stock exchange orders represent authorization from a client to a broker to perform securities trades on their behalf (Yassin, 2004, p. 99). Client orders are entered by brokers into the exchange's system. However, brokers will only act upon receipt of a signed account agreement, with securities and cash deposited in an account that enables brokers to execute orders on the clients' behalves (Houadef, 2008, p. 61).

However, the digitization of securities has shifted the account agreement from between the broker and the customer to between the client and the qualified account holder. (Shaouch, 2005, p. 175).

3. Characterization of the Transfer of Securities Ownership on the Stock Exchange Under General Rules

The electronic sale of securities is a standard sales contract, even when concluded online. Therefore, conventional contract principles apply also to electronic contracts.

Traditionally, securities ownership transferred during a physical session where offer and acceptance occurred. Now, while the sale of securities is done remotely via brokers, it is still viewed as an immediate agreement, since the online agreement is treated as an agreement between parties, even within a virtual context (Fekir, 2017, p. 40).

The trading of financial instruments resembles sales agreements, and is generally subject to rules that govern such contracts and other rules specific to their traits.

3.1 The Contracting Mechanism in the Securities Exchange

Stock exchange intermediaries negotiate securities within the exchange after receiving client orders for purchase and sale (*Subsection One*). Additionally, the Central Securities Depository's settlement system allows for automated settlement of securities between intermediaries (*Subsection Two*).

3.1.1 Conducting Trading Sessions on the Stock Exchange

Trading starts when a client directs a broker. All securities transactions must be handled through financial intermediaries and the Central Securities Depository (Ismail, 2000, p. 400).

The pre-execution phase starts with the client instructing the intermediary about the specific type and quantity of securities they wish to trade (Regulation No. 03/02, 2003).

The account manager verifies the details, and documents the purchase order. If the order is to sell securities, the custodian blocks the designated shares in the client's account. The manager must then notify the broker about the share balance before documenting the order (Ismail, 2000, p. 400).

When buy and sell orders match, the Central Securities Depository completes the clearing and settlement. The conclusion of the contract on the stock market establishes the rights and obligations of both buyer and seller (Al-Masawra, 2012, p. 76).

3.1.2 Conducting Clearing and Settlement Sessions on the Stock Exchange

Historically, securities were paper certificates traded physically (Regulation No. 03/02, 2003). however, they now exist as central registrations, removing the need for their physical handling. Physical securities have been abolished, converted to intangible movables recorded in electronic accounts owned by their holders.

The transfer of securities is therefore electronic, through account-to-account transfers and the clearing and settlement is completed by the Central Securities Depository. Securities that have been deposited at the depository are automatically converted to electronic book-entry records in client accounts by opening a current account with the account manager.

According to Stock Exchange trading rules, the ownership transfers from seller to buyer upon the entry of the securities into the buyer's account, as declared by the agent. This exchange depends on the post-purchase clearing and settlement process that transfers the securities from the seller's account to the buyer's. This process is critical because a lack of

proper credit of the buyer's broker account renders the agreement void from the registration date. Thus, ownership shifts to the buyer on the account registration date (Hussein & Ibrahim, 2012, p. 266).

Therefore, brokerage and depository companies are the main direct parties to the contract while the seller and buyer remain as indirect parties. Therefore, the ownership is completed through the delivery between the brokerage and depository companies only upon the settlement process. (Belgoudi, 2016, p. 227).

3.2 Applying the Contracting Mechanisms in the Securities Exchange Under General Rules

Before identifying the challenges caused by the transfer of financial instruments, it is necessary to specify their nature.

3.2.1 The Nature of Securities

Following Law 03/04 on the Securities Exchange, financial instruments have been modified. Originally paper certificates, they are now account entries. The transfer of ownership only occurs through segregation and subsequent delivery, achieved through account-to-account transfers, as securities have become fungible assets.

What form does the delivery of accounting entries take?

- The transformation of the financial instrument's form: Central deposit rules transformed financial instruments from tangible paper certificates with serial numbers into account entries. These represent specific, fungible items that can be exchanged, with ownership transferring via electronic account-to-account transfers under central deposit rules.

This transformation is considered the delivery that achieves the segregation necessary for the ownership transfer of securities, now fungible movables in electronic format (Mohamed, 2015, p. 165).

- Delivery as segregation in the relationship between the financial intermediary and the Central Securities Depository:
- Delivery, which ensures the segregation of securities, occurs between

the financial intermediary and the Central Securities Depository. This segregation is complete after the custodian blocks the balance to complete the settlement, representing the segregation of securities, a direct effect of the sales contract.

3.2.2 Negative Effects of the Ownership Transfer Rule and Methods to Avoid Them

The negative effects of the ownership transfer rule, and ways to circumvent them, are outlined below:

A. Negative Effects of the Ownership Transfer Rule

The transfer rule, despite its necessity, has downsides during the transition of ownership. It particularly introduces problems related to rights tied to financial instruments and varying interpretations of ownership.

A crucial issue is asserting financial instrument rights. Determining who has authority over these rights during the period from trade execution to registration in the buyer's account is essential. Typically, ownership transfers to the buyer upon sale, which legally entitles them to full rights. However, stock market procedures complicate matters: The seller retains ownership records until registration is complete, allowing them to continue to exercise associated privileges such as voting or receiving dividends. However, the true owner (the buyer) is prevented from utilizing these rights because of the delayed registration.

This situation creates a conflict between legal theory and practical reality, with general rules vesting ownership in the buyer, whilst procedures mean sellers continue to enjoy privileges.

Another major challenge is the artificial inflation of owners due to delayed registration. Under general legal rules, transfer only occurs when the seller owns the securities, however under stock market rules the buyer is recognized as the owner immediately upon the contract's completion.

This causes a simultaneous recognition of the seller and the buyer as owners, albeit in different capacities. The seller is the registered owner, whilst the buyer is the legal owner under the contract, creating an inflated count that does not reflect true ownership and complicating the administration of rights.

These issues become more significant in high-volume trading contexts where delays in registration create distortions in the ownership records, undermining data accuracy and making the administration of rights more complex. Therefore, it is essential to ensure a smoother transfer of ownership.

B. Methods to Avoid the Negative Effects of the Ownership Transfer Rule

To manage these problems, authorities have developed a system that involves multiple intermediaries, such as brokers, account managers, and the Central Securities Depository, to expedite the execution of trades and ensure the accurate record of securities in new owner's accounts. The aim is to safeguard trading processes while limiting disputes about ownership.

These measures have changed the precise time when ownership legally transfers. While previously, it was seen to occur immediately upon conclusion of a sales contract, rules require ownership transfer only upon account registration. This is not a contravention of contract law, which calls for immediate transfer, but rather an application specific to digital financial instruments.

The rationale for this change is linked to the nature of fungible financial instruments, where transfer requires segregation of specific units for allocation to their correct owner.

The Central Securities Depository is key to this segregation. Upon completion of a trade, the depository will deduct units from the seller's account and credit them to the buyer's account. Simultaneously, cash payments are managed through secure channels to complete the transaction.

This process is a well-structured system designed to protect the rights of all parties. It ensures that sellers receive payment and buyers gain control of securities. The inclusion of intermediaries means that the process is in line with legal and procedural requirements, thereby lowering disputes and increasing the market's trustworthiness.

This framework helps to manage ownership in a dematerialized system while also meeting larger objectives, fostering a secure trading environment that contributes to market growth.

4. CONCLUSION

The transition to electronic accounting entries of securities has caused multiple challenges, specifically for the transfer of ownership. These issues relate to identifying the contractual parties and establishing the exact moment of legal transfer. Based on this analysis, we can conclude the following:

- **Delayed Ownership Transfer:** Ownership is postponed until the registration date. Thus, the seller can continue to exercise all rights linked to the securities until this point, such as attending meetings and voting. This creates a delay in the buyer being able to enjoy the same rights.
- **Difference Between Old and New Systems:** The transition to accounting entries by Law 03/04 is markedly different from old registration procedures. Under the new system, transfer happens through registration and settlement, whilst in the past the transfer was done upon mutual agreement, with the registration being an additional formality.
- **Condition-Based Ownership Transfer:** Transfer can be seen to be subject to a suspensive condition linked to completion of the settlement process, meaning that the buyer's rights are established upon completion of that process.
- **Recommendations**

To overcome the present difficulties and enhance efficiency and security, the following recommendations are presented:

- **Strengthening Legal Frameworks:** There is an immediate need to introduce legislation and regulatory guidelines that protect users of IT by establishing clear processes that safeguard the rights of all those involved in trading.
- **Fostering a Culture of Electronic Trading:** Promoting the adoption of electronic trading through a better understanding of these processes is essential. This involves facilitating the prompt transfer of trading orders to brokers, who are then responsible for entering these into the

electronic stock exchange system.

–**Verifying Broker Reliability:** Investors must diligently confirm the authenticity and trustworthiness of the brokers they will be dealing with to prevent fraud and ensure safe and transparent trade procedures.

To conclude, the digitization of securities trading has modernized the process, but requires regulatory action and education to overcome these challenges. By adopting these recommendations, the system can function with greater transparency and trust.

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