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Note by the Secretariat

Addendum

Contents

	<i>Page</i>
Chapter V. Priority of a security right	3
A. General rules	3
Article 27. Competing security rights	3
Article 28. Competing security rights in the case of advance registration	4
Article 29. Rights of buyers or other transferees, lessees or licensees of an encumbered asset	4
Article 30. Rights of buyers or other transferees, lessees or licensees of an encumbered asset in the case of specialized registration	5
Article 31. Rights of the insolvency representative	6
Article 32. Preferential claims	6
Article 33. Rights of judgement creditors	6
Article 34. Non-acquisition security rights competing with acquisition security rights ..	7
Article 35. Competing acquisition security rights	9

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Article 36. Acquisition security rights competing with the rights of judgement creditors	9
Article 37. Acquisition security rights in proceeds	9
Article 38. Subordination	10
Article 39. Future advances, future encumbered assets and maximum amount.	10
Article 40. Irrelevance of knowledge of the existence of a security right	10
B. Asset-specific rules.	10
Article 41. Negotiable instruments	10
Article 42. Rights to payment of funds credited to a bank account	11
Article 43. Money	11
Article 44. Negotiable documents and tangible assets covered.	12
Article 45. Intellectual property.	12
Article 46. Non-intermediated securities	12

Chapter V. Priority of a security right

A. General rules

Article 27. Competing security rights

1. Subject to articles 28-37, priority among competing security rights created by the same grantor in the same encumbered asset is determined according to the order of third-party effectiveness.

[2. Priority among competing security rights created by different grantors in the same encumbered asset is determined according to the order of third-party effectiveness[, provided that, upon transfer of the encumbered asset, the secured creditor of each grantor complies with the requirements of article 27, option A or B, [of the registry-related provisions] to preserve the third-party effectiveness and priority of its security right].]

[3.] The priority of a security right is not affected by a change in the method by which it is made effective against third parties, provided that there is no time period during which the security right is not effective against third parties.

[4.] The priority of a security right in the proceeds of an encumbered asset is the same as the priority of the security right in that asset.

[5.] If two or more security rights in the same tangible asset continue in a mass or product as provided in article 11, they retain the same priority as the security rights in the asset had as against each other immediately before the asset became part of the mass or product.

[6.] If security rights in separate tangible assets continue in the same mass or product and each security right is effective against third parties, the secured creditors are entitled to share in the aggregate maximum value of their security rights in the mass or product according to the ratio of the value of the respective security rights.

[7.] For the purposes of paragraph [6], the maximum value of a security right is the lesser of the value determined in accordance with article 11 and the amount of the secured obligation.

[8.] An acquisition security right in a separate tangible asset that continues in a mass or product and is effective against third parties has priority as against a security right granted by the same grantor in the mass or product.

[Note to the Working Group: The Working Group may wish to consider paragraph 2, which has been added within square brackets to deal with priority conflicts among security rights granted by different grantors (i.e. the grantor and successive transferees of the same encumbered asset). In this connection, the Working Group may wish to note that paragraph 2 may need to be coordinated with articles 18 and 19. The Working Group may also wish to note that paragraph 4 has been revised to deal with the priority of a security right in the proceeds of an encumbered asset, rather than with the time of third-party effectiveness, as recommendation 100 of the Secured Transactions Guide, on which it was originally based. The Working Group may also wish to consider whether paragraphs 5 and 6 of this article will need to be coordinated further with article 11.]

Article 28. Competing security rights in the case of advance registration

Option A

The priority of a security right with respect to which a notice has been registered in the Registry before the conclusion of a security agreement or, in the case of a security right in a future asset, before the grantor acquires rights in the asset or the power to encumber it, is determined according to the time of registration.

Option B

[For the purposes of articles 27, paragraph 1, 30, paragraph 1 and 33, paragraph 1, [...] in] [In] the case of a security right with respect to which a notice has been registered in the Registry before the conclusion of a security agreement or, in the case of a security right in a future asset, before the grantor acquires rights in the asset or the power to encumber it, the time of registration is treated as the time of third-party effectiveness [, provided that there is no period after the time of registration in which there is neither registration nor third-party effectiveness].

[Note to the Working Group: The Working Group may wish to note that this article has been included in the draft Model Law pursuant to a decision by the Working Group (see A/CN.9/830, para. 86) and consider the options offered. The Working Group may also wish to consider the heading and the scope of this article (that is, whether it should apply also in the case of competing security rights or also in the case of a priority conflict between a security right and the rights of a transferee of an encumbered asset (art. 30, para. 1) or a judgement creditor (art. 33, para. 1).]

Article 29. Rights of buyers or other transferees, lessees or licensees of an encumbered asset

1. If an encumbered asset is sold or otherwise transferred, leased or licensed and a security right in that asset is effective against third parties at the time of the sale or other transfer, lease or licence, a buyer or other transferee, lessee or licensee acquires its rights subject to the security right except as provided in this article.
2. A buyer or other transferee of an encumbered asset acquires its rights free of the security right, if the secured creditor authorizes a sale or other transfer of the asset free of the security right.
3. The rights of a lessee or licensee of an encumbered asset are not affected by a security right if the secured creditor authorizes the grantor to lease or license the asset unaffected by the security right.
4. A buyer of a tangible encumbered asset sold in the ordinary course of the seller's business acquires its rights free of the security right, provided that, at the time of the conclusion of the sale agreement, the buyer does not have knowledge that the sale violates the rights of the secured creditor under the security agreement.
5. The rights of a lessee of a tangible encumbered asset leased in the ordinary course of the lessor's business are not affected by the security right, provided that, at the time of the conclusion of the lease agreement, the lessee does not have

knowledge that the lease violates the rights of the secured creditor under the security agreement.

6. Subject to the rights of a secured creditor with a security right in intellectual property in accordance with article 45, the rights of a non-exclusive licensee of an intangible encumbered asset licensed in the ordinary course of the licensor's business are not affected by the security right, provided that, at the time of the conclusion of the licence agreement, the licensee does not have knowledge that the licence violates the rights of the secured creditor under the security agreement.

7. If a buyer or other transferee of a tangible encumbered asset acquires its rights free of a security right, any subsequent buyer or other transferee also acquires its rights free of that security right.

8. If the rights of a lessee of a tangible encumbered asset or licensee of an intangible encumbered asset are not affected by the security right, the rights of any sub-lessee or sub-licensee are also unaffected by that security right.

[Note to the Working Group: The Working Group may wish to consider whether it is sufficiently clear that exceptions to the rule in paragraph 1 apply only to buyers or other transferees, lessees or licensees for value, and not to donees or other gratuitous transferees, is sufficiently clear or whether the matter should be explicitly clarified in this article or in the Guide to Enactment (see Secured Transactions Guide, chap. V, para. 89).]

**Article 30. Rights of buyers or other transferees, lessees or licensees
of an encumbered asset in the case of specialized registration¹**

1. A security right in an asset that is made effective against third parties by registration in [the enacting State to specify the specialized registry or title certificate, if any] has priority over a security right in the same asset which is made effective against third parties by any other method.

2. If an encumbered asset is sold or otherwise transferred, leased or licensed and, at the time of the sale or other transfer, lease or licence, a security right in that asset is effective against third parties by registration in [the enacting State to specify the specialized registry or title certificate, if any], the buyer or other transferee, lessee or licensee acquires its rights subject to the security right, except as provided in paragraphs 2-8 of article 29.

3. If a security right in an asset that may be made effective against third parties by registration in [the enacting State to specify the specialized registry or title certificate, if any], has not been made effective against third parties by such registration, a buyer or other transferee acquires its rights free of the security right and a lessee's or licensee's rights are unaffected by the security right.

[Note to the Working Group: The Working Group may wish to note that the heading of this article does not reflect the contents of paragraph 1 and to consider whether: (a) the heading should be adjusted; or (b) paragraph 1 should be included in article 28, and paragraphs 2 and 3 should be included in article 29.]

¹ This rule is an example for the consideration of enacting States that have a specialized registration regime.

Article 31. Rights of the insolvency representative

[1.] A security right that is effective against third parties under this Law at the time of the commencement of insolvency proceedings with respect to the grantor remains effective against third parties and retains the priority it had before the commencement of the insolvency proceedings, unless another claim has priority pursuant to [the enacting State to specify its insolvency law].

[[2.] If a security right is effective against third parties at the time of commencement of insolvency proceedings with respect to the grantor, the secured creditor is entitled to take any action necessary to maintain the third-party effectiveness and priority the security right had before commencement of the insolvency proceedings.

[3.] An acquisition security right that is effective against third parties by the registration of a notice in the Registry after the commencement of insolvency proceedings with respect to the grantor and within the period specified in article 34, subparagraph (a)(ii), has the priority under this Law that it acquires as a result of such registration.]

[Note to the Working Group: The Working Group may wish to note that paragraph 1 is based on recommendation 4 of the UNCITRAL Legislative Guide on Insolvency Law and recommendations 238 and 239 of the Secured Transactions Guide, paragraph 2 is based on recommendation 238 of the Secured Transactions Guide (see A/CN.9/830, para. 87) and paragraph 3 is intended to state explicitly what is implicit in paragraph 1 of this article and article 34. As these recommendations refer to what the insolvency law should provide, the Working Group may wish to consider whether this article should be deleted.]

Article 32. Preferential claims

The following claims arising by operation of other law have priority over a security right that is effective against third parties but only up to [the enacting State to specify the amount for each category of claim]:

- (a) [...];
- (b) [...].²

Article 33. Rights of judgement creditors

1. Subject to the rights of acquisition secured creditors in accordance with article 36, the rights of an unsecured creditor that has obtained a judgement or provisional order (“judgement creditor”) have priority over a security right, if, before the security right is made effective against third parties, the judgement creditor [has taken the steps to be specified by an enacting State for a judgement creditor to acquire rights in the encumbered asset or to refer to the relevant provisions of other law with respect to judgements or provisional court orders].

² The enacting State will not need this article if it does not have any preferential claims.

2. The priority of the rights of the judgement creditor referred to in paragraph 1 does not extend to credit disbursed by the secured creditor:

(a) Within [the enacting State to specify a short period of time, such as 30 days] from the time the judgement creditor notified the secured creditor that it had taken the steps referred to in paragraph 1; or

(b) Pursuant to an irrevocable commitment in a fixed amount or an amount to be fixed pursuant to a specified formula of the secured creditor to extend credit, if the commitment was made before the judgement creditor notified the secured creditor that it had taken the steps referred to in paragraph 1.

[The Working Group may wish to consider whether the judgement creditor should have priority under paragraph 2 only if the secured creditor received the notification and, if so, whether this matter should be clarified in paragraph 2 of this article, another article for the receipt rule to apply throughout the draft Model Law or in the Guide to Enactment.]

Article 34. Non-acquisition security rights competing with acquisition security rights³

Option A⁴

1. Except as provided in article 30 with respect to a security right that is made effective against third parties by registration in [the enacting State to specify the specialized registry or title certificate, if any]:

(a) An acquisition security right in an asset other than inventory, consumer goods, intellectual property or rights of a licensee under a licence of intellectual property, held by the grantor [primarily] for sale or licence in the ordinary course of the grantor's business or used or intended to be used by the grantor [primarily] for personal, family or household purposes, has priority over a competing non-acquisition security right created by the grantor, provided that:

(i) The acquisition secured creditor is in possession of or has acquired the asset; or

(ii) A notice with respect to the acquisition security right is registered in the Registry within [a short period of time to be specified by the enacting State] after the grantor obtains possession of or acquires the asset;

(b) An acquisition security right in inventory, intellectual property or rights of a licensee under a licence of intellectual property, held by the grantor [primarily]

³ This section includes the unitary-approach recommendations of the *Secured Transactions Guide*. If a State prefers to adopt the non-unitary approach recommendations, it may wish to consider implementing instead recommendations 187-202 of the *Secured Transactions Guide*. [In particular, States may wish to consider doing so if they have implemented regional legislation along the Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions (the "Late Payment Directive"), article 9 of which, provides that "Member States shall provide in conformity with the applicable national provisions designated by private international law that the seller retains title to goods until they are fully paid for if a retention of title clause has been expressly agreed between the buyer and the seller before the delivery of the goods".]

⁴ A State may adopt option A or option B of this article.

for sale or licence in the ordinary course of the grantor's business has priority over a competing non-acquisition security right created by the grantor, provided that:

- (i) The acquisition secured creditor is in possession of or has acquired the asset; or
 - (ii) Before the grantor obtains possession of or acquires the asset:
 - a. A notice with respect to the acquisition security right is registered in the Registry; and
 - b. A notice that is sent by the acquisition secured creditor is received by the non-acquisition secured creditor that has registered a notice in the Registry with respect to a security right created by the grantor in an asset of the same kind, stating that the acquisition secured creditor has or intends to acquire an acquisition security right and describing the asset sufficiently to enable the non-acquisition secured creditor to identify the asset that is the object of the acquisition security right; and
 - (c) An acquisition security right in consumer goods, intellectual property or rights of a licensee under a licence of intellectual property, used or intended to be used by the grantor [primarily] for personal, family or household purposes, has priority over a competing non-acquisition security right created by the grantor in the same asset.
2. A notice that is sent in accordance with subparagraph 1(b)(ii)b., may cover acquisition security rights under multiple transactions between the same parties without the need to identify each transaction and is sufficient only for security rights in assets of which the grantor obtains possession or which the grantor acquires within [a period of time to be specified by the enacting State] after the notice is received.

Option B

Except as provided in article 30:

- (a) An acquisition security right in an asset other than consumer goods, intellectual property or rights of a licensee under a licence of intellectual property, used or intended to be used by the grantor [primarily] for personal, family or household purposes, has priority as against a competing non-acquisition security right created by the grantor, provided that:
 - (i) The acquisition secured creditor is in possession of or acquires the asset; or
 - (ii) A notice with respect to the acquisition security right is registered in the Registry within [a short period of time to be specified by the enacting State] after the grantor obtains possession of or acquires the asset; and
- (b) An acquisition security right in consumer goods, intellectual property or rights of a licensee under a licence of intellectual property, used or intended to be used by the grantor [primarily] for personal, family or household purposes, has priority over a competing non-acquisition security right created by the grantor in the same asset.

[Note to the Working Group: The Working Group may wish to note that subparagraph 1(b)(ii)b. of option A refers to a notice received by an earlier registered inventory financier.]

Article 35. Competing acquisition security rights

1. Subject to paragraph 2, the priority between competing acquisition security rights is determined according to article 27.
2. An acquisition security right of a seller or lessor, or a licensor of intellectual property, that was made effective against third parties within the period specified in article 34, subparagraph (a)(ii), has priority over a competing acquisition security right of a secured creditor other than a seller or lessor, or a licensor of intellectual property.

Article 36. Acquisition security rights competing with the rights of judgement creditors

An acquisition security right that is made effective against third parties within the period specified in article 34, subparagraph (a)(ii), has priority over the rights of a judgement creditor that would otherwise have priority under article 32.

Article 37. Acquisition security rights in proceeds⁵

Option A

1. A security right in proceeds of an asset other than inventory, consumer goods, intellectual property or rights of a licensee under a licence of intellectual property, held by the grantor [primarily] for sale or licence in the ordinary course of the grantor's business or used or intended to be used by the grantor [primarily] for personal, family or household purposes, has the same priority as the acquisition security right in that asset.
2. A security right in proceeds of inventory, intellectual property or rights of a licensee under a licence of intellectual property, held by the grantor [primarily] for sale or licence in the ordinary course of the grantor's business, has the same priority as the acquisition security right in that asset, except where the proceeds take the form of receivables, negotiable instruments, or rights to payment of funds credited to a bank account.
3. A security right in proceeds has the same priority as the security right in that asset, provided that the acquisition secured creditor notifies non-acquisition secured creditors that, before the proceeds arose, the acquisition secured creditor registered a notice with respect to assets of the same kind as the proceeds in the Registry.

Option B

Notwithstanding article 34, the priority of an acquisition security right in a tangible asset, intellectual property or rights of a licensee under a licence of intellectual property that is effective against third parties does not extend to its proceeds.

⁵ A State may adopt option A of this article, if it adopts option A of article 34, or option B of this article if it adopts option B of article 34.

Article 38. Subordination

1. A person may at any time subordinate its priority under this Law in favour of any existing or future competing claimant without the need for the beneficiary to be a party to the subordination.
2. Subordination does not affect the rights of competing claimants other than the person subordinating its priority and the beneficiary of the subordination.

[Note to the Working Group: The Working Group may wish to consider: whether: (a) a subordination agreement has to be in writing or may also be oral; (b) the Guide to Enactment should explain whether, if third-party effectiveness of the security right has been established by registration of a notice, an amendment notice may be registered to reflect the new order of priority; and (c) the rule that an agreement cannot affect third parties (art. 4, para. 2) is not enough to cover unilateral subordination and thus paragraph 2 of this article is necessary and should be retained.]

Article 39. Future advances, future encumbered assets and maximum amount

1. Subject to the rights of judgement creditors under article 32, the priority of a security right extends to all secured obligations, including obligations incurred after the security right became effective against third parties.
2. The priority of a security right covers all encumbered assets described in a notice registered in the Registry, irrespective of whether they are acquired by the grantor or come into existence before or after the time of registration.
- [3. The priority of the security right is limited to the maximum amount set out in the notice registered in the Registry.]⁶

Article 40. Irrelevance of knowledge of the existence of a security right

Knowledge of the existence of a security right on the part of a secured creditor does not affect its priority under this Law.

B. Asset-specific rules

Article 41. Negotiable instruments

1. A security right in a negotiable instrument that is made effective against third parties by possession of the instrument has priority over a security right in the instrument that is made effective against third parties by registration of a notice in the Registry.
2. A buyer or other consensual transferee of an encumbered negotiable instrument acquires its rights free of the security right that is made effective against third parties by registration of a notice in the Registry if the buyer or other consensual transferee:

⁶ This provision will be necessary if the enacting State implements articles 6, subparagraph 3(e), and 9, subparagraph (e) [of the registry-related provisions].

(a) Qualifies as a protected holder [the enacting State may wish to use any other term used in its law]; or

(b) Takes possession of the negotiable instrument and gives value [the enacting State may wish to use any other term used in its law] without knowledge that the sale or other transfer is in violation of the rights of the secured creditor under the security agreement.

Article 42. Rights to payment of funds credited to a bank account

1. A security right in a right to payment of funds credited to a bank account that is made effective against third parties by the secured creditor becoming the account holder has priority over a competing security right that is made effective against third parties by any other method.
2. A security right in a right to payment of funds credited to a bank account with respect to which the secured creditor is the depositary bank has priority over a competing security right made effective against third parties by any method other than by the secured creditor becoming the account holder.
3. A security right in a right to payment of funds credited to a bank account that is made effective against third parties by a control agreement has priority over a competing security right other than a security right of the depositary bank or a security right that is made effective against third parties by any method other than by the secured creditor becoming the account holder.
4. The order of priority among competing security rights in a right to payment of funds credited to a bank account that are made effective against third parties by the conclusion of control agreements is determined on the basis of the time of conclusion of the control agreements.
5. A depositary bank's right under other law to set off obligations owed to it by the grantor against the grantor's right to payment of funds credited to a bank account maintained with the depositary bank has priority as against a security right in the right to payment of funds credited to the bank account, except a security right that is made effective against third parties by the secured creditor becoming the account holder.
6. A transferee of funds from a bank account pursuant to a transfer initiated or authorized by the grantor acquires its rights free of a security right in the right to payment of funds credited to the bank account, unless the transferee has knowledge that the transfer violates the rights of the secured creditor under the security agreement.
7. Paragraph 6 does not adversely affect the rights of transferees of funds from bank accounts under [the enacting State to specify the relevant law].

Article 43. Money

1. A transferee that obtains possession of money that is subject to a security right acquires its rights free of the security right, unless that person has knowledge that the transfer violates the rights of the secured creditor under the security agreement.
2. This article does not adversely affect the rights of persons in possession of money under [the enacting State to specify the relevant law].

Article 44. Negotiable documents and tangible assets covered

1. Subject to paragraph 2, a security right in a tangible asset made effective against third parties by possession of the negotiable document covering that asset has priority over a competing security right made effective against third parties by any other method.
2. Paragraph 1 does not apply to a security right in a tangible asset other than inventory if the security right of the secured creditor not in possession of the negotiable document was made effective against third parties before the earlier of:
 - (a) The time that the asset became covered by the negotiable document; and
 - (b) The time of conclusion of an agreement between the grantor and the secured creditor in possession of the negotiable document providing for the asset to be covered by a negotiable document so long as the asset became so covered within [a short period of time to be specified by the enacting State] from the date of the agreement.
3. A transferee of an encumbered negotiable document under [the enacting State to specify the relevant law under which certain transferees of negotiable documents acquire their rights free of competing claims] acquires its rights free of a security right in the negotiable document and the tangible assets covered thereby that is made effective against third parties by registration of a notice in the Registry or by possession of the documents or the assets covered thereby.

Article 45. Intellectual property

Article 29, paragraph 6, does not affect any rights that a secured creditor may have [as an owner or licensor of intellectual property] under [the relevant law relating to intellectual property to be specified by the enacting State].

Article 46. Non-intermediated securities

1. A security right in certificated non-intermediated securities made effective against third parties by the secured creditor's possession of the certificate has priority over a competing security right by the same grantor in the same securities made effective against third parties by registration of a notice in the Registry.
2. A security right in uncertificated non-intermediated securities made effective against third parties by a notation of the security right or registration of the name of the secured creditor as the holder of the securities in the books maintained for that purpose by or on behalf of the issuer has priority over a security right in the same securities made effective against third parties by any other method.
3. A security right in uncertificated non-intermediated securities made effective against third parties by the conclusion of a control agreement has priority over a security right in the same securities made effective against third parties by registration of a notice in the Registry.
4. The order of priority among competing security rights in uncertificated non-intermediated securities that are made effective against third parties by the conclusion of control agreements is determined on the basis of the time of conclusion of the control agreements.

Option A

5. This article does not adversely affect the rights of holders of non-intermediated securities under [the enacting State to specify the relevant law relating to the transfer of securities].

Option B

5. A buyer or other consensual transferee of encumbered non-intermediated securities under [the enacting State to specify the relevant law relating to the transfer of securities] acquires its rights free of the security right.
