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Draft Guide to Enactment of the draft Model Law on Secured Transactions

Note by the Secretariat

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I. Purpose of the Guide to Enactment

1. In preparing and adopting the [draft] UNCITRAL Model Law on Secured Transactions (the "Model Law"), the United Nations Commission on International Trade Law ("UNCITRAL" or the "Commission") was mindful of the fact that the Model Law would be a more effective tool for States modernizing and harmonizing their legislation, as well as organizations assisting States, if background and explanatory information were provided to executive and legislative branches of Government to assist in their consideration of the Model Law for enactment (the "Guide to Enactment").[1]

2. In addition, the Commission was aware that in the preparation of the Model Law it was assumed that the Model Law would be accompanied by such a Guide to Enactment. For example, it was decided in respect of a number of issues not to settle them in the Model Law but to address them in the Guide so as to provide guidance to States enacting the Model Law (see, for example, paras. 68 and 124 below). Thus, the Guide to Enactment also addresses or clarifies matters that were not settled in the Model Law but were referred to in the Guide to Enactment.[2]

3. Moreover, when it referred the task of the preparation of the Guide to Enactment to the Working Group, the Commission agreed that the Guide to Enactment should: (a) be as short as possible; (b) include cross-references to the UNCITRAL Legislative Guide on Secured Transactions (the "Secured Transactions Guide") and the other texts of the Commission on secured transactions; (c) focus on giving guidance to legislators rather than users of the text; (d) explain the thrust of each provision of the Model Law and any difference with the corresponding recommendations of the Secured Transactions Guide or the provisions of another UNCITRAL text on secured transactions; and (e) give guidance to States with respect to matters referred to them and in particular explain each option offered in various articles of the Model Law to assist enacting States in choosing one of the options offered.[3]

4. Mindful of the fact that the Secured Transactions Guide contains extensive commentary, the Commission decided that the Guide to Enactment should nevertheless be prepared. The reason was that the commentary of the Secured Transactions Guide had a different structure and did not contain a straightforward discussion of each recommendation but rather a discussion of the comparative advantages and disadvantages of various workable approaches with the recommendation being set out as a conclusion of that discussion. At the same time, to avoid repetition, the Commission agreed that the Guide to Enactment should not repeat, but should rather incorporate by reference, those comments contained in the Secured Transactions Guide that could assist in explaining a provision of the Model Law.

5. The Commission was also aware of the likelihood that the Model Law would be used in a number of States with limited familiarity with the type of secured transaction covered by in the Model Law. So, the Guide to Enactment, much of

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[1] *Official Records of the General Assembly, Seventieth Session, Supplement No. 17* (A/70/17) para. 215.

[2] Ibid.

[3] Ibid., para. 216.

which is drawn from the travaux préparatoires of the Model Law, is also intended to be helpful to other users of the text, such as judges, arbitrators, practitioners and academics.

6. In view of the above, the information presented in the Guide to Enactment is intended to briefly explain the thrust of each provision of the Model Law and its relationship with the corresponding recommendation(s) of the Secured Transactions Guide or other UNCITRAL texts on secured transactions, including the Supplement on Security Rights in Intellectual Property (the "Intellectual Property Supplement"), the United Nations Convention on the Assignment of Receivables in International Trade (the "Assignment Convention") and the UNCITRAL Guide on the Implementation of a Security Rights Registry (the "Registry Guide").

7. The Guide to Enactment was prepared by the Secretariat and is based on the considerations of the Working Group and the Commission. [It was considered and approved in principle by the Working Group at its [thirtieth] and [thirty-first] sessions (see […] respectively) and by the Commission at its [fiftieth] session (see […]).[4]]

II. Purpose and origin of the Model Law

A. Purpose of the Model Law

8. The Model Law is designed to assist States in implementing the recommendations of the Secured Transactions Guide, the Intellectual Property Supplement and the Registry Guide with respect to security rights in movable assets. The overall objective of those texts and the Model Law is to promote low-cost credit by enhancing the availability of secured credit (see Secured Transactions Guide, rec. 1, subpara. (a)). Like all those texts, the Model Law is intended to be useful to States that do not currently have efficient and effective secured transactions laws, as well as to States that already have workable laws but wish to modernize their laws and harmonize them with the laws of other States whose secured transactions laws are generally consistent with the recommendations of those texts (see Secured Transactions Guide, Introduction, para. 1).

9. Thus, the provisions of the Model Law are based on the recommendations of the Secured Transactions Guide, including the Intellectual Property Supplement. The Model Registry-related Provisions are also based on the Registry Guide. The provisions of the Model Law on security rights in receivables are substantially based on the recommendations of the Secured Transactions Guide, which in turn are based on the Assignment Convention.

B. Background

10. At its first session, in 1968, the Commission included the topic of security interests in goods in its future work programme.[5] From its third session in, 1970, to

[4] Ibid., [*Seventy-second Session, Supplement No. 17* (A/72/17), para. […].]
[5] Ibid., *Twenty-third Session, Supplement No. 16* (A/7216), paras. 40-48.

its thirteenth session, in 1980, the Commission discussed the topic[6] and, at its thirteenth session, in 1980, decided that no further work should be carried out and the subject should no longer be accorded priority as "the world-wide unification of the law of security interests in goods, for the reasons brought out in the discussions, was in all likelihood unattainable".[7]

C. Preparatory work and adoption

11. At its forty-third session, in 2010, the Commission had before it a note by the Secretariat on possible future work in the area of security interests (A/CN.9/702 and Add.1). The Commission agreed that four issues related to secured transactions law listed in document A/CN.9/702, paragraph 2(a)-(d), were interesting (non-intermediated securities, registration of security rights, a model law and a contractual guide on secured transactions) and should be retained on its future work agenda.[8] At the same time, in view of the limited resources available to it, the Commission agreed that it could not undertake work on all four issues at the same time and that, as a result, it should set priorities. In that regard, there was general agreement that priority should be given to work on registration of security rights in movable assets.

12. At that session, the Commission decided that Working Group VI should be entrusted with the preparation of a text on registration of security rights in movable assets as a matter of priority. It was also agreed that other topics, such as security rights in non-intermediated securities, a model law based on the recommendations of the Guide and a text dealing with the rights and obligations of the parties should be retained in the future programme of Working Group VI for further consideration by the Commission at a future session on the basis of notes to be prepared by the Secretariat within the limits of existing resources.[9]

13. At its forty-fifth session, in 2012, the Commission decided that, upon its completion of the Registry Guide, Working Group VI should undertake work to prepare a simple, short and concise model law on secured transactions based on the Secured Transactions Guide and consistent with all texts prepared by UNCITRAL on secured transactions.[10] At that session, the Commission noted that the Working Group, at its twenty-first session, had agreed to propose to the Commission that the Working Group should develop a model law on secured transactions based on the general recommendations of the Secured Transactions Guide and consistent with all the texts prepared by UNCITRAL on secured transactions. It was also noted that the Working Group had agreed to propose to the Commission that the topic of security rights in non-intermediated securities should be retained on its work agenda and be considered at a future session (A/CN.9/743, para. 76).[11]

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[6] For this project, see www.uncitral.org/uncitral/uncitral_texts/security_past.html.

[7] *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 28.

[8] Ibid., *Sixty-fifth session, Supplement No. 17* (A/65/17), para. 264.

[9] Ibid., para. 268.

[10] Ibid., *Sixty-seventh Session, Supplement No. 17* (A/67/17), para. 105.

[11] Ibid., para. 101.

14. Recalling that, at its forty-third session, in 2010, the Commission had agreed that the topics mentioned above should be retained on the programme of the Working Group for further consideration, the Commission considered the proposals of the Working Group. It was widely felt that a simple, short and concise model law on secured transactions could usefully complement the Secured Transactions Guide and would be extremely useful in addressing the needs of States and in promoting implementation of the Secured Transactions Guide. While a concern was expressed that a model law might limit the flexibility of States to address the local needs of their legal traditions, it was generally viewed that a model law could be drafted in a sufficiently flexible manner to adapt to various legal traditions. Moreover, there was support for the idea that a model law could greatly assist States in addressing urgent issues relating to access to credit and financial inclusion, in particular for small and medium-sized enterprises.[12]

15. As to the topic of security rights in non-intermediated securities, it was widely felt that the topic merited further consideration. The Commission noted that non-intermediated securities, in the sense of securities other than those credited to a securities account, that were used as security for credit in commercial finance transactions were excluded from the scope of the Secured Transactions Guide (see rec. 4, subparas. (c)-(e) of the Guide), the Unidroit Convention on Substantive Rules for Intermediated Securities (Geneva, 2009; the "Unidroit Securities Convention") and the Convention on the Law Applicable to Certain Rights in respect of Securities held with an Intermediary (The Hague, 2006; the "Hague Securities Convention").[13]

16. At its twenty-third session, in 2013, Working Group VI had a general exchange of views on the basis of a note prepared by the Secretariat entitled "Draft Model Law on Secured Transactions" (A/CN.9/WG.VI/WP.55 and Add.1 to 4).[14] The Working Group developed the Model Law in six one-week sessions,[15] the final taking place in February 2016.

17. At its forty-seventh session, in 2014, the Commission expressed its satisfaction for the considerable progress achieved by the Working Group in its work and requested the Working Group to expedite its work so as to complete the draft Model Law, including certain definitions and provisions on non-intermediated securities (see A/CN.9/811), and to submit it to the Commission for adoption together with a guide to enactment as soon as possible.

18. At its forty-eighth session, in 2015, the Commission considered and approved the substance of article 26 of chapter IV of the Model Law and articles 1-29 of the draft Registry Act.[16] At that session, the Commission also agreed that a guide to

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[12] Ibid., paras. 102 and 103.

[13] Ibid., para. 104.

[14] See A/CN.9/767, paras. 63 and 64.

[15] The reports of the Working Group on its work during these 6 sessions are contained in documents A/CN.9/796, A/CN.9/802, A/CN.9/830, A/CN.9/836, A/CN.9/865 and A/CN.9/871. During these sessions, the Working Group considered documents A/CN.9/WG.VI/WP.57 and Add.1 to 4, A/CN.9/WG.VI/WP.59 and Add.1, A/CN.9/WG.VI/WP.61 and Add.1 to 3, A/CN.9/WG.VI/WP.63 and Add.1 to 4, A/CN.9/WG.VI/WP.65 and Add.1 to 4, and A/CN.9/WG.VI/WP.68 and Add.1 and 2.

[16] *Official Records of the General Assembly, Seventieth Session, Supplement No. 17* (A/70/17), para. 214.

enactment of the Model Law should be prepared and referred that task to the Working Group.[17]

19. In preparation for the forty-ninth session of the Commission, the text of the Model Law as approved by Working Group VI was circulated to all Governments and to interested international organizations for comment. At that session, the Commission had before it the reports of the Working Group on its twenty-eighth and twenty-ninth sessions (A/CN.9/865 and A/CN.9/871), the Model Law (A/CN.9/884 and Add.1-4), the Guide to Enactment prepared by the Secretariat (A/CN.9/885 and Add.1-4) and the comments received from Governments (A/CN.9/886 and A/CN.9/887). At that session, the Commission […].

20. After consideration of the Model Law, the Commission adopted the following decision:

[…].[18]

III. The Model Law as a tool for modernizing and harmonizing laws

21. The Model Law is in the form of a legislative text that is recommended to States for incorporation into their national law. Unlike an international convention, model legislation does not require the State enacting it to notify the United Nations or other States that may have also enacted it. However, States are strongly encouraged to inform the UNCITRAL secretariat of any enactment of the new Model Law (or any other model law resulting from the work of UNCITRAL). This information may be made available on the UNCITRAL website to send the message that the enacting State has adopted an international standard and, in any case, assist other States in their consideration of the Model Law.

22. In incorporating the text of model legislation into its legal system, a State may wish to consider modifying or leaving out some of its non-fundamental provisions. In the case of a convention, the possibility of changes being made to the uniform text by the States parties (normally referred to as “declarations”) is much more restricted; trade law conventions in particular usually either totally prohibit declarations or allow only very few, specific ones. The flexibility inherent in model legislation is particularly desirable in those cases where it is likely that the State would wish to make various modifications to the uniform text before it would be ready to enact it as national law. Some modifications may be expected, in particular when the uniform text is closely related to the national court and procedural system. This, however, also means that the degree of harmonization achieved through model legislation is likely to be lower than that achieved by a convention.

23. However, this relative disadvantage of model legislation may be balanced by the fact that the number of States enacting model legislation is likely to be higher than the number of States adhering to a convention. In order to achieve a satisfactory degree of modernization, harmonization and certainty, it is

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[17] Ibid., para. 216.

[18] Ibid., [*Official Records of the General Assembly, Seventy-first Session, Supplement No. 17* (A/71/17), para. […].]

recommended that States make as few changes as possible in incorporating the new Model Law into their legal systems and that they take due regard of its basic principles, including the unitary, functional and comprehensive approach to secured transactions, notice registration, party autonomy and the international origin of the Model Law. In general, in enacting the Model Law, it is advisable to adhere as much as possible to the uniform text in order to make the national law as efficient as possible for all users and as transparent and familiar as possible for foreign users. This does not deprive enacting States of the necessary flexibility as the Model Law provides options and leaves a number of matters to enacting States.

24. While it is recommended that the Model Law should be implemented in one law, depending on its legal tradition and drafting conventions, the enacting State may implement the Model Registry-related Provisions in its secured transactions law, in a separate statute or other type of legal instrument, such as rules, regulations, orders, by-laws, proclamations or the like adopted by a legislative or executive body, or some of these Provisions in its secured transactions law and the rest in a separate statute or other type of legal instrument. Similarly, the conflict-of-laws provisions may be incorporated in the secured transactions law (at the beginning or at the end of it) or in a separate law (civil code or other law).

IV. Main features of the Model Law

A. Relationship of the Model Law with the secured transactions texts of UNCITRAL

25. The Secured Transactions Guide, including the Intellectual Property Supplement, and the Registry Guide contain detailed commentary and recommendations on all issues to be addressed in a modern law on secured transactions. However, they are long texts and States will need assistance in implementing their recommendations. Thus, the Model Law was prepared to complement those texts and to assist States in implementing their recommendations.

26. The Model Law reflects the policies embodied in the recommendations of those texts. The difference in the formulation between a provision of the Model Law and the relevant recommendation is generally due to the legislative nature of the Model Law and is briefly explained in the remarks to the relevant provision of the Model Law below.

27. For reasons explained below, the Model Law also addresses matters that were not addressed in a recommendation or even discussed in the Secured Transactions Guide, including the Intellectual Property Supplement, or in the Registry Guide (e.g. security rights in non-intermediated securities and the effectiveness of the registration of an amendment or cancellation notice that has not been authorized by the secured creditor). At the same time, the Model Law does not address certain matters that were addressed in the Secured Transactions Guide (e.g. security rights in the right to receive the proceeds under an independent undertaking and security rights in attachments).

B. Key objectives and fundamental policies of the Model Law

28. The overall objective of the Model Law is the same as that of the Secured Transactions Guide, that is, to promote low-cost credit by enhancing the availability of secured credit (see Secured Transactions Guide rec. 1 and Introduction, paras. 43-59). The fundamental policies of the Model Law are the same as those of the Secured Transactions Guide (see Secured Transactions Guide, Introduction, paras. 60-72). In enacting the Model Law, States may wish to consider issues of harmonization with existing law, legislative method, drafting technique and post-enactment acculturation (see Secured Transactions Guide, Introduction, paras. 73-89).

29. Depending on its drafting method and technique, the enacting State may wish to consider including the key objectives of the Model Law in a preamble or other statement of objectives of the law. That statement could be used for the purpose of the interpretation of, and the filling of gaps in, the Model Law (see paras. 75 and 76 below).

V. Assistance from the UNCITRAL secretariat

A. Assistance in drafting legislation

30. In the context of its training and assistance activities, the UNCITRAL secretariat assists States with technical consultations for the preparation of legislation based on the Model Law. The same assistance is brought to Governments considering legislation based on other UNCITRAL model laws (e.g. the UNCITRAL Model Law on Cross-Border Insolvency, the UNCITRAL Model Law on International Commercial Arbitration and the UNCITRAL Model Law on International Commercial Conciliation) or considering adhesion to one of the international trade law conventions prepared by UNCITRAL (e.g. the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit (New York, 1995) and the Assignment Convention).

31. Further information concerning the Model Law and other model laws and conventions developed by UNCITRAL, may be obtained from the UNCITRAL secretariat at the address below:

International Trade Law Division, Office of Legal Affairs
United Nations
Vienna International Centre
P.O. Box 500
A-1400 Vienna, Austria
Telephone: (+43-1) 26060-4060 or 4061
Telecopy: (+43-1) 26060-5813
Electronic mail: uncitral@uncitral.org
Internet home page: www.uncitral.org

B. Information on the interpretation of legislation based on the Model Law

32. The UNCITRAL secretariat welcomes comments concerning the Model Law and the Guide to Enactment, as well as information concerning enactment of legislation based on the Model Law. Once enacted, the Model Law will be included in the CLOUT information system, which is used for collecting and disseminating information on case law relating to the conventions and model laws that have emanated from the work of UNCITRAL. The purpose of the system is to promote international awareness of the legislative texts formulated by UNCITRAL and to facilitate their uniform interpretation and application. The UNCITRAL secretariat publishes, in the six official languages of the United Nations, abstracts of decisions and arbitral awards. In addition, upon individual request and subject to any copyright and confidentiality restrictions, the UNCITRAL secretariat makes available to the public all decisions and arbitral awards on the basis of which the abstracts were prepared. The system is explained in a user's guide that is available from the UNCITRAL secretariat in hard copy (A/CN.9/SER.C/GUIDE/1/Rev.2) and on the above-mentioned Internet home page of UNCITRAL.

VI. Article-by-article remarks

Chapter I. Scope of application and general provisions

Article 1. Scope of application

33. Article 1 is based on recommendations 1-7 of the Secured Transactions Guide (see chap. I, paras. 1-4). It is intended to set out the various types of transaction and asset covered by the Model Law (see art. 1, paras. 1-4), as well as to clarify the relationship between the Model Law and other law (see art. 1, paras. 5 and 6). Generally, the Model Law has the same comprehensive scope of application as the Secured Transactions Guide and applies to any property right in any type of movable asset, such as equipment, inventory and receivables, provided that the property right is created by an agreement and secures payment or other performance of an obligation (see art. 1, para. 1, and the definition of the term "security right" in art. 2, subpara. (ii)). However, there are a few differences between the scope of the Model Law and the scope of the Secured Transactions Guide.

34. Like the Secured Transactions Guide (see rec. 3) and the Assignment Convention (see art. 1, para. 1, and art. 2, subpara. (a)), the Model Law also applies to outright transfers of receivables (see art. 1, para. 2). The main reasons for this approach are that: (a) outright transfers of receivables take place in the context of financing transactions; and (b) it is sometimes difficult to determine at the outset of a transaction whether an assignment will be held to be an outright or a security assignment (see Secured Transactions Guide, chap. I, paras. 25-31). The enacting State may wish to consider excluding from the scope of the Model Law certain types of outright transfers of receivables that are not financing transactions (e.g. outright transfers of receivables for collection purposes only or as part of a sale of the business out of which they arose; see para. 39 below).

35. In addition, unlike the Secured Transactions Guide which covered security rights in the right to receive payment under an independent undertaking (see rec. 2, subpara. (a)), the Model Law excludes from its scope security rights in both the right to receive and the right to request payment under an independent guarantee or letter of credit, whether commercial or standby (see art. 1, subpara. 3(a)). The reason is that there are various specialized financing practices in those areas and dealing with them in the Model Law would be unduly complex. States interested in addressing those practices in their general secured transactions law can always implement the relevant recommendations of the Secured Transactions Guide (recs. 27, 50, 107, 127, 176 and 212).

36. Moreover, like the Secured Transactions Guide (see rec. 4, subpara. (b)), to the extent that its provisions are inconsistent with law relating to intellectual property, the Model Law defers to law relating to intellectual property (see art. 1, subpara. 3(b)). This limitation may not be necessary if the enacting State has already coordinated or otherwise addressed the relationship between the Model Law and its law relating to intellectual property.

37. Also, unlike the Secured Transactions Guide (see rec. 4, subpara. (c)), the Model Law does not exclude from its scope security rights in non-intermediated securities (see art. 1, subpara. 3(c)). The reasons for this approach are that: (a) such securities often are part of commercial finance transactions (in which, for example, it is common for the lender's security to include in the assets to be encumbered shares of the borrower's wholly-owned subsidiaries or the shares of the borrower itself); (b) there are wide divergences among national regimes in this regard; and (c) such securities are not addressed in any other uniform law text. To the contrary, security rights in intermediated securities are excluded as such securities are typically part of financial market transactions and are addressed in other uniform law texts; see Secured Transactions Guide, chap. 1, paras. 37 and 38).

38. Finally, the Model Law excludes payment rights under or from financial contracts governed by netting agreements (see art. 1, subpara. 3(d)), including foreign exchange transactions, because they raise complex issues that require special rules (see Secured Transactions Guide, chap. I, para. 39).

39. Combining the policy of recommendations 4, subparagraph (a), and 7 of the Secured Transactions Guide, the Model Law permits the enacting State to exclude further types of asset (or transaction), provided that other law governs the matters that are addressed in the Model Law (see art. 1, subpara. 3(e)). The reason for this approach is to avoid inadvertently creating gaps (where other law does not govern an issue addressed in the Model Law) or overlaps (where other law governs an issue addressed in the Model Law). In addition, the Model Law provides guidance to States as to possible exclusions, referring to types of asset, such as ships and aircraft, that are subject to specialized secured transactions and asset-based registration regimes.

40. Similarly, with respect to the application of the Model Law to proceeds, while the relevant provision of the Model Law (see art. 1, para. 4), is formulated somehow differently from recommendation 6 of the Secured Transactions Guide, there is no policy difference between the two rules. The policy may be explained as follows. In the case of a security right in an asset covered by the Model Law (e.g. receivables), the security right extends to its identifiable proceeds (see art. 10, para. 1); this rule

applies even if the proceeds are of a type of asset that is outside the scope of the Model Law (e.g. as intermediated securities), except other law applies and governs the matters addressed in the Model Law.

41. With respect to the relationship with consumer protection law, the Model Law is intended to preserve the application of consumer protection law that protects a grantor or a debtor of an encumbered receivable (see art. 1, para. 5, of the Model Law rec. 2, subpara. (b), of the Secured Transactions Guide and art. 4, para. 4, of the Assignment Convention). For example, under consumer-protection law, it may not be possible to create a security right in all present and future assets, employment benefits, at least up to a certain amount, or necessary household items of a consumer. Enacting States that do not have a developed consumer-protection law may need to consider whether enactment of the Model Law should be accompanied by the enactment of such special protections for consumers. It should also be noted that the Model Law already includes certain consumer-specific rules. For example, under article 23, an acquisition security right in consumer goods is effective against third parties upon its creation (see also para. 119 below).

42. Following the approach of the Secured Transactions Guide (see rec. 18), the Model Law (see art. 1, para. 6), is intended to preserve limitations to the creation or the enforceability of a security right in certain types of asset (e.g. employment benefits) that are based on any other statutory or case law. At the same time, it is intended to ensure that such limitations based on the sole ground that an asset is a future asset or a part or undivided interest in an asset are overridden (see art. 8, paras. (a) and (b)). However, paragraph 6 does not apply to contractual limitations (also known as negative pledge agreements). The Model Law overrides explicitly contractual limitations on the creation of a security right in receivables (see art. 13) or rights to payment of funds credited to a bank account (see art. 15). [With respect to other types of asset, contractual limitations on the creation of a security right are overridden implicitly to the extent that the Model Law allows the owner of an asset to create a security right in that asset, even if the security or other agreement expressly restricts that right. The Model Law does not condition the creation, third-party effectiveness or priority of a security right in an asset on the grantor having the right to encumber it (art. 6, para. 1, refers also to the "power to encumber"; see para. 78 below). However, the rights and obligations of third-party obligors are determined by the other law (see arts. 59-69).]

43. Finally, unlike the Secured Transactions Guide, the Model Law does not apply to attachments to movable or immovable property. Thus, the Model Law does not include a provision along the lines of recommendation 5, which provides that, while the law recommended in the Secured Transactions Guide does not apply to immovable property, it does apply to attachments to immovable property. Enacting States are encouraged to include in their enactments of the Model Law provisions based on the relevant recommendations of the Secured Transactions Guide (see recs. 21, 25, 43, 48, 87, 88, 164, 165, 184, 195 and 196).

Article 2. Definitions and rules of interpretation

44. Article 2 contains definitions and rules of interpretation with respect to most key terms used in the Model Law. Other terms are defined or explained in various articles of the Model Law. For example, the term "registry" is defined in article 1, subparagraph (k), of the Model Registry-related Provisions. Article 2 is based on the

terminology and rules of interpretation of the Secured Transactions Guide (see Secured Transactions Guide, Introduction, paras. 15-20). Rules of interpretation include the following: (a) the word "or" is not intended to be exclusive; (b) the singular includes the plural and vice versa; and (c) the words "include" or "including" are not intended to indicate an exhaustive list (see Secured Transactions Guide, Introduction, para. 17).

Acquisition security right

45. An acquisition security right is a security right that secures the grantor's obligation with respect to credit provided to enable the grantor to acquire a tangible asset (other than reified intangible assets; see art. 2, subparas. (b) and (jj)), intellectual property and the rights of a licensee in intellectual property. This definition, in conjunction with the definition of "security right," results in retention-of-title transactions, conditional sales and financial leases being treated in the Model Law as "acquisition security rights." For a security right to be an acquisition security right, the credit it secures has to be used for that purpose. Where a security right secures obligations in addition to the credit extended and used for the purpose of acquiring the encumbered asset, it is an ordinary security right to the extent of those additional obligations.

Bank account

46. To underline the distinction between a "bank account" and a "securities account", the Model Law defines: (a) the former term as "an account maintained by [essentially, a deposit taking institution] to which funds may be credited or debited"; (b) the latter term as "an account maintained by an intermediary to which securities may be credited or debited"; and (c) the term "securities" in a manner that clearly excludes funds (see art. 2, subparas. (c), (gg) and (ff) respectively). The term "bank account", therefore, includes any current or checking and savings account. The term does not include a right against the bank to payment evidenced by a negotiable instrument. The enacting State may wish to consider including a definition of the term "bank" in its secured transactions law or rely for this purpose on other law.

Certificated non-intermediated securities

47. The term "represented" used in the definition of the term "certificated non-intermediated securities" (see art. 2, subpara. (d)) is broad enough to cover the approaches taken in different jurisdictions (e.g. "covered" or "embodied"). The term "certificate" means only a tangible document subject to physical possession. Thus, securities represented by an electronic certificate are considered to be uncertificated securities under the Model Law.

Competing claimant

48. A competing claimant may have a right in the same encumbered asset as original encumbered asset or as proceeds (see art. 2, subpara. (e)). Other creditors of the grantor with a right in the same encumbered asset include judgement creditors.

Consumer goods

49. Unlike the definition of the term "consumer goods" in the Secured Transactions Guide on which it is based, the definition of the term in the Model Law (see art. 2, subpara. (f)) includes the word "primarily" to ensure that: (a) goods used primarily for personal family or household purposes and only incidentally for business purposes would be treated as consumer goods; and (b) goods used primarily for business purposes and only incidentally for personal, family or household purposes would not be treated as consumer goods.

Control agreement

50. While the effect of a control agreement is to render a security right effective against third parties (see art. 18), its purpose is to ensure: (a) the cooperation of the depositary institution or the issuer of securities in the enforcement of a security right; and (b) the priority of the secured creditor that has control. Unlike the definition of this term in the Secured Transactions Guide, on which it is based, the definition of the term in the Model Law does not refer to a "signed writing" (see art. 2, subpara. (g)). This difference does not reflect a policy change but rather a decision that this matter should be left to the authorization requirements of the enacting State. In any case, a control agreement does not need to be in a single writing. It should also be noted that, on the assumption that other law would address this matter, the Model Law does not include a provision implementing the recommendations of the Secured Transactions Guide with respect to electronic communications (see Secured Transactions Guide, recs. 11 and 12).

Equipment

51. Unlike the definition of the term "equipment" in the Secured Transactions Guide on which it is based, the definition of the term in the Model Law includes the word "primarily" to ensure that: (a) goods used by a person primarily in the operation of its business and only incidentally for other purposes would be treated as equipment; and (b) goods used by a person primarily for other purposes and only incidentally in the operation of its business would not be treated as equipment (see art. 2, subpara. (l)). This definition also includes the words "or intended to be used" to ensure that goods are treated as equipment as long as their intended use is in the operation of a person's business. This definition also includes the words "other than inventory" to draw a distinction between "equipment" and "inventory".

Insolvency representative

52. As defined in the Model Law (see art. 2, subpara. (p)), the term "insolvency representative" is sufficiently broad to include the person responsible for administering or supervising insolvency proceedings (see UNCITRAL Legislative Guide on Insolvency Law (the "Insolvency Guide"), part two, chap. III, paras. 11-18 and 35).

Intangible asset

53. The term "intangible asset" includes receivables, rights to the performance of obligations other than receivables, rights to payment of funds credited to a bank

account and uncertificated non-intermediated securities, as well as any asset other than a tangible asset (see art. 2, subpara. (q)).

Inventory

54. In States in which a licence of tangible assets is possible, the term "lease of tangible assets" in this definition includes the licence of tangible assets (see art. 2, subpara. (r)).

Money

55. The term "money", whose definition is based on a definition contained in the Secured Transactions Guide, is intended to include not only the national currency (i.e. banknotes and coins, as well as virtual currency, such as bitcoin) of the enacting State but also the currency of another State (see art. 2, subpara. (u)) No reference is made to currency "currently" authorized as a legal tender, because if currency is not "currently" authorized as a legal tender, it would not qualify as a legal tender. Rights to payment of funds credited to a bank account and negotiable instruments are recognized as distinct concepts in the Model Law and they are not included in the term "money".

Non-intermediated securities

56. The term "non-intermediated securities" refers to securities (i.e. shares and bonds) that are not held in a securities account (see art. 2, subpara. (v)). The term does not include the rights of an intermediary or a competing claimant in securities held by the intermediary directly against the issuer where equivalent securities are credited by the intermediary to a securities account in the name of the grantor.

Notification of a security right in a receivable

57. The definition of the term "notification of a security right in a receivable" is based on the definition of the term "notification of the assignment" and recommendation 118 of the Secured Transactions Guide (see art. 2, subpara. (y)). The requirement for the identification of the encumbered receivable and the secured creditor was moved to article 60, paragraph 1, as it states a substantive rule on the effectiveness of a notification of a security right, a matter that is already addressed in that article.

Possession

58. […]

Priority

59. The definition of the term "priority" is based on the definition in article 5, subparagraph (g), of the Assignment Convention (see art. 2, subpara. (aa)). The difference in its formulation from the formulation of the definition of the term in the Secured Transactions Guide is due to the need to clarify that the person with priority may be a person with a security right or another competing claimant.

Proceeds

60. The term "proceeds" in the Model Law has the same meaning as in the Secured Transactions Guide (see art. 2, subpara. (bb)). It is important to note that it covers: (a) proceeds of the sale or other disposition, lease or licence of an encumbered asset (broadly understood); (b) proceeds of proceeds; and (c) natural or civil fruits. The terms revenues, dividends and distributions, which were included in the definition of this term in the Secured Transactions Guide, have been deleted on the understanding that they are covered by the term "civil fruits".

61. The term is not limited to proceeds received by the grantor but includes proceeds received by a transferee of an encumbered asset. The reason for this approach is that, if such a limitation were imposed, a transferee of an encumbered asset that acquired the asset subject to the security right could sell the asset further and keep the proceeds free of the security right. This result would limit the extent to which the secured creditor would be actually secured, in particular if the value of the encumbered asset diminished or the proceeds disappeared or were difficult to trace. In addition, transferees are anyway protected by other provisions of the Model Law. For example, a security right in certain types of identifiable proceeds is effective against third parties only for a short period of time and, thereafter, only if it is made effective against third parties by one of the relevant methods of third-party effectiveness (see. art. 19, para. 2); and a buyer or other transferee of an encumbered asset acquires its rights free of the security right, if the secured creditor authorized the sale or other transfer free of the security right, or if the sale or other transfer was in the ordinary course of business of the seller or other transferor (see art. 32, para. 2).

62. However, it should be noted that, as a result of the approach of the Model Law, in certain circumstances, third-party transferees would have no way of finding out that the assets were proceeds of another asset in which somebody else had a security right. This would apply be the case at least where the proceeds would be cash proceeds and a security right in such proceeds would be effective against third parties without the registration of an amendment notice (see art. 19, para. 1, of the Model Law and art. 26, option C, of the Model Registry-related Provisions). Thus, the enacting State may wish to consider limiting the term "proceeds" to proceeds received by the grantor or consider other ways to avoid a prejudice to third-party financiers (e.g. requiring the registration of an amendment notice in the case of a transfer of an encumbered asset; see art. 26, option A or B, of the Model Registry-related Provisions or protecting good faith transferees).

Receivable

63. Like the Secured Transactions Guide, the Model Law defines the term "receivable" in a broad way to cover even non-contractual receivables, such as tort receivables (see art. 2, subpara. (cc)). However, the term "receivable" does not include rights to payment evidenced by a negotiable instrument, rights to payment of funds credited to a bank account and rights to payment under a non-intermediated security, as they are treated as distinct types of asset that are subject to different asset-specific rules.

Secured obligation

64. The term "secured obligation" includes any obligation secured by a security right, including obligations arising from credit extended to finance the operation of a business or the purchase of goods (see art. 2, subpara. (ee)). It includes: (a) monetary and non-monetary obligations (see art. 2, subpara. (ii)); and (b) obligations already incurred at the time of the extension of the credit, as well as obligations incurred thereafter, if the security agreement so provides. As in other UNCITRAL texts, in the Model Law also the singular includes the plural and vice versa (see para. 44 above). So, for example, a reference to the secured obligation would be sufficient to cover all present and future secured obligations.

Securities

65. The definition of the term "securities" in the Model Law is narrower than the definition of the term in article 1, subparagraph (a), of the Unidroit Securities Convention (see art. 2, subpara. (ff)). The reason is that, while a broad definition is appropriate for the purposes of that Convention, it is overly broad for the purposes of the Model Law and could result in subjecting security rights in receivables, negotiable instruments, money and other generic intangible assets to the special rules applicable to security rights in non-intermediated securities. In any case, each enacting State would need to coordinate the definition of the term "securities" in its secured transactions law with the definition of the term in its securities transfer law.

Securities account

66. The definition of the term "securities account" in the Model Law is derived from article 1, subparagraph (c), of the Unidroit Securities Convention (see art. 2, subpara. (gg)).

Tangible asset

67. The term "tangible asset" in the Model Law includes consumer goods, equipment and inventory. These terms do not refer to subcategories of tangible assets but rather to the way in which particular tangible assets are used by the grantor (see art. 2, subpara. (jj)). Thus, the same cars could qualify as "consumer goods", if they are used by the grantor for personal, family or household purposes, as "equipment", if they are used by the grantor in the operation of its business, or as "inventory", if the grantor is a car dealer or manufacturer. The term also includes the reified intangible assets listed in the definition except for the purposes of certain articles that contain rules that are non-applicable to reified intangible assets.

International obligations of this State

68. The Model Law leaves to the enacting State the issue whether international treaties (such as the Assignment Convention) prevail over domestic law. For example, in the case of a conflict between a provision of the Model Law and a provision of any treaty or other form of agreement to which an enacting State is a party with one or more other States, the requirements of the treaty or agreement may prevail (see art. 3 of the UNCITRAL Model Law on Cross-Border Insolvency). Such an approach may need to be limited to international treaties that directly address matters governed by the Model Law. In other States, in which international

treaties are not self-executing but require internal legislation in order to become enforceable law, such an approach might be inappropriate or unnecessary (see Guide to Enactment and Interpretation of the UNCITRAL Model Law on Cross-Border Insolvency, paras. 91-93).

Article 3. Party autonomy

69. Article 3 is based on article 6 of the Assignment Convention (the first sentence of which is based on art. 6 of the United Nations Convention on Contracts for the International Sale of Goods ("CISG")) and recommendation 10 of the Secured Transactions Guide. It is intended to reflect the principle that, with the exception of the provisions listed in article 3, parties are free to vary by agreement the effect of the provisions of the Model Law as between them.

70. An agreement referred to in paragraph 1 may be not only between the secured creditor and the grantor but also between the secured creditor or the grantor and other parties whose rights may be affected by the Model Law, such as the debtor of an encumbered receivable, or between the secured creditor and a competing claimant.

71. Paragraph 2 reiterates the general principle that an agreement between two parties cannot affect the rights of a third party. The reason for stating a general principle of contract law is that the Model Law deals with relationships in which an agreement between two parties (e.g. the grantor and the secured creditor) might have or inadvertently appear to have an impact on the rights of third parties (e.g. the debtor of a receivable).

Article 4. General standards of conduct

72. Article 4 is based on recommendation 131 of the Secured Transactions Guide (see chap. VII, para. 15). It is included in chapter I on the scope of application and general provisions, rather than in chapter VII on enforcement, as it states a standard of conduct with which parties should comply when they exercise their rights and perform their obligations under the Model Law, even outside the context of enforcement. Under article 4, any person must exercise all its rights and perform all its obligations under the Model Law in good faith and in a commercially reasonable manner. The violation of this obligation may result in liability in damages and other consequences that are left to the relevant law of the enacting State.

73. The concept of "commercial reasonableness" refers to the commercial transaction context and best practices. Meeting the specific standards referred to in other provisions of the Model Law (e.g. art. 76, para. 4, according to which notice is to be given within a short period of time) should generally be construed as meeting the general standards of conduct referred to in this article.

74. Article 4 is listed in article 3 as a mandatory law rule. As a result, the duty to act in good faith and in a commercially reasonable manner cannot be waived or varied by agreement.

Article 5. International origin and general principles

75. Article 5 is inspired by article 7 of the CISG and based on article 3 of the UNCITRAL Model Law on Electronic Commerce, article 4 of the UNCITRAL Model Law on Electronic Signatures and article 2A of the UNCITRAL Model Law

on International Commercial Arbitration. It is intended to limit the extent to which a national law implementing the Model Law would be interpreted only by reference to concepts of national law.

76. The Model Law is a tool not only for modernizing but also for harmonizing secured transactions laws (see paras. 21-24 above). To promote harmonization, paragraph 1 provides that the provisions of a national law implementing the Model Law should be interpreted with reference to its international origin and the observance of good faith. Paragraph 2 is intended to provide guidance with respect to the filling of gaps in a law implementing the Model Law by reference to the general principles on which the Model Law is based (see paras. 28 and 29 above).

Chapter II. Creation of a security right

A. General rules

Article 6. Creation of a security right

77. Article 6 is based on recommendations 13-15 of the Secured Transactions Guide (see chap. II, paras. 12-37). Its purpose is to deal with the creation of a security right, as well as the form and the minimum content of a security agreement, so as to enable parties to obtain a security right in a simple and efficient manner (see Secured Transactions Guide, rec. 1, subpara. (c)). A security right is created by agreement, for the content of which there are no requirements other than those listed in paragraphs 3 and 4, and for the conclusion of which no terms of art need be used.

78. Under paragraph 1, an agreement is sufficient to create a security right, provided that at the time of the conclusion of the security agreement the grantor has either a right in the asset to be encumbered or the power to encumber it. This is the case, for example, where: (a) the grantor is the owner of the asset; and (b) the grantor is in possession of the asset on the basis of a security agreement (including a retention-of title sale or conditional lease) with the owner ("possession" is defined as actual possession; see art. 2, subpara. (z)). In addition, it should be noted that a transferor of a receivable can continue to have a right in or the power to encumber the receivable, even if it has already transferred the receivable. Moreover, it should be noted that, in the case of an anti-assignment agreement between the owner/grantor and the debtor of a receivable, the owner/grantor may not have the right as against the debtor of the receivable to transfer or encumber the receivable, but does have a right in the receivable, and also the power to encumber it. Paragraph 2 clarifies that, in the case of future assets (i.e. assets produced or acquired by the grantor after the conclusion of the security agreement; see definition in art. 2, subpara. (n)), the security right is created when the grantor acquires rights in them or the power to encumber them.

79. Paragraph 3 sets out the requirements that a written security agreement has to meet. Whether written or oral, a security agreement creates a security right but need not use any special words to achieve that result (see art. 2, subpara. (hh)). From the two alternative wordings set out in paragraph 3 within square brackets, the enacting State may wish to select the one that is most fitting to its contract law. If the enacting State retains the words "concluded in", a security agreement that is not in written form is not effective. If the enacting State retains the words "evidenced by",

a security agreement that is not in written form is in principle effective but its existence may only be evidenced by a writing.

80. Depending on what it considers as most efficient financing practices and reasonable assumptions of market participants, the enacting State may wish to consider whether to retain subparagraph 3(d). One approach is to retain subparagraph 3(d) to facilitate the grantor's access to secured financing from other creditors in situations where the value of the assets encumbered by the prior security right exceeds the maximum amount indicated in the notice registered with respect to that right. Another approach is to leave out subparagraph 3(d) to facilitate the grantor's access to credit by the first secured creditor (for the comparative advantages and disadvantages of the two approaches, see Secured Transactions Guide, chap. IV, paras. 92-97).

81. Under paragraph 4, where the secured creditor is in possession of the encumbered asset, there is no need for a written security agreement and thus the existence of a security agreement may be concluded in or evidenced by any other means.

Article 7. Obligations that may be secured

82. Article 7 is based on recommendation 16 of the Secured Transactions Guide (see chap. II, paras. 38-48). It is primarily intended to ensure that future, conditional and fluctuating obligations may be secured. The main reason for this approach is to facilitate modern financing transactions, in the context of which disbursements are made at different times depending on the needs of the grantor (e.g. revolving credit facilities for the grantor to buy inventory). This approach does not preclude the introduction of special protections for grantors (e.g. setting a maximum amount for which the security right may be enforced; see art. 6, subpara. 3(d); or limiting the creation of a security right in or the transferability of specific types of movable asset, such as employment benefits in general or up to a specific amount; see art. 1, para. 6).

Article 8. Assets that may be encumbered

83. Article 8 is based on recommendation 17 of the Secured Transactions Guide (see chap. II, paras. 49-57 and 61-70). It is primarily intended to ensure that future movable assets, parts of movable assets and undivided rights in movable assets, generic categories of movable assets, as well as all movable assets of a person, may become the subject of a security right.

84. It should be noted that the fact that future movable assets may be subject to a security right does not mean that statutory limitations to the creation or enforcement of a security right in specific types of movable asset (e.g. employment benefits in general or up to a specific amount) are overridden (see art. 1, para. 6).

85. It should also be noted that the fact that all movable assets of a grantor may be subject to a security right so as to maximize the credit that may be available and improve the terms of the credit agreement does not mean that other creditors of the grantor are necessarily unprotected. The protection of other creditors (within and outside insolvency proceedings) is a matter of other law and is foreseen in articles 33 and 34 of the Model Law.

Article 9. Description of encumbered assets

86. Article 9 is based on recommendation 14, subparagraph (d), of the Secured Transactions Guide (see chap. II, paras. 58-60). In view of their importance, the requirements for the description of encumbered assets in a security agreement are presented in a separate article. Article 9 is intended to ensure that a security right may be created in an asset or class of assets even if the description in the security agreement is generic, such as "all inventory" or "all receivables" (see Secured Transactions Guide, chap. II, paras. 58-60).

Article 10. Right to proceeds and commingled funds

87. Article 10 is based on recommendations 19 and 20 of the Secured Transactions Guide (see chap. II, paras. 72-89). Paragraph 1 is intended to ensure that, unless otherwise agreed by the parties (as this article is not listed in article 4 as a mandatory law rule), a security right in an asset automatically extends to its identifiable proceeds. The rationale for this rule is that it reflects the normal expectations of the parties and ensures that the secured creditor is sufficiently secured. Otherwise, a grantor could effectively deprive a secured creditor of its security either by disposing of those assets to a person who would take free of the security right or to a person from whom those assets could not easily be recovered.

88. By way of example, where the original encumbered asset is inventory, the cash or receivables generated from the sale of the inventory are proceeds. If upon payment of the receivables the funds received are deposited in a bank account, the right to payment of the funds credited to the bank account are also proceeds of the inventory. So, is a check issued by the holder of that bank account to buy new inventory and a warehouse receipt issued by the warehouse in which new inventory may be stored.

89. Paragraph 2 introduces an exception to the identifiability requirement in paragraph 1. A security right in an asset extends to its proceeds in the form of funds that are commingled with other funds even though the funds that are proceeds cannot be identified separately from the funds that are not proceeds (see subpara. 2(a)).

90. Subparagraph 2(b) limits that security right to the value of the proceeds immediately before they were commingled. So, if a sum of €1,000 is deposited in a bank account and at the time of enforcement the bank account has a balance of €2,500, the security right extends to the sum of €1,000.

91. Subparagraph 2(c) deals with situations in which the balance in the bank account fluctuates and, at some point of time, is less than the value of the proceeds deposited (e.g. less than €1,000). In such a case, the security right extends to the lowest value between the time when the proceeds were commingled and the time the security right in the proceeds is claimed. So, if in the example given, the balance in the account when the proceeds were deposited was €1,500, then it went down to €500 and at the time of enforcement was €750, the security right extends to €500 (i.e. the lowest intermediate balance).

Article 11. Tangible assets commingled in a mass or product

92. Article 11 is based on recommendations 22 and 91 of the Secured Transactions Guide (see chap. II, paras. 90-95 and 100-102, and chap. V, paras. 117-123). It accomplishes three related objectives. First, it transforms the security right in the original asset into a security right in the mass or product. Second, it limits the value of that security right by tying its value to the value of the original asset in the mass or product. Third, it addresses situations in which more than one secured creditor has a claim to a mass or product as a result of a security right in its components.

93. Paragraph 1 is intended to ensure that a security right in assets commingled in a mass or product, even though they are no longer identifiable, continues in the mass or product.

94. Under option A, the security right that extends to a mass or product is limited to the value of the encumbered assets immediately before they were commingled and became part of the mass or product. So, if a secured creditor has a security right in €100,000 worth of oil (100,000 litres at €1 per litre) that is commingled with €50,000 worth of oil in the same tank and thus the mass has €150,000 worth of oil, the security right encumbers €100,000 worth of oil.

95. Under option B, the same rule applies only to products (see para. 3). So, if encumbered flour worth €100 is commingled and bread worth €500 is produced, the security right is limited to €100. But option B (see para. 2) contains a different rule with respect to tangible assets commingled in a mass. In the example just given, the security right is limited to two thirds of the value of the oil (i.e. €100,000 worth of oil).

96. It should be noted that the word “limited” in paragraph 2 of option A and paragraphs 2 and 3 of option B means that, if the value of the encumbered asset commingled in the mass or product increases after commingling, the increased value is unencumbered. In other words, the secured creditor does not benefit from commodity price increases (see Secured Transactions Guide, chap. V, para. 118 ad finem). Similarly, the word “limited” does not address the question of what is the amount secured if the price of the encumbered asset decreases after commingling. The rule applicable to all types of encumbered asset applies to tangible assets commingled in a mass or product, namely that each party bears the risk of decreases of the price of the encumbered asset. Thus, in the example given above, if, at the time of enforcement, the value of the mass is only €75,000 because of a drop on oil prices (€0.5 per litre), the secured creditor should be able to enforce its security right against only €50,000 worth of oil. If the value of the oil goes up (€1.5 per litre), the secured creditor should not benefit from it as its claim is sufficiently secured and thus should be able to enforce its security right against €100,000 worth of oil (not €150,000).

Article 12. Extinguishment of a security right

97. Article 12 deals with the extinguishment of a security right, which triggers the obligation of a secured creditor to return an encumbered asset or register an amendment or cancellation notice (see art. 52 of the Model Law and art. 20, subpara. 3(c), of the Model Registry-related Provisions). Article 12 refers to full payment or other satisfaction of all present and future secured obligations, including conditional obligations. This means that a security right is extinguished only where

there is full payment or other satisfaction of the secured obligation and there is no longer any commitment of the secured creditor to extend further credit. As a result, the security right is not extinguished where temporarily there is a zero balance but there is an existing commitment of the secured creditor to extend further credit (e.g. on the basis of revolving credit arrangement).

B. Asset-specific rules

Article 13. Contractual limitations on the creation of a security right

98. Article 13 is based on recommendation 24 of the Secured Transactions Guide (see chap. II, paras. 106-110 and 113), which in turn is based on article 9 of the Assignment Convention. Paragraph 1 provides that an agreement limiting the grantor's right to create a security right in the receivables listed in paragraph 4 (often referred to as "trade receivables") does not prevent the creation of a security right where such an agreement exists. The rationale underlying this approach is to facilitate the use of receivables as security for credit, which is in the interest of the economy as a whole, without unduly interfering with party autonomy. This rule does not affect statutory limitations to the creation or enforcement of a security right in certain types of receivable (e.g. consumer or sovereign receivables; see art. 1, paras. 5 and 6).

99. Paragraph 2 makes it clear that, while under paragraph 1 a security right is effective notwithstanding an agreement to the contrary, the grantor is not excused from any liability to its counter-party for damages caused by breach of that contractual provision, if such liability exists under other law. Thus, under paragraph 2, if the debtor of the receivable has sufficient negotiating power to force the creditor/grantor to accept the inclusion of an "anti-assignment clause" in their agreement and a breach of that agreement by the grantor results in a loss to the debtor of the receivable, the grantor is liable to the debtor of the receivable for damages under contract law. However, the debtor of the receivable may not avoid the contract because of that breach or raise against the secured creditor (assignee) any claim it may have against the grantor for that breach; in addition, under paragraph 3, a secured creditor that accepts a receivable as security for credit is not liable to the debtor of the receivable for the grantor's breach just because it had knowledge of the "anti-assignment clause". Otherwise, the anti-assignment agreement would in effect prevent a secured creditor from obtaining a security right in a receivable covered by the anti-assignment agreement.

100. As a result of the rules in paragraphs 1-3, a secured creditor does not have to examine each contract from which a receivable might arise to determine whether it contains an anti-assignment clause. This facilitates transactions relating to pools of receivables that are not specifically identified (with respect to which a search of the underlying transactions is possible but not necessarily time- or cost-efficient), as well as transactions relating to future receivables (with respect to which such a search would not be possible at the time of the conclusion of the security agreement).

101. Paragraph 4 limits the scope of the rule in paragraph 1 to broadly defined trade receivables. It does not apply to so-called "financial receivables", because, where the debtor of the receivable is a financial institution, even partial invalidation of an

anti-assignment clause could affect obligations undertaken by the financial institution towards third parties (see Secured Transactions Guide, para. 108).

102. Article 13 applies also to anti-assignment agreements limiting the creation of a security right in any personal or property rights securing or supporting payment or other performance of an encumbered receivable or other intangible asset, or negotiable instrument (see art. 14).

Article 14. Personal or property rights securing or supporting payment or other performance of an encumbered receivable or other intangible asset, or negotiable instrument

103. Paragraph 1 reflects the thrust of recommendation 25 of the Secured Transactions Guide (see chap. II, paras. 111-122). It is intended to ensure that a secured creditor with a security right in a receivable or another of the assets described in paragraph 1 automatically has the benefit of any personal right that supports payment or other performance of the receivable (e.g. a guarantee) and any property right that secures such payment or other performance (e.g. a security right in another asset). For example, if a receivable is secured by a guarantee or mortgage, the secured creditor with a security right in that receivable obtains the benefit of that guarantee or mortgage. This means that, if the receivable is not paid, the secured creditor may seek payment from the guarantor or enforce the mortgage (which may require that the secured creditor is registered as a mortgagee; see para. 105 below).

104. Under paragraph 2, which reflects the thrust of article 10 of the Assignment Convention, where the rights securing or supporting payment of a receivable are independent rights (i.e. they are transferable only with a new act of transfer), the grantor is obliged to transfer the benefit of that right to the secured creditor (e.g. an independent guarantee or stand-by letter of credit).

105. This article does not affect a right in immovable property that under other law is transferable separately from the obligation that the right in the immovable property secures. In addition, this article does not affect any duties of the grantor to the debtor of the receivable or other intangible asset, or the obligor of the negotiable instrument. Moreover, to the extent that the automatic effects of paragraph 1 are not impaired, this article does not affect any requirement under other law relating to the form or registration of the creation of a security right in any asset that is not covered in the Model Law (e.g. registration of a mortgage in the relevant immovable property registry).

Article 15. Right to payment of funds credited to a bank account

106. Article 15 is based on recommendation 26 of the Secured Transactions Guide (see chap. II, paras. 123-125). It is intended to implement article 13 with respect to rights to payment of funds credited to a bank account. As a result of article 15, a security right may be created in a right to payment of funds credited to a bank account without the consent of the depositary institution. However, as a result of article 67, the creation of such a security right does not affect the rights and obligations of the depositary institution or obligate the depositary institution to provide any information about the bank account to third parties.

Article 16. Tangible assets covered by negotiable documents

107. Article 16 is based on recommendation 28 of the Secured Transactions Guide (see chap. II, para. 128). Its purpose is to follow existing law in which a negotiable document is treated as a reified right in the tangible assets it covers. As a result, there is no need separately to create a security right in those tangible assets if there is a security right in the document (e.g. inventory or crops deposited in a warehouse for which the warehouse operator issued a negotiable warehouse receipt).

108. In view of the definition of the term "possession" in article 2, subparagraph (z), possession of the issuer of a negotiable document includes possession by its representative or a person acting on behalf of the issuer (including in the context of multi-modal transport contracts). A security right in a negotiable document extends to the tangible assets covered by the document and will continue to exist even after the document no longer covers the assets. However, effectiveness against third parties through possession of the document applies only as long as the document covers the assets and lapses once they are released by the issuer (see art. 25, para. 2, and para. 122 below).

Article 17. Tangible assets with respect to which intellectual property is used

109. Article 17 is based on recommendation 243 of the Intellectual Property Supplement (see paras. 108-112). It is intended to ensure that: (a) unless otherwise agreed (as art. 17 is not listed in art. 3 among the mandatory law provisions of the Model Law), a security right in a tangible asset does not automatically extend to the intellectual property right contained therein; and (b) that a security right in an intellectual property right does not automatically extend to the tangible asset with respect to which the intellectual property right is used (e.g. the copyrighted software included in a personal computer or the trademark on an inventory of clothes).

Chapter III. Effectiveness of a security right against third parties

A. General rules

Article 18. Primary methods for achieving third-party effectiveness

110. Article 18 is based on recommendation 32 of the Secured Transactions Guide (see chap. III, paras. 19-86). It is intended to set out the primary methods for achieving third-party effectiveness (i.e. registration in the general security rights registry and possession of a tangible asset by the secured creditor). Other methods (e.g. control and registration in the books of an issuer of securities) are set out in the asset-specific provisions of this chapter (see paras. 120-124 below).

111. States that have specialized registries with respect to assets covered by the Model Law (e.g. patent or trademark registries) or title notation systems (e.g. with respect to motor vehicles) may wish to consider whether registration with respect to security rights in those types of asset should take place in the security rights registry, in a specialized registry or both. If registration may take place in both (or, if a security right may also be noted on a title certificate), the enacting State may wish to ensure coordination (with national or international specialized registries),

including by way of linking the relevant registries so that information entered in one will also become available in the other and by way of appropriate priority rules (see Secured Transactions Guide, chap. IV, para. 117, and Registry Guide, paras. 64-66). With respect to security rights in attachments to immovable property and receivables arising from sale or lease of, or secured by, immovable property, the enacting State may wish to consider issues of coordination with immovable property registries (see Registry Guide, paras. 67-69). Finally, the enacting State may wish to consider issues of international coordination among national security rights registries (Registry Guide, para. 70).

Article 19. Proceeds

112. Article 19 is based on recommendations 39 and 40 of the Secured Transactions Guide (see chap. III, paras. 87-96). It is intended to determine the circumstances in which the security right in proceeds that is provided for in article 10 is effective against third parties.

113. Under paragraph 1, a security right in proceeds in the form of money, receivables, negotiable instruments or rights to payment of funds credited to a bank account is automatically effective against third parties, that is, without the need for any further act. For example, upon the sale of inventory that is subject to a security right that is effective against third parties, the security right in any receivable, cash, bank deposit, or check generated by the sale that are proceeds of the originally encumbered inventory is effective against third parties without any further act.

114. Unlike recommendation 39, on which this article is based, paragraph 1 does not refer to the description of the proceeds in the notice. This change is a drafting change and does not constitute a change of policy. The reason for this change is that, once the proceeds are described in the notice (in line with the security agreement), they constitute original encumbered assets, and article 18 is sufficient in dealing with the third-party effectiveness of a security right in those assets.

115. For proceeds other than those covered in paragraph 1, paragraph 2 provides that, if a security right in an asset was effective against third parties, the security right in its proceeds is effective against third parties for a short period of time; thereafter, the security right in the proceeds continues to be effective against third parties only, if before the expiry of that short period, it is made effective against third parties by one of the methods set out in article 18 or the asset-specific provisions of this chapter.

Article 20. Changes in the method for achieving third-party effectiveness

116. Article 20 is based on recommendation 46 of the Secured Transactions Guide (see chap. III, paras. 120 and 121). It is intended to ensure that a security right made effective by one method may later be made effective by another method, and that third-party effectiveness is continuous as long as there is no time gap between the two methods.

Article 21. Lapse in third-party effectiveness

117. Article 21 is based on recommendation 47 of the Secured Transactions Guide (see chap. III, paras. 122-127). It is intended to ensure that, if third-party

effectiveness lapses, it may be re-established. In such a case, third-party effectiveness dates only from the time it is re-established.

Article 22. Continuity in third-party effectiveness upon a change of the applicable law to this Law

118. Article 22 is based on recommendation 45 of the Secured Transactions Guide (see chap. III, paras. 117-119). Under paragraph 1, if the law enacting the Model Law becomes applicable as a result, for example, of a change in the location of the encumbered asset or the grantor, a security right that was effective against third parties under the previously applicable law continues to be effective against third parties under the law enacting the Model Law for a short period of time, unless its third-party effectiveness under the initially applicable law has already lapsed. Thereafter, the security right is effective against third parties only if, before the expiry of that period, it is made effective against third parties under the relevant provisions of the law enacting the Model Law. Under paragraph 2, if the third-party effectiveness of a security right does not lapse, it dates back to the time it was first achieved under the previously applicable law.

Article 23. Acquisition security rights in consumer goods

119. Article 23 is based on recommendation 179 of the Secured Transactions Guide (see chap. IX, paras. 125-128). An acquisition security right in consumer goods is automatically effective against third parties [except as against buyers or other transferees, lessees or licensees of the consumer goods] [if the consumer goods are below a value to be specified by the enacting State]. This limitation is intended to [require registration for a security right in consumer goods to be effective against buyers or other transferees, lessees or licensees of consumer goods] [to exempt from registration only low-value consumer transactions]. If registration in a specialized registry or notation in a title certificate is also possible, such an acquisition security right in consumer goods should not have the special priority of an acquisition security right over a security right registered in a specialized registry. This approach would be necessary to avoid any interference with any specialized registration system (see Secured Transactions Guide, recs. 179 and 181).

B. Asset-specific rules

Article 24. Rights to payment of funds credited to a bank account

120. Article 24 is based on recommendation 49 of the Secured Transactions Guide (see chap. III, paras. 138-148). It adds to the primary methods of article 18 three asset-specific methods of achieving third-party effectiveness of a security right in a right to payment of funds credited to a bank account. First, if the secured creditor is the depositary institution, no additional action is required for a security right to become effective against third parties. Second, the security right is effective against third parties upon conclusion of a control agreement (see art. 2, subpara. (g)(ii)) among the grantor, the secured creditor and the depositary institution. Third, the security right is effective against third parties if the secured creditor becomes the account holder. The exact action required for the secured

creditor to become the account holder depends on the relevant law and practice of the enacting State.

Article 25. Negotiable documents and tangible assets covered by negotiable documents

121. Article 25 is based on recommendations 51-53 of the Secured Transactions Guide (see chap. III, paras. 154-158). It addresses the relationship between the third-party effectiveness of a security right in a negotiable document and the third-party effectiveness of a security right in the tangible assets covered by the document.

122. Under paragraph 1, if a security right in a negotiable document (which extends to the assets covered by the document under article 16) is effective against third parties, the security right in the assets covered by the document is also effective against third parties for as long as the assets are covered by the document. Under paragraph 2, possession of the document is sufficient to make the security right in the assets covered by the document effective against third parties. Under paragraph 3, the security right referred to in paragraph 2 remains effective against third parties for a short period of time after the secured creditor relinquishes the possession of the document for the purpose of enabling the grantor to deal with the assets covered by it.

Article 26. Uncertificated non-intermediated securities

123. Article 26 is a new provision that does not correspond to any of the recommendations of the Secured Transactions Guide, which did not apply to any type of securities (see rec. 4, subpara. (c)). It addresses the methods, other than registration of a notice, by which a security right in uncertificated non-intermediated securities may be made effective against third parties. First, the security right may be made effective against third parties by notation of the security right or entry of the name of the secured creditor as the holder of the securities in the books maintained by the issuer or another person on behalf of the issuer for that purpose (the enacting State should choose the method that best suits its legal system). Second, as in the case of a security right in a right to payment of funds credited to a bank account, the conclusion of a control agreement with respect to the encumbered securities will result in the security right in those securities being effective against third parties.

124. Under article 19 of the Convention Providing a Uniform Law For Bills of Exchange and Promissory Notes (Geneva, 1930; the “Geneva Uniform Law”), “when an endorsement contains the statements ‘value in security’ (‘valeur en garantie’), ‘value in pledge’ (‘valeur en gage’), or any other statement implying a pledge, the holder may exercise all the rights arising out of the bill of exchange, but an endorsement by him has the effects only of an endorsement by an agent” (art. 22 of the United Nations Convention on International Bills of Exchange and International Promissory Notes (the “Bills and Notes Convention”) contains a similar rule, according to which such a holder “may endorse the instrument only for purposes of collection”). An enacting State that has enacted the Geneva Uniform Law (or the Bills and Notes Convention) may wish to include: (a) this rule in its enactment of the Model Law (as a rule of creation and/or third-party effectiveness of a security right in negotiable instruments, negotiable documents and

non-intermediated securities); and (b) a rule dealing with the comparative priority of such a security right. Another option would be to leave the matter to articles 44, paragraph 2, 47, paragraph 3, and 49, paragraph 3, under which such a holder of a negotiable instrument, negotiable document or non-intermediated security would take its rights free of, or unaffected by, any security right. A further option would be to leave the matter to the relevant domestic law rule dealing with the hierarchy between domestic law and an international convention (see para. 68 above).