SUMMARY OF UNCITRAL LEGISLATIVE GUIDE ON SECURED TRANSACTIONS AND THE SUPPLEMENT ON SECURITY RIGHTS IN INTELLECTUAL PROPERTY

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Acquisition Financing: Summary of the Guide's recommendations

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Creation of a security right

1. UNCITRAL'S Legislative Guide on Secured Transactions (the "Guide") provides that a security right (i.e., a "security interest") may be created by agreement between the grantor (i.e., "secured debtor") and the secured creditor. This security agreement needs to identify the parties and reasonably describe the encumbered assets (i.e., the "collateral") [Recom. 12].

2. The security agreement shall be in writing, or even oral as long as it is accompanied by delivery of possession of the encumbered assets to the secured creditor (or to any other person holding the assets on behalf of the secured creditor). The Guide adopts a very flexible notion of writing, including electronic communications, and it is left open whether to require some form of signature [Recom. 13]. It is very important to keep creation requirements to a minimum, because the Guide recommends that those same requirements apply to retention-of-title and other acquisition finance devices.

3. A security right is created at the time the requirements for its creation are met, unless the parties agree to postpone the moment the security right takes effect between them to a later time (they cannot agree to an earlier time, as this might affect the rights of third parties) [Recom. 14].

4. Once a security right is created, it becomes effective between the grantor and the secured creditor (i.e., at that point in time the security right "attaches" to the encumbered assets). The grantor may create more than one non-possessory security right in the same asset, thus using the full value of such asset by granting other security rights in favor of other creditors, while remaining in possession of such asset to generate the income necessary to pay its debts. However, in order for a security right to be effective against third parties (i.e., in order to "perfect" the security right or make it "opposable" vis-à-vis third parties), an additional step must be taken (e.g., registration or "filing" in a general security rights registry, transfer of possession of a tangible encumbered asset, registration in a specialized registry or yet another act.) [Recoms. 33-35].

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5. The Guide takes a broad and flexible approach both as to the assets that may be encumbered as well as to the obligations that may be secured. Thus, security rights may be created not only in assets that exist or belong to the grantor at the time the security agreement is concluded and the security right is created, but also in assets that may arise or may be acquired by the grantor in the future. A single security agreement is all what is needed to cover present as well as future or after-acquired assets.

6. All obligations, monetary as well as non-monetary, present or future, may be secured by a security right, irrespective of whether the obligor is a physical person or a legal entity, a merchant or a consumer (subject, of course, to consumer protection laws that are mandatorily applicable) [Recom. 15].

7. Unless the parties agree otherwise, a security right extends to whatever is received in lieu of the encumbered assets, i.e., to the "proceeds" of the encumbered assets [Para. 3(jj)]. The proceeds must be susceptible of being identified.[2]

Pre-default rights and obligations of the parties

8. Under the Guide, the parties are in principle free to structure their security agreement as they wish [Recom. 9]. A set of non-mandatory rules are provided by the Guide, which apply in the absence of agreement of the parties. The policy objectives pursued by those rules seek to provide a reasonable allocation of responsibilities for the care of the encumbered assets, while promoting access to credit at affordable costs [Recom. 106].

9. The Guide also provides for a set of mandatory rules dealing with issues that are likely to arise during the life of the secured transaction and once the secured obligation is fully performed (e.g., the duty of care of the person in possession of the encumbered asset, the duty to return the assets or terminate any registration notice upon full payment and termination of all credit commitments) [Recom. 107].

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[2] Procceds in the form of money commingled with other property are to be treated as identifiable proceeds if, at any time after the money proceeds were commingled with the other property, the total amount or value of the commingled property was more than the amount or value of the money proceeds (so, if the value of the proceeds is US$1,000 and the value of the total property is US$5,000, only US$1,000 is deemed to be identifiable proceeds). If, at any time after the money proceeds are commingled with other property, the total amount of the commingled property was less than the amount or value of the money proceeds, competing claimants are to share proportionally to their loss (i.e., if the value of the money proceeds for Secured Creditor A and Secured Creditor B is US$1,000 each, and the total value of the commingled property is US$8,000, the amount of identifiable proceeds for each one is US$4,000) [Recom. 20]. Proceeds other than money are to be treated as identifiable proceeds pursuant to the share the value of the proceeds bears to the total value of the commingled proceeds (i.e., if the proceeds of Secured Creditor A have a value of US$10,000 and the proceeds of Secured Creditor B a value of US$20,000, and the total value of the commingled proceeds is US$40,000, then Secured Creditor A will get ¼ and Secured Creditor B will get ½) [Recom. 21].

Acquisition financing devices

10. According to the Guide, "acquisition security rights" are those securing an obligation to pay any unpaid portion of the purchase price or other obligation incurred to enable the grantor to acquire the encumbered asset. The definition is broad enough to cover retention of title devices (i.e., arrangements enabling a person to acquire possession or use of assets subject to an obligation to pay their price to a person who retains title until the price is paid), as well as hire-purchase agreements, finance leases, and the traditional retention of title clause in a sale of goods contract.

11. The policy objective of the Guide's provisions on acquisition financing is to provide a source of affordable credit, particularly for small/medium-sized enterprises; to facilitate financing operations by creating transparency; and to ensure equal treatment for all acquisition financiers [Statement of purposes, Part XII of the Guide]. In pursuing this agenda, the Guide suggests that domestic law should treat as secured transactions all devices that perform security functions (including the transfer of title to tangibles or the outright assignment of receivables for security purposes). This functional, comprehensive approach would embrace more or less all title transfer "security" devices (i.e., "in rem" rights securing payment or the performance of obligations).[3]

12. Yet, the Guide takes into account that some legal systems may be reluctant, for various reasons, to recharacterize acquisition financing devices as secured transactions. Thus, the Guide leaves it free to States to either adopt a so-called "**unitary approach**", subsuming all transactions serving security functions, irrespective of how they are denominated (retention of title, financial leases, etc.), into a unitary and generic notion of "security right" (thus mirroring Article 9 of the UCC and the PPSA of Canada, New Zealand and other common-law jurisdictions).[4] Alternatively, States may opt for a so-called "**non-unitary approach**", maintaining the traditional characterization of retention of title and other acquisition financing devices, yet applying to those transactions the same rules that apply to security rights insofar as the creation, effectiveness against third parties, priority, and other financing aspects of the transaction.

13. Thus, the so-called "non-unitary approach" adopted by the Guide, as an alternative to the "unitary approach", admits the possibility of functionally similar security-type transactions, where the substantive treatment would be the same as secured

[3] Recommendation 2(e): "*The law should apply: …(e) To all types of property rights created contractually to secure the payment or other performance of an obligation, irrespective of the form of the relevant transaction, including the various forms of retention of title, financial leases and hire-purchase agreements, as well as transfers of title by way of security*."

[4] In the context of a unitary approach, acquisition financing devices are arrangements that, whether denominated security devices or not, enable a person to acquire possession or use of assets subject to an obligation to pay their price to a person that retains a security right in them until the price is paid." Recom. 2(e) and Recom. 8, note (a) to definition (b).

transactions but the legal characterization of the transaction remains different [See generally, Part XII of the Guide]. Whether a State adopts a unitary or non-unitary approach, the rules applicable to acquisition financing devices and non-acquisition financing devices are equivalent, because all providers of acquisition financing are to be treated in an equal way (treating all providers of acquisition financing in an equal way pursues the policy objective of promoting competition among them, thus enhancing the availability of credit at the lowest possible cost).

14. Accordingly, all acquisition financing devices are subject to the same requirements of form, same rules on third-party effectiveness, and in order to promote transparency, all acquisition-financing devices are subject to registration [Recom. 184]. Basically, all acquisition financing devices, under the unitary or non-unitary approach, obtain a super priority status, outranking an earlier security right over the same assets that would ordinarily have priority under the general first-to-file principle.[5] However, to avoid overburdening consumer transactions, the Guide exempts from registration acquisition financing transactions relating to consumer goods [Recom. 185].

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[5] Thus, the priority of an acquisition financing device (i.e., "purchase money security interest") dates back to the time the transaction is concluded as long as registration takes place within a short period of grace (20 or 30 days) after delivery of the goods to the buyer. This priority rule is an exception to the general first-to-file priority principle, ranking the acquisition financing security right ahead of a prior security right with an after-acquired property clause. Because the acquisition financier adds value to the estate of the borrower, this priority rule is meant to protect such acquisition financier without affecting other creditors (who can protect themselves, for example, by registering on Day 1 and wait for 20 or 30 days before actually advancing any funds, so as to avoid that an acquisition financier who might register within the period of grace might get ahead of them).