

A Model Law on Secured Transactions

A representation of structure? An object of imitation? A type or design?

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Introduction

The three senses of the noun-adjective “model” reproduced in the sub-title are copied from the Oxford English Dictionary.¹ They perfectly reflect the different inquiries that spring to mind whenever one enters onto the terrain of law reform through model laws. Should we understand model laws as we understand “model airplanes”? Should we understand them as we understand runway performers at a fashion show? Or should we understand them as we would an architect’s or an engineer’s template?

Unsurprisingly the polysemic character of the word is reflected in current critical discussions about the utility and desirability of transnational model laws.

Some, focusing on the first meaning, see model laws as nothing more than a simpler, reduced scale version of something else. So, for example, one often hears about a particular kind of model secured transactions laws that they are “Article 9 *lite*”, or “Article 9 for dummies”. They are just small scale, non-functioning, plastic reproductions of the genuine article.

Others, focusing on the idea that a model may be an object of imitation, see model laws in aspirational terms. None of us can look like a fashion model or reach the state of moral grace achieved by Gandhi, Schweitzer, or Mandela. Concomitantly, we do not expect that any real law enacted by a State could ever achieve in practice what a model law promises.

Still others imagine model laws neither as impoverished reflections of anything that already exists in the world, nor as an ideal to which one should aspire, but rather as an archetype, a blueprint by which something may be created. In this sense, a model law appears more or less to be a variant on what UNCITRAL has already produced with its Legislative Guide on Secured Transactions.

I have already speculated several times about the several dimensions of transnational secured transactions reform, and the role of different policy instruments in achieving legal modernization.² I do not propose to review those reflections here. Rather, I want to focus on two specific questions: should UNCITRAL now undertake a project to transform the recommendations of the Legislative Guide into a Model Law? and if so, how should it pursue that objective?

¹ OED online *q.v.* model

² Notably, in R.A. Macdonald, “Transnational secured Transactions Reform: Book IX of the Draft Common Frame of Reference in Perspective” (2009) *ZeuP* 745-782; “Three Metaphors of Norm Migration in International Context” (2009) 34 *Brooklyn Journal of International Law* 603-653; “In Praise of the Hypothecary Charge” (2007) *deCITA* 287-308; “Article 9 Norm Entrepreneurship” (2006) 43 *Canadian Business Law Journal* 240-291.

I. Desirability, Feasibility and Timing of a Model Law

Friedrich von Savigny famously entitled one of his leading works (in its English translation) “On the vocation of our age for legislation and jurisprudence”.³ Widely seen at the time as a polemical response to the codification movement, von Savigny’s book can also be read as a treatise on law reform. What conditions, he asked, conduce to successful law reform through judicial incrementalism, and what conditions conduce to legislative law reform?

Some years ago, as founding president of the Law Commission of Canada I had occasion to reflect on the von Savigny thesis. In developing its Strategic Agenda and 5-year Research Plan the Commission posed itself the following questions: (1) Why do we think that law reform needs to be textual? Why chirographic? (2) Why do we imagine that legislation is the ideal type of legal chirographism? Why a statute rather than international conventions, judicial judgements, treatises, practice manuals, cautionary tales, and so on? (3) Why do we think that law reform needs to be exclusively the product of the political state? Why do we believe that multiple constitutive (or epistemic) communities lack the capacity to develop better law?⁴

As we think about whether the Legislative Guide on Secured Transactions should be transformed into a Model Law the questions reveal their continuing relevance. The curse of the 21st century, we all know, is that the possible becomes the necessary. And in the case of the transformation of the Legislative Guide, the hypothetical (to borrow from Kant) becomes the categorical. Because we *can* generate a Model Law, we *must* produce a Model Law.

With these two opening caveats, let me address very briefly the issues evoked by the title to this subsection.

A. Is a model law desirable?

No. There has never been a “one size fits all” multijurisdictional model law that has really succeeded – unless you count adoption by multiple legislatures of sub-national units. By contrast, the answer might be different if the question were posed in the plural. For example, it might be that a document like a Legislative Guide could be transformed into multiple model laws. Were this route to be taken, of course, one would confront the conundrum of deciding how many model laws should be developed. In addition, one would have to decide the criterion of regroupment: is the key criterion “legal tradition”? is it related to the “nature of the economy”? perhaps the organizing principle should be related to “political and social structures”? Finally, one might ask whether UNCITRAL should take the lead in developing diverse model laws, or whether the

³ Frederick K. Von Savigny, *On the vocation of our age for legislation and jurisprudence* (Abraham Hayward, trans) London: Littlewood and Co., 1831.

⁴ For further development of these themes, as elaborated in the work of the Law Commission of Canada, see R. A. Macdonald, “Jamais deux sans trois ...Once Commission, Twice Reform, Thrice Law » (2007) 22 *Canadian Journal of Law and Society* 117-143; "Law Reform and Its Agencies" (2000) 79 *Canadian Bar Review* 99-118; "ReCommissioning Law Reform" (1997) 35 *Alberta Law Review* 831-880.

optimal strategy would be to provide technical assistance to individual States, or States that voluntarily come together to work towards enactment of similar national laws.

B. Is a model law feasible?

No. Experience teaches that a transnational model law is feasible in only three situations: (1) where the idea is to create an international normative regime (as in the Convention on mobile equipment financing); (2) where the model creates a regime that deals with a relatively new field not subject to widespread or detailed regulation, and where the goal is to relieve national legislatures of the burden of statutory development (as would be the case if there were a project meant to structure securitizations and the use of derivatives as security); or (3) where the model law is aimed at providing a short, specific, patch on an relatively closely defined existing framework of national legislation (as might have been the case of a short model law on, say, letter of credit financing). None of these situations obtain in respect of the Legislative Guide on Secured Transactions.

Moreover, every time one seeks to transform an existing normative instrument (whether a series of judicial decisions, or a practice manual, or a legislative guide) into another form of instrument such as a model law, one runs the risk of re-opening debate on controversial policy issues. Should this occur, UNCITRAL is put on the horns of a dilemma: either to accept a revisiting of these policy choices, the consequence of which is sponsor two projects (a Legislative Guide and a Model Law) that point in different directions, or to refuse to entertain a reopening of policy questions, in which case support for the new project would dissipate.

C. Is the timing right?

No. Any particular law reform project succeeds when there is a happy of coincidence of supply and demand. A failure of equilibrium on either side of the balance scale is a recipe for failure. Currently, in the realm of secured transactions law, there is an *oversupply* of model laws: EBRD, OHADA, DCFR and the OAS Inter-American model law. There is no, however, an oversupply of Legislative Guides. The genius of the Legislative Guide is that, to borrow an old saw of comparative law, it works not by “reason of the rule” (as is typically the case with formulaic model laws), but by “the rule of reason” (the detailed exploration of policy alternatives and the providing of elaborated rationales for the choices made).

One might also observe that there is an *under-demand* for model laws. Some States, such as Australia, Ukraine and Hungary, were working on a reform of secured transactions law in much the same direction as proposed by the Legislative Guide at the same time, and have either recently enacted or are on the verge of enacting a reformed law. Other States, such as those of the European Union, likewise have sponsored unofficial attempts to produce model laws (once again in much the same direction as UNCITRAL) meant for consumption by member States. Neither of these groups of States (to which may be added those of the OAS) are plausible customers of yet another model law. Still other States or groups of States are in one of three situations: they are confronted with a model law that has been elaborated over time and which is in the final stages of pre-enactment; or they are well advanced in developing a new law that is respectful of local practice; or they are just beginning to consider whether (and how) to modernize secured transactions law.

For States in the first situation, it is too late to put a process on hold while waiting for a model law, although a document like the Legislative Guide can provide very valuable insight as to how existing proposals may be improved at their margins. For States in the second situation, unless the model law actually incorporates these local practices into its basic framework (or in the case of multiple model laws, into the basic framework of one of the variants), it is a Legislative Guide that focuses on policy choices and rationales that will be most helpful. For States in the third situation, it is too early in the legislative reform process for them to benefit from a model law; here also a Legislative Guide that moves from a statement of the problem, through an elaboration of key objectives, through a detailed discussion of failures of current approaches and the presentation of plausible policy options for enactment will provide States with the resources needed to make informed choices about how to proceed, without at the same time appearing to dictate particular outcomes.

II. Policy considerations

Any State that contemplates enacting a model law confronts a number of issues that may roughly characterized as demanding thoughtful consideration of social, economic and legal policy. These issues range from the sublime to the trivial. In reflecting on how UNCITRAL should address these considerations were it to contemplate moving from a Legislative Guide to a Model Law four appear to me as non-trivial (even if perhaps not sublime).

A. Relationship to “other law”

A Legislative Guide is a document that purports to give guidance to States as to the optimal content of a particular piece of legislation. Inevitably a Legislative Guide that aims to provide specific direction as to norms to enact will also reflect meta-choices about scope of application, organization, style of expression, and the optimal precision of legislative rules.

Prior to these decisions internal to a model law is another: what is the relationship of the model law to other norms and instruments in a State? The UNCITRAL Legislative Guide reflects important choices of this type. For example, the Guide takes as its central theme “consensual secured transactions in moveable property.” From this, a number of *exclusions* and references to “other law” follow, even though, were one to cast the scope of the project only slightly differently, these topics would be included under the Guide. The point is obvious when one contrasts the Legislative Guide with the organization of the relevant chapters of a typical Civil Code. For example, the Civil Code of Québec conceives security rights as embracing all legal devices that provide for a right in property that attenuates or counters the principles of universal patrimonial liability and equality of creditors. Hence, and first, it embraces security on both moveable and immovable property. Second, it embraces proprietary security (hypothecs), possessory security (rights of retention), mere execution preferences (privileges), and (like the Legislative Guide) the use of title to secure performance of an obligation (security trusts, instalment sales, rights of resolution, sales with a right of redemption, financial leases, and so on). Third, it embraces both consensual (hypothecs, title transactions, consensual liens) and non-consensual (legal hypothecs, privileges, rights of retention) security.

By contrast, the Legislative Guide *includes* various transactions and topics that the typical Civil Code consigns to “other law”. These transactions include, for example, assignments not intended as security. In so far as additional topics are concerned, the Legislative Guide includes chapters on registry systems, conflicts of laws, transitional measures and aspects of insolvency. While the Guide makes no claim that these matters should be included in a single statute dealing with security rights (on the model, say, of Article 9 of the UCC) the implication is that they are significant enough that they should be incorporated within the frame of Guide, rather than left to be dealt with by “other law”.

Both by decisions about what to include in the Guide, and by decisions that consign rules relating to immoveables, non-proprietary security and non-consensual security to “other law”, the Guide reflects a particular policy choice as to what *really* matters. In enacting a model law, however, a State might evaluate the relative importance of topics differently. It might well follow all the specific recommendations of the Guide to the letter decide to exclude matters that the Guide includes (enacting them in “other law”), and to include matters that the Guide excludes (thereby expanding the coverage of the Guide).

B. Commercial law or consumer law?

Historically, the “civil law” in Romano-Germanic legal tradition, and the “common law” in the Anglo-American tradition were seen as the overall default regime of legal regulation. In Romano-Germanic states, the civil law was conceived as the default regime of “private law” that would apply in matters of “public law” only to the extent explicitly incorporated. More than this, the civil law was understood as the basic regime of law governing everyday relationships and transactions between citizens. In derogation from the basic principles announced in a Civil Code, these States developed parallel Commercial Codes which often elaborated specialized rules governing transactions that were either “objectively” or “subjectively” commercial. Somewhat later, and in part because of the development of retail commercial activity and a service economy, these same States came to elaborate Consumer Codes. The rules governing security rights in the Civil Code formed the default regime of everyday transactions, to which the Commercial Codes engrafted regimes for relationship between enterprises, and Consumer Codes added special protections for transactions involving consumers.

In Anglo-American States, the common law was also conceived as the default regime of legal regulation, applicable equally to private law and (except where explicitly excluded – as in Crown liability) to public law matters. Consequently, as in the continental tradition, it applied to commercial relationships and consumer transactions. But since Anglo-American States were reluctant to enact general commercial or consumer codes, to keep up with evolving mercantile practice in the 19th century, legislatures were obliged to enact specific statutory regimes – bills of sale, conditional sales, hire-purchase, corporate charges, etc. – and in the mid-20th century to regulate certain business practices through consumer protection legislation.

The Legislative Guide, like Article 9 of the Uniform Commercial Code (which is, of course, not a commercial code in sense understood in Romano-Germanic systems), does not follow the historical pattern of either civil law or common law States. Rather, it presumes that the basic default regime of secured transactions should be that governing commercial relationships, and that policy decisions to protect consumers and consumer-like third parties should be left to “other law” expressed in consumer protection acts and family property statutes. As a result, in addition

to the core assets charged in everyday secured transactions (consumer durables, credit card receivables) and everyday business finance secured transactions (equipment, inventory and ordinary trade receivables), the Legislative Guide covers security over a number of more specialized assets (documents of title, negotiable instruments, bank accounts, letters of credit, and, in its Annex, intellectual property).

While the backdrop to the Legislative Guide is commercial transactions, many Civil Codes take the opposite tack. They elaborate rules governing entitlement to grant security (natural persons not carrying on an enterprise may not grant security on a universality of assets), pre-default rights and obligations (a security right does not automatically attach to fruits, revenues and proceeds), enforcement of security (hypothecary debtors may not only redeem the security upon default, but may also reinstate the security), that contemplate consumers as the basic transactional constituency. Here again the Guide reflects a basic policy choice about what constitutes the core of a secured transactions regime – commercial finance.

C. Organization, Style and Mode of Expression

To the degree a model law is meant to serve as a template for legislative action, it is necessary to consider a number of features that are implicit in the manner of its drafting. Not surprisingly, these same features are also present, and apparent, in the way the Legislative Guide has itself been crafted.

A first point to observe is that the general organizational theme of functionalism pervades the Guide. The unitary and functional approach first elaborated in Article 9 underlies the basic scope provision. In addition, functionalism underlies the Guide's concept of proceeds – a concept that embraces not only what is received in replacement of charged property (that is, through a notion of real subrogation), but also what is received upon disposition of charged property even if the property remains charged following disposition, and what in normal civil law parlance is characterized as natural or civil fruits (revenues), even if no disposition takes place. Furthermore, even where the Guide contemplates (as in acquisition financing) the use of title as security, the creditor's title right (retention of title) is structured so that it produces "functionally equivalent results" to those that obtain under the regime governing acquisition security rights..

Second, the style of the Guide is very much the style of a common law statute. The general ossature of the civil law that divides normative instruments into categories and sub-categories that are interrelated in descending orders of generality is not followed. Rather, each recommendation appears as a more-or-less free standing specific direction to a court. Even though the Legislative Guide contains a series of recommendations, it is written with numerous paragraphs and sub-clauses of the type that would induce a read to imagine that each recommendation could simply be transposed into statutory language by the removal of the opening words "The law should provide ...". If this were done, it is obvious that the resulting model law would rest on similar, common law, assumptions about the style of legislation, and the manner in which the conceptual apparatus of the statute is presented.

A further point about the mode of legislative expression involving a significant policy choice by States concerns the role of mandatory and suppletive rules. As a general principle of statutory drafting in common law States, one does not announce norms that merely set a default position away from which parties are entitled to derogate by contract. That is, the principle of party

autonomy finds expression not just in relation to its basic content – parties may choose their co-contracting party, the terms of their agreement, and the consequences they wish to attribute to these terms upon default – but also in terms of what legislation states. This view of legislation is reflected both in the absence of suppletive rules structuring the relationship of the parties prior to default, and is present in the general principle that permits non-judicial realization of security rights, even as against consumers.

D. Ideal-type or lowest common denominator rules

A final policy issue flows directly from the fundamental operating assumption that underlies the Legislative Guide. When attempting to think about law reform, law reformers are often torn between two approaches. One is to imagine the possibility of enacting the perfect law, as seen from an ideal-type perspective. Doing so requires reformers to abstract from the messy world of conflicting economic interests, politics and history reflected in current legislative regimes of all States. The goal is to proclaim a few basic policy objectives, to assert fundamental axioms about human and regulatory behaviour and to deduce a normative regime that rests on these axioms and achieves these goals in the most efficient and effective manner. This is the approach taken by the Legislative Guide and by a number of model law proposals of the past decades – EBRD and OAS regimes most prominently.

The other approach is to take the law as it exists in the State or the States for which one is proposing a law reform project and (in the case of multiple States) to find the lowest common denominator of policies, principles and concepts that are consistent with the law in each State. In such an approach, the reality test is not undertaken by reference to axioms and assumptions about human behaviour, but rather by reference to how human beings are actually reacting in relation to a set of existing policy prescriptions. Such a lowest common denominator approach is that taken by the von Bar project's DCFR for the EU, by the OHADA proposals in West Africa, and of course, within the United States by the Article 9 project. No-one today believes that Article 9 is derived from an ideal-type law reform endeavour. Indeed, with the most recent amendments to Article 9, it has radically departed from the partially ideal-type perspective that animated its creation half a century ago. Article 9.3 now more resembles the kind of lowest common denominator model law that is jurisdiction specific in scope, approach and expression.

In view of the evolution of Article 9, one might ask of the Legislative Guide whether it can be effectively transformed into a model law on the ideal-type basis, or will the necessary accommodation to local circumstance require that it be recast into a number of regional model laws of the lowest common denominator kind.

III. Contents and Structure of the Model Law

It is difficult to respond meaningfully to queries about the content and structure of a model law without focusing on particular States and particular legal regimes. Nonetheless, based on experiences in drafting and re-drafting secured transactions laws in different contexts, it seems to me that the several issues must be considered prior to picking up the legislative pen. In other words, the answer to the question whether the model law should *include*, for example (1) IP-related issues, (2) conflicts of laws, (3) insolvency, and (4) specialized transition rules (as the

Guide does) and should *exclude*, for example, (1) immoveables, (2) non-consensual security, and (3) consensual liens (as the Guide does) presupposes a more general reflection on what the model law is meant to do within the legal regime into which it is being inserted.

Let me put the point slightly differently, using three examples. It is one thing to say in a Legislative Guide that States wishing to modernize their law so as to produce an efficient and effective secured transactions regime should (1) adopt a functional approach, (2) separate creation from third party effectiveness, (3) provide for a general registry of security rights, (4) order priorities primarily by reference to time rather than quality of claim, (5) permit non-judicial realization, and (6) establish a non-discriminatory regime of acquisition financing. It is quite another, however, to say that the rules required to operationalize such principles need to appear in that order, in a single legislative document, drafted in the form of an Income Tax Act.

Again, it is one thing to propose, to take another example, that States adopt an extensive rule relating to the transfer of a security right into the proceeds “arising on account of secured collateral” or to project a security right into attachments to immoveable property. It is quite another to presume that, in order to achieve this objective, States will have to recharacterize fruits, products and revenues, and to stretch their concept of real subrogation to capture proceeds even when the security right survives disposition.

Finally, it is one thing to provide for alternative approaches in a Legislative Guide as the UNCITRAL Guide does notably in respect of unitary and non-unitary approaches to acquisition financing. It is quite another to imagine that an enacting State would not have to choose between the proffered alternatives.

To illustrate these points I propose simply to set out for comparative purposes alternative approaches to drafting of rules relating to scope, proceeds and acquisition financing, taking two Canadian models – the Ontario *Personal Property Security Act* (PPSA) and the *Civil Code of Québec* (CCQ) – as exemplars. Of course, I could have also chosen to illustrate the point by comparing the concepts of priority in the PPSA and rank in the CCQ, and the notions of perfection in the PPSA and publicity in the CCQ. This said, I believe the three illustration I have selected are sufficient to illustrate the contrast. I leave to the reader’s judgement the appropriate lessons to draw from these comparisons.

A. Scope

There are, obviously several ways to express scope provisions. The approach taken by Article 9 and its derivatives, and by the Legislative Guide is to treat the statute as discrete legislation and describe the situations to which it applies. So, for example, the Ontario Personal Property Security Act (PPSA) defines a “security interest” since that is the primary term by the application of the Act is determined. The definition accomplishes two objectives. It limits the term to interests in “personal property”; and it enacts a legal fiction according to which certain other transactions that do not secure performance of an obligation – transfers of accounts, leases of more than one year – are deemed to be “security interests”:

“security interest” means an interest in personal property that secures payment or performance of an obligation, and includes, whether or not the interest secures payment or performance of an obligation,

- (a) the interest of a transferee of an account or chattel paper, and*
- (b) the interest of a lessor of goods under a lease for a term of more than one year;*

The fiction is then repeated in section 2, which speaks specifically to scope. Section 2 also further limits the scope of the PPSA to consensual transactions:

2. *Subject to subsection 4 (1), this Act applies to,*

- (a) every transaction without regard to its form and without regard to the person who has title to the collateral that in substance creates a security interest including, without limiting the foregoing,*
 - (i) a chattel mortgage, conditional sale, equipment trust, debenture, floating charge, pledge, trust indenture or trust receipt, and*
 - (ii) an assignment, lease or consignment that secures payment or performance of an obligation;*
- (b) a transfer of an account or chattel paper even though the transfer may not secure payment or performance of an obligation; and*
- (c) a lease of goods under a lease for a term of more than one year even though the lease may not secure payment or performance of an obligation.*

Given the broad scope provision of section 2, it is then necessary to elaborate a list of transactions otherwise caught by section 2 which are excluded from the application of the PPSA. Section 4 enumerates these limitations on scope.

4. (1) *Except as otherwise provided under this Act, this Act does not apply,*

- (a) to a lien given by statute or rule of law, except as provided in subclause 20 (1) (a) (i) or section 31;*
- (b) to a deemed trust arising under any Act, except as provided in subsection 30 (7);*
- (c) to a transfer of an interest or claim in or under any policy of insurance or contract of annuity, other than a contract of annuity held by a securities intermediary for another person in a securities account;*
- (d) to a transaction under the Pawnbrokers Act;*
- (e) to the creation or assignment of an interest in real property, including a mortgage, charge or lease of real property, other than,*
 - (i) an interest in a fixture, or*
 - (ii) an assignment of a right to payment under a mortgage, charge or lease where the assignment does not convey or transfer the assignor's interest in the real property;*
- (f) to an assignment for the general benefit of creditors to which the Assignments and Preferences Act applies;*

- (g) to a sale of accounts or chattel paper as part of a transaction to which the Bulk Sales Act applies;
 - (h) to an assignment of accounts made solely to facilitate the collection of accounts for the assignor; or
 - (i) to an assignment of an unearned right to payment to an assignee who is to perform the assignor's obligations under the contract.
- (2) The rights of buyers and sellers under subsection 20 (2) and sections 39, 40, 41 and 43 of the Sale of Goods Act are not affected by this Act.

The central logic of the Personal Property Security Act is transactional, not conceptual; that logic is also directed to consequences rather than principles. Compare this type of formulation to that found in the *Civil Code of Québec* (CCQ). The CCQ begins by situating the idea of a security right (the hypothec) and other legal devices (prior claims) within the broader framework of debtor-creditor relationships, and states how the notion derogates from the default principles of debtor-creditor law.

2644. *The property of a debtor is charged with the performance of his obligations and is the common pledge of his creditors.*

2646. *Creditors may institute judicial proceedings to cause the property of their debtor to be seized and sold.*

If the creditors rank equally, the price is distributed proportionately to their claims, unless some of them have a legal cause of preference.

2647. *Prior claims and hypothecs are the legal causes of preference.*

Once the principle and exception are established, the CCQ elaborates a functional definition of the hypothec and defines the nature, types and scope of the concept.

2660. *A hypothec is a real right on a movable or immovable property made liable for the performance of an obligation. It confers on the creditor the right to follow the property into whose hands it may be, to take possession of it or to take it in payment, or to sell it or cause it to be sold and, in that case, to have a preference upon the proceeds of the sale ranking as determined in this Code.*

2664. *Hypothecation may take place only on the conditions and according to the formalities authorized by law.*

A hypothec may be conventional or legal.

2665. *A hypothec is movable or immovable depending on whether the object charged is movable or immovable property or a universality of movable or immovable property.*

A movable hypothec may be created with or without delivery of the movable hypothecated. Where it is created with delivery, it may also be called a pledge.

2666. *A hypothec is a charge on one or several specific corporeal or incorporeal properties, or on all the properties included in a universality.*

In view of the logic of debtor-creditor law – creditors may seize only the debtor’s exigible estate (the common pledge) – it is necessary to deal with transactions that deploy title to property to secure the performance of an obligation. The CCQ states a default principle in article 1801. Any clause in a contract that purports to deploy title to secure the performance of an obligation is deemed not written. This principle is subject to two exceptions: the security trust, and the Quebec equivalent of the historical fiducia cum creditore, the sale with a right of redemption. The latter achieves its regulatory effect by deeming the seller to be a borrower and the acquirer to be a hypothecary creditor, thereby incorporating by reference the entire regulatory regime governing hypothecs. The former achieves its regulatory effects in a manner similar to the PPSA regimes. It imposes a procedural overlay on the trustee seeking to enforce the trust following default by the debtor.

1263. *The purpose of an onerous trust established by contract may be to secure the performance of an obligation. If that is the case, to have effect against third persons, the trust must be published in the register of personal and movable real rights or in the land register, according to the movable or immovable nature of the property transferred in trust.*

In case of default by the settlor, the trustee is governed by the rules regarding the exercise of hypothecary rights set out in the Book on Prior Claims and Hypothecs.

1756. *Where the object of the right of redemption is to secure a loan, the seller is deemed to be a borrower and the acquirer is deemed to be a hypothecary creditor. The seller does not, however, lose the right to exercise his right of redemption unless the acquirer follows the rules respecting the exercise of hypothecary rights laid down in the Book on Prior Claims and Hypothecs.*

1801. *Any clause by which a creditor, with a view to securing the performance of the obligation of his debtor, reserves the right to become the irrevocable owner of the property or to dispose of it is deemed not written.*

A comparison of these two techniques for achieving a regulation of security devices through adoption of a functional approach reveals that there is nothing inherent in the “substance of the transaction“ idea that demands adoption of the drafting style of a common law statute. While the CCQ regime does not presently bring retention of title into the hypothecary regime in the manner of article 1756, as explained in section C below, it does so in the same manner as security trusts are subjected to the regulatory frame.

B. Proceeds

Consider now the question of proceeds. The Ontario Personal Property Security Act offers an exceptionally wide definition of “proceeds“. As noted, this definition embraces what traditionally are known as products, fruits and revenues as well as what is received upon disposition under a concept of real subrogation, and even includes what is received upon disposition even if there is no ground for subrogation (i.e. the security continues in the initially charged asset). As with the definition of a security interest, it rests on a fiction driven by the desire to achieve a particular regulatory outcome regardless of the conceptual framework of the underlying law.

“proceeds” means identifiable or traceable personal property in any form derived directly or indirectly from any dealing with collateral or the proceeds therefrom, and includes,

- (a) any payment representing indemnity or compensation for loss of or damage to the collateral or proceeds therefrom,*
- (b) any payment made in total or partial discharge or redemption of an intangible, chattel paper, an instrument or investment property, and*
- (c) rights arising out of, or property collected on, or distributed on account of, collateral that is investment property; (“produit”)*

The consequences of the proceeds right are then described by reference to the way in which it may achieve the best status as against third parties (i.e. the manner in which it can be perfected). Here again, it is to be noted that the announced rule significantly departs from the underlying premise of third-party effectiveness in that because perfection is automatic without the need to file a new financing statement. Section 25 provides:

25. (1) *Where collateral gives rise to proceeds, the security interest therein,*

- (a) continues as to the collateral, unless the secured party expressly or impliedly authorized the dealing with the collateral free of the security interest; and*
- (b) extends to the proceeds.*

(2) *Where the security interest was perfected by registration when the proceeds arose, the security interest in the proceeds remains continuously perfected so long as the registration remains effective or, where the security interest is perfected with respect to the proceeds by any other method permitted under this Act, for so long as the conditions of such perfection are satisfied.*

(3) *A security interest in proceeds is a continuously perfected security interest if the interest in the collateral was perfected when the proceeds arose.*

(4) *If a security interest in collateral was perfected otherwise than by registration, the security interest in the proceeds becomes unperfected ten days after the debtor acquires an interest in the proceeds unless the security interest in the proceeds is perfected under this Act.*

Finally the PPSA provides that the priority rules applicable to perfected security interests in initially encumbered collateral apply to proceeds derived therefrom.

30. (1) *If no other provision of this Act is applicable, the following priority rules apply to security interests in the same collateral:*

- 1. Where priority is to be determined between security interests perfected by registration, priority shall be determined by the order of registration regardless of the order of perfection.*
- 2. Where priority is to be determined between a security interest perfected by registration and a security interest perfected otherwise than by registration,*
 - i. the security interest perfected by registration has priority over the other security interest if the registration occurred before the perfection of the other security interest, and*
 - ii. the security interest perfected otherwise than by registration has priority over the other security interest, if the security interest perfected otherwise than by registration was perfected before the registration of a financing statement related to the other security interest.*

(5) *For the purpose of subsection (1), the date for registration or perfection as to collateral is also the date for registration or perfection as to proceeds.*

Consider now the analogous rules in the Civil Code of Québec. To begin, there is no general proceeds right. Article 2674 limits the notion of proceeds to situations of real subrogation – that is to cases where the hypothec on the initially charged property is extinguished because the property was sold in the ordinary course of business of the debtor.

2674. *A hypothec on a universality of property subsists but extends to any property of the same nature which replaces property that has been alienated in the ordinary course of business of an enterprise.*

A hypothec on an individual property alienated in the same way extends to property that replaces it, by the registration of a notice identifying the new property.

If no property replaces the alienated property, the hypothec subsists but extends only to the proceeds of the alienation, provided they may be identified.

2675. *A hypothec on a universality of property subsists notwithstanding the loss of the hypothecated property where the debtor or the grantor replaces it in a reasonable time, having regard to the quantity and nature of the property.*

Of course, while the CCQ does not adopt the general proceeds of disposition rule that goes beyond the real subrogation concept, it would not be difficult to draft article 2674 to accomplish that outcome in respect of hypothecs over moveable property. Such a draft would not, however,

cover the case of products, fruits and revenues. These assets, while derived from initially encumbered assets, are in no way proceeds. The basic principle of the CCQ flows directly from fundamental property law concepts: the rights of usus, fructus and abusus attach to the right of ownership (or titularity of a lesser real right). Article 2733 repeats this provision.

2733. A hypothec does not divest the grantor or the person in possession, who continue to enjoy their rights over the charged property and may dispose of it, subject to the rights of the hypothecary creditor.

Here again, while the policy a requiring a separate charging clause to capture fruits is in my view preferable, nothing prevents the drafting of the Code so that a hypothec automatically embraces natural fruits and civil fruits (revenues). Non-regenerative products subtracted from initially charged assets would, of course, automatically be charged with the security by virtue of the principle of indivisibility. The codal provision to capture fruits and revenues would simply mirror the existing provision on accessions. That provision, article 2671 provides:

2671. A hypothec extends to everything united to the property by accession.

As in the case of the scope provisions, there are obvious differences in legislative technique. The PPSA again relies on a fiction that trumps existing property concepts in order to achieve a desired outcome. In this respect the functional definition of proceeds is no different than the functional definition of a security interest. Of course, in both cases, the same critique of functionalism may be made. The drafting of the CCQ illustrates how it is possible to achieve substantively identical results to those generated by the PPSA while nonetheless respecting the conceptual logic of basic property law. An important lesson can be derived from this conclusion. There is nothing inherently uncivilian about attempting to legislative a modernized secured transactions regime that extends a security right into all identifiable assets that are derived directly or indirectly from the initially encumbered asset.

C. Acquisition financing

Consider now a third illustration -- the question of acquisition financing. Following Article 9, the Ontario Personal Property Security Act adopts a generic view of acquisition financing that focuses on the nature of the secured transaction, and not on the parties to it (either sellers or lenders). The PPSA adopts the language of Article 9 – purchase money security interest – and defines this central concept as follows.

“purchase-money security interest” means,

- (a) a security interest taken or reserved in collateral, other than investment property, to secure payment of all or part of its price,*
- (b) a security interest taken in collateral, other than investment property, by a person who gives value for the purpose of enabling the debtor to acquire rights in or to the collateral, to the extent that the value is applied to acquire the rights, or*
- (c) the interest of a lessor of goods under a lease for a term of more than one year;*

For a third time one sees the impact of functionalism in the elaboration of a key concept in the PPSA. The idea is simply that there are many ways by which a person (a debtor) may acquire the utilities of a moveable asset equivalent to an ownership right. Whether as a purchaser, an exchanger, the beneficiary of a loan for consumption, or through operation of the rules of specification, any transaction translative of ownership is an acquisition transaction. Likewise, any transaction not translative of ownership but that produces functionally equivalent results – a lease, a loan for use, a complex deposit, a possessory right as beneficiary of a trust – will be considered as an acquisition transaction. Moreover, the functionalism extends beyond the characterization of the transaction. All providers of financing – whether the co-contracting party (seller, exchanger, lessor, lender for consumption, etc.) or a third party (lender of money, trustee, etc.) – and all forms of acquisition financing – whether in cash, credit or in kind – are caught by the definition.

The significance of the definition lies in the priority position that accrues to the acquisition financier. In general terms the idea is to provide that the purchase-money security interest will have priority over even previously-registered (and in the case where there is a grace period for registration of a purchase-money security interests, even previously-*perfected*) holders of non-acquisition security interests. The complexity of section 35 derives from the fact that it must trace rules not only for sellers and lenders, but also because it envisions different rules for inventory and other assets, and because it must solve internal priority problems among competing acquisition financiers. This is especially important in the case of sub-section 33(3) dealing with competitions between lender and seller acquisition financing.

33. (1) *A purchase-money security interest in inventory or its proceeds has priority over any other security interest in the same collateral given by the same debtor, if,*

(a) the purchase-money security interest was perfected at the time,

(i) the debtor obtained possession of the inventory, or

(ii) a third party, at the request of the debtor, obtained or held possession of the inventory,

whichever is earlier;

(b) before the debtor receives possession of the inventory, the purchase-money secured party gives notice in writing to every other secured party who has, before the date of registration by the purchase-money secured party, registered a financing statement that describes the collateral as, or as including,

(i) items or types of inventory, all or some of which are the same as the items or types of inventory that will be subject to the purchase money security interest,

(ii) inventory, or

(iii) accounts; and

(c) the notice referred to in clause (b) states that the person giving it has or expects to acquire a purchase-money security interest in inventory of the debtor, describing such inventory by item or type.

(2) Except where the collateral or its proceeds is inventory or its proceeds, a purchase-money security interest in collateral or its proceeds has priority over any other security interest in the same collateral given by the same debtor if the purchase-money security interest,

(a) in the case of collateral, other than an intangible, was perfected before or within ten days after,

(i) the debtor obtained possession of the collateral as a debtor, or

(ii) a third party, at the request of the debtor, obtained or held possession of the collateral,

whichever is earlier; or

(b) in the case of an intangible, was perfected before or within ten days after the attachment of the purchase-money security interest in the intangible.

(3) Where more than one purchase-money security interest is given priority by subsections (1) and (2), the purchase-money security interest, if any, of the seller has priority over any other purchase-money security interest given by the same debtor.

Compare this formulation to the position set out in the Civil Code of Québec. A first observation is that the CCQ continues to distinguish between rights available to (1) sellers and lessors who deploy title as an acquisition financing device, (2) sellers and others whose acquisition financing agreements are translative of ownership and who take a vendor's hypothec, and (3) third party financiers such as lenders.

1741. Except in the case of a sale with a term, the seller of movable property may, within 30 days of delivery, consider the sale resolved and revendicate the property if the buyer, being in default, has failed to pay the price and if the property is still entire and in the same condition and has not passed into the hands of a third person who has paid the price thereof, or of a hypothecary creditor who has obtained surrender thereof.

Where the buyer is in default to pay the price and the property meets the conditions prescribed for resolution of the sale, the seizure of the property by a third person is no hindrance to the rights of the seller.

1745. An instalment sale is a term sale by which the seller reserves ownership of the property until full payment of the sale price.

A reservation of ownership in respect of a road vehicle or other movable property determined by regulation, or in respect of any movable property acquired for the service or operation of an enterprise, has effect against third persons only if it has

been published; effect against third persons operates from the date of the sale provided the reservation of ownership is published within 15 days. As well, the transfer of such a reservation has effect against third persons only if it has been published.

- 1749.** *A seller or transferee who, upon the default of the buyer, elects to take back the property sold is governed by the rules regarding the exercise of hypothecary rights set out in the Book on Prior Claims and Hypothecs; however, in the case of a consumer contract, only the rules contained in the Consumer Protection Act are applicable to the exercise by the seller or transferee of the right of repossession.*

If the reservation of ownership required publication but was not published, the seller or transferee may take the property back only if it is in the hands of the original buyer; the seller or transferee takes the property back in its existing condition and subject to the rights and charges with which the buyer may have encumbered it.

If the reservation of ownership required publication but was published late, the seller or transferee may likewise take the property back only if it is in the hands of the original buyer, unless the reservation was published before the sale of the property by the original buyer, in which case the seller or transferee may also take the property back if it is in the hands of a subsequent acquirer; in all cases, the seller or transferee takes the property back in its existing condition, but subject only to such rights and charges with which the original buyer may have encumbered it at the time of the publication of the reservation of ownership and which had already been published.

- 1842.** *Leasing is a contract by which a person, the lessor, puts movable property at the disposal of another person, the lessee, for a fixed term and in return for payment.*

The lessor acquires the property that is the subject of the leasing from a third person, at the demand and in accordance with the instructions of the lessee.

- 1847.** *The rights of ownership of the lessor have effect against third persons only if they have been published; effect against third persons operates from the date of the leasing contract provided the rights are published within 15 days.*

As well, the transfer of the lessor's rights of ownership has effect against third persons only if it has been published.

- 1851.** *Lease is a contract by which a person, the lessor, undertakes to provide another person, the lessee, in return for a rent, with the enjoyment of a movable or immovable property for a certain time.*

1852. The rights resulting from the lease may be published.

Publication is required, however, in the case of rights under a lease with a term of more than one year in respect of a road vehicle or other movable property determined by regulation, or of any movable property required for the service or operation of an enterprise, subject, in the latter case, to regulatory exclusions; effect of such rights against third persons operates from the date of the lease provided they are published within 15 days. A lease with a term of one year or less is deemed to have a term of more than one year if, by the operation of a renewal clause or other covenant to the same effect, the term of the lease may be increased to more than one year.

In each of these cases of title security – the vendor’s right of resolution and reclamation, the instalment sale, the finance lease (leasing), and the lease for more than one year – the Code elaborates a slightly different regime. Only the instalment sale (retention of title) is subjected to a regulatory regime for enforcement that tracks that applicable to hypothecs. But in all, the question of the acquisition financier’s priority is determined by reference to basic principles of property law: *nemo dat quod non habet*. The only one of these transactions that contemplates direct third-party acquisition financing is the contract of leasing. In all the other cases, a lender would have to take an assignment of the seller’s or the lessor’s rights. This differentiated regime also applies in the case of the vendor’s hypothec as set out in article 2954. Only true sellers (and by extension other former owners of assets sold under a contract translatif of ownership – e.g. exchangers) may claim a vendor’s hypothec, and the privileged priority position attaching to it.

2954. A movable hypothec acquired on the movable of another or on a future movable ranks from the time of its registration but after the vendor's hypothec, if any, created in the grantor's act of acquisition, provided it is published within 15 days after the sale.

As in the two cases previously noted -- scope and proceeds – one can see obvious differences in legislative technique. It is true that there are substantive differences between the PPSA and CCQ regimes, especially as concerns third-party lender acquisition financing, but these can be overcome simply by modifying codal drafting. The signal distinction is this. The PPSA relies on the fiction that the seller (or any other prior owner) of property necessarily has no interest in the asset being sold other than the desire to obtain its price. From this fiction, it is easy to reduce the entire panoply of property rights and remedies elaborated over the past centuries to recognize and protect a seller’s other interests, to a simple economic calculation. Once this “essentialisation” of a seller’s (prior owner’s) interest is accomplished, it is easy to expand this fiction into a fully functional description of acquisition financing in which lenders and sellers are treated as equals. Again relies on a fiction that trumps existing property concepts in order to achieve a desired outcome. And yet, as sub-section 33(3) of the PPSA reveals, it is impossible to obliterate the concept of ownership: as between earlier lender acquisition financiers and later seller acquisition financiers (including not only owners in agreements translatif of ownership, but also lessors) priority goes to the seller, presumably because ownership still counts for something. To conclude once again, while the CCQ is drafted in a way that maintains conceptual distinctions between principal rights in re (habitually ownership) and accessory rights in re (habitually hypothecs and pledges), there is nothing in this drafting style that prevents achieving

substantively identical results to those generated by the PPSA. There is nothing inherently uncivilian about attempting to provide approximately equal access to an acquisition financing priority for sellers, lessors and lenders, and preserving within the category of such financiers a special priority for owners over lenders.

Conclusion

Let me return to the three senses of the noun-adjective “model” reproduced in the sub-title are copied from the Oxford English Dictionary.

It would be a mistake to conceive a model law as “Article 9 for dummies”. The Legislative Guide is a richer, more elaborated and pedagogically sophisticated normative instrument. It needs no “model”.

It would also be a mistake to conceive a model law as a statement of an unrealizable statement of moral perfection. Here again, the Legislative Guide serves to elaborate such an aspiration while nonetheless explicitly tempering the aspiration with the *realpolitik* of the world in which real states enact real laws.

Finally, it would also be a mistake to conceive a model law as an archetype or a blueprint. No single model law could ever provide such a blueprint, and the Legislative Guide is currently a carefully worked out statement of considerations that should inform the move by national States from recognition of the need for action towards the elaboration of a specific blueprint for legislation.

And so I offer a concluding epigram: “the perfect is the enemy of the good, and the quest for the perfect undermines the good already accomplish.”