United Nations A/CN.9/914

General Assembly

Distr.: General
27 March 2017

Original: English

United Nations Commission on International Trade Law
Fiftieth session
Vienna, 3-21 July 2017

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

Note by the Secretariat

Contents

V.17-01869 (E) 300317 310317

Preface

At its forty-eighth session, in 2015, the Commission considered and approved the substance of article 26 of chapter IV of the draft Model Law on Secured Transactions and articles 1-29 of the draft Registry Act.[1]

At that session, the Commission also agreed that a guide to enactment of the Model Law should be prepared and referred that task to Working Group VI (Security Interests).[2]

At its forty-ninth session, in 2016, the Commission considered and adopted the UNCITRAL Model Law on Secured Transactions (the decision of the Commission and the relevant General Assembly resolution are contained in annexes I and II respectively).[3]

At that session, the Commission also noted that the Guide to Enactment was already at an advanced stage and was an extremely important text for the implementation and interpretation of the Model Law, and gave Working Group VI up to two sessions to complete its work and submit the Guide to Enactment to the Commission for final consideration and adoption at its fiftieth session in 2017.[4]

At its thirtieth and thirty-first sessions in December 2016 and February 2017, Working Group VI approved the substance of the draft Guide to Enactment.[5]

[At its fiftieth session, in 2017, the Commission considered and adopted the Guide to Enactment of the UNCITRAL Model Law on Secured Transactions (the decision of the Commission and the relevant General Assembly resolution are contained in annexes III and IV respectively).[6]]

---

[1] *Official Records of the General Assembly, Seventieth Session, Supplement No. 17* (A/70/17), para. 214. The draft Model Law and the draft registry Act are contained in documents A/CN.9/852 and A/CN.9/853.

[2] Ibid., para. 216.

[3] Ibid., *Seventy-first Session, Supplement No. 17* (A/71/17), paras. 17-118. The draft Model Law, including the draft Model Registry-related Provisions, is contained in documents A/CN.9/884 and Add.1-4; the draft Guide to Enactment of the Model Law is contained in documents A/CN.9/885 and Add.1-4; and the compilation of comments by States is contained in documents A/CN.9/886, A/CN.9/887 and Add.1.

[4] Ibid., paras. 121 and 122.

[5] The reports of the Working Group are contained in documents A/CN.9/899 and A/CN.9/904. During these sessions, the Working Group considered documents A/CN.9/WG.VI/WP.71/Add.1-6 and A/CN.9/WG.VI/WP.73. Earlier versions of the Guide to Enactment are contained in documents A/CN.9/WG.VI/WP.66 and Add.1-4 and A/CN.9/WG.VI/WP.69 and Add.1-2.

[6] *Official Records of the General Assembly, Seventy-second Session, Supplement No. 17* (A/72/17), para. […]. The draft Guide to Enactment is contained in documents A/CN.9/914 and Add.1-6. For the earlier project of UNCITRAL on security interests (1975-1980), see http://www.uncitral.org/uncitral/uncitral_texts/security_past.html.

I. Purpose of the Guide to Enactment

1. The Guide to Enactment is intended to explain briefly the thrust of each provision of the UNCITRAL Model Law on Secured Transactions (the "Model Law") and its relationship with the corresponding recommendation(s) of the UNCITRAL Legislative Guide on Secured Transactions (the "Secured Transactions Guide")[7] and other UNCITRAL texts on secured transactions,[8] including the United Nations Convention on the Assignment of Receivables in International Trade (the "Assignment Convention"),[9] the UNCITRAL Legislative Guide on Secured Transactions: Supplement on Security Rights in Intellectual Property (the "Intellectual Property Supplement"),[10] and the UNCITRAL Guide on the Implementation of a Security Rights Registry (the "Registry Guide").[11]

2. A number of the provisions of the Model Law indicate that a State enacting the Model Law (the "enacting State") is required to make a decision or choose among several options. The Guide to Enactment is also intended to explain the import of these decisions or choices and thus assist enacting States in making those decisions or choices.[12] To avoid unnecessary repetition, the Guide to Enactment incorporates by reference the relevant recommendations and commentary contained in the Secured Transactions Guide, the Intellectual Property Supplement and the Registry Guide, rather than repeating them.

3. The Guide to Enactment is primarily directed to executive and legislative branches of Governments. However, it may also provide useful insight to other users of the text, such as judges, arbitrators, practitioners and academics. It has been prepared by the Secretariat at the request of the Commission,[13] and is based on the deliberations and decisions of the Commission and Working Group VI.[14]

II. Purpose of the Model Law

4. 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 increase the availability of and decrease the cost of credit by providing for an effective and efficient secured transactions law (see Secured Transactions Guide, rec. 1 (a)). Like those texts, the Model Law is based on the assumption that, to the extent that a secured creditor is entitled to rely on the value of the encumbered asset for the payment of the secured obligation, the risk of non-payment is reduced and this is likely to have a beneficial impact on the availability and the cost of credit. It should also be noted that, like those texts, the Model Law is intended to be useful to both States that currently do not have efficient and effective secured transactions laws and States that already have such laws but wish to modernize them, and harmonize

---

[7] United Nations publication, Sales No. E.09.V.12.

[8] *Official Records of the General Assembly, Seventieth Session, Supplement No. 17* (A/70/17), paras. 215 and 216.

[9] General Assembly resolution 56/81, annex (United Nations publication, Sales No. E.04.V.14).

[10] United Nations publication, Sales No. E.11.V.6.

[11] United Nations publication, Sales No. E.14.V.6.

[12] *Official Records of the General Assembly, Seventieth Session, Supplement No. 17* (A/70/17), para. 216.

[13] See footnote 1 above.

[14] The reports of the Working Group on its work during the six sessions devoted to the preparation of the Model Law 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 those 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. For the reports of the Commission on its work during the two sessions it devoted to the Model Law and the document considered by the Commission during those sessions, see footnotes 1 and 3 above.

them with the laws of other States that have modern secured transactions laws that are generally consistent with the Model Law (see Secured Transactions Guide, Introduction, para. 1).

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

5. In general, States that incorporate the Model Law into their national law are advised to adhere as much as possible to its uniform text. This can help the enacting State to obtain the full economic benefit of the legal system envisioned by the Model Law, to avoid unintended consequences that may follow when a change in one provision has unforeseen effects elsewhere in the law, and to gain the benefits flowing from the harmonization of its secured transactions law with that of other States. This does not deprive enacting States of any necessary flexibility as the Model Law provides options and leaves a number of matters to enacting States.

6. Examples of flexibility in the Model Law include the following: (a) the Model Law draws the attention of the enacting State to the need to adjust certain terms used in the Model Law to ensure that they are meaningful in the context of local law (e.g. "authorized deposit-taking institution", "movable property", "immovable property" and "securities"; see art. 2, subparas. (c), (u) and (hh)); (b) several provisions of the Model Law refer within square brackets to issues that are left to the enacting State (e.g. art. 1, para. 3 (e)); (c) other provisions of the Model Law include options from which the enacting State is able to choose (e.g. art. 6, para. 3); (d) the Model Law leaves it to the enacting State to decide how to clarify in its enactment of the Model Law that the general rules are subject to the asset-specific rules (see footnote 4 of the Model Law); (e) the Model Law leaves it to the enacting State to decide whether to implement the Model Registry Provisions in its enactment of the Model Law, in a separate statute or in another type of legal instrument (see footnote 8 of the Model Law); and (f) the Model Law leaves it to the enacting State to decide whether to incorporate the conflict-of-laws provisions of the Model Law in its enactment of the Model Law or in a separate law addressing conflict-of-laws issues generally (see footnote 36 of the Model Law).

7. The enacting State may need to make some changes to the Model Law in order to adapt it to its national legal system. Any modification, however, should not depart from the fundamental provisions of the Model Law, such as those implementing the functional, integrated and comprehensive approach to secured transactions (e.g. art. 1, para. 1, and art. 2, subpara. (kk)), the protection of the grantor and the debtor of the receivable (e.g. art. 1, paras. 5 and 6), the right of the parties to structure their security agreement as they wish to meet their needs (e.g. art. 3), the notice registration system (e.g. art. 18), the priority between a security right and the right of a competing claimant (e.g. art. 29) and the right to enforce a security right without application to a court or other authority while protecting the rights of the grantor and other parties with rights in the encumbered asset (e.g. art. 77, para. 3, and art. 78, para. 3). Otherwise, the enacting State will not be able to obtain the full economic benefits to be derived from the Model Law or achieve the harmonization of its law with the law of other States that enact the Model Law (for the harmonization of the enactment of the Model Law with other laws of the enacting State, see para. 8 below).

8. In enacting the Model Law, States will also need to consider whether complementary amendments to other related laws (e.g. contract, property, insolvency, civil procedure and electronic commerce law) are required to ensure the overall coherence of its national law (see Secured Transactions Guide, Introduction, paras. 80-83). For example, it is extremely important that the insolvency law of the enacting State recognizes the effectiveness of a security right, its priority and its enforceability in the case of the grantor's insolvency (for the treatment of security rights in insolvency, see Secured Transactions Guide, chap. XII). In addition,

enacting States will need to consider: (a) harmonization with the existing concepts and drafting styles (see Secured Transactions Guide, Introduction, paras. 73-89); and (b) transition issues, including the preparation of an official commentary, model notice forms and agreements, the organization of educational programmes for users of the new law and the introduction of a case law reporting system if one is not already in place (see Secured Transactions Guide, Introduction, paras. 84-89).

9. Unlike an international convention, model laws do not require enacting States to notify the United Nations or other enacting States of their enactment. However, States are strongly encouraged to inform the UNCITRAL secretariat of their enactment of the Model Law (or indeed any other model law resulting from the work of UNCITRAL). This information will be made available on the UNCITRAL website to publicize the fact that the enacting State has adopted an international standard and will assist other States in their consideration of the Model Law.

IV. Main features of the Model Law

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

10. The Secured Transactions Guide, the Intellectual Property Supplement and the Registry Guide contain detailed commentary and recommendations on the issues that need to be addressed in a modern law on secured transactions. However, they are lengthy texts and States will need assistance in transforming their recommendations into concrete legislative language. The Model Law responds to this need. By providing concrete legislative language, the Model Law also provides a higher level of uniformity than a guide.

11. The Model Law reflects the policies embodied in the recommendations of the Secured Transactions Guide, the Intellectual Property Supplement and the Registry Guide. Differences in formulation between those recommendations and corresponding provisions of the Model Law are generally due to the legislative nature of the Model Law and are briefly explained in the relevant parts of the Guide to Enactment.

12. For reasons explained below in the relevant parts of the Guide to Enactment, the Model Law also addresses, in a manner that is consistent with the goals and the policies of the Secured Transactions Guide and the other texts of UNCITRAL on secured transactions, matters that were not addressed in a recommendation, or even discussed in those texts (e.g. security rights in non-intermediated securities). Conversely, certain matters that were addressed in the Secured Transactions Guide are excluded from the scope of the Model Law (e.g. security rights in the right to receive the proceeds under an independent undertaking) or are not addressed specifically (e.g. security rights in attachments to encumbered movable assets or immovable property).

13. 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. Even if a State that does not yet have an efficient and modern secured transactions law ratifies or accedes to the Convention, it will need to enact the Model Law as well, because: (a) the Convention applies only to security rights and outright transfers of receivables; (b) subject to limited exceptions, the Convention applies only to the assignment of international receivables and the international assignment of receivables (see art. 1, para. 1); (c) the Convention explicitly refers important matters (i.e. third-party effectiveness and priority) to the applicable domestic law, that is, the law of the assignor's location (see art. 22); and (d) the Convention leaves other issues (e.g. the form of the assignment) to domestic law.

14. Conversely, a State enacting the Model Law will be well advised to ratify or accede to the Convention as well, in order to promote effective international receivables financing, in particular as a convention provides a higher level of uniformity and transparency than a model law. States that are parties to a convention have the same law, except to the extent the convention allows reservations, while States enacting a model law have compatible but rarely exactly the same laws. As an example of the benefits that can flow from ratification or accession to the Convention, it should be noted that exporters often face difficulty in obtaining financing based on receivables arising from the sale of exported goods because lenders in the exporter's State are unwilling to extend credit secured by receivables owed by customers located in States with whose laws the lenders are not familiar, or are only prepared to extend such credit at a higher cost, which small- and medium-size enterprises may not be able to afford. If both the enacting State (where the assignor and the assignee are located) and the State where the debtors of the receivables arising from the sale of exported goods are located ratify or accede to the Convention, lenders will be more willing to extend receivables financing to the exporters and at more affordable cost, because they will understand the legal rules that apply to the receivables owed to the exporters and thus will be more confident that they will be able to collect them.

B. Key objectives and fundamental policies of the Model Law

15. As already mentioned (see para. 4 above), the overall economic objective of the Model Law is the same as that of the Secured Transactions Guide (see Secured Transactions Guide rec. 1 and Introduction, paras. 43-59). 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 similar statement accompanying its enactment of the Model Law. That statement could be used in interpreting and in filling gaps in the Model Law (see para. 77 below).

16. The same is true for the fundamental policies of the Model Law and the Secured Transactions Guide (see Secured Transactions Guide, Introduction, paras. 60-72). One of these fundamental policies is a functional, integrated and comprehensive approach to secured transactions, under which any right created by agreement in any type of movable asset to secure the performance of an obligation is treated as a security right for the purposes of triggering the application of the Model Law, regardless of the terms used by the parties to describe their agreement (e.g. pledge, charge, transfer of title for security purposes, retention-of-title sale or financial lease; see Secured Transactions Guide, Introduction, para. 62, chap I, paras. 110-112, and chap. IX, paras. 60-84).

17. The enacting State may also wish to consider producing an official commentary or guide to its enactment of the Model Law for use by courts and legal practitioners in interpreting and applying the law (see Secured Transactions Guide, Introduction, para. 86). This is likely to be particularly helpful if the Model Law introduces significant changes to the enacting State's previous secured transactions laws. Such a guide could explain the intent of particular provisions, in particular if they deviate significantly from the previous law, and, where necessary, provide concrete examples. Even more importantly, such an official commentary or guide could explain the fundamental principles that underlie the Model Law, such as the functional, integrated and comprehensive approach to secured transactions referred to in the previous paragraph. As the Guide to Enactment discusses all these and other relevant issues (either directly or by reference to the Secured Transactions Guide), the enacting State's commentary or guide could refer to the Guide to Enactment and the Secured Transactions Guide to allow its courts to obtain interpretative guidance from the international source from which its law was derived.

V. Assistance from the UNCITRAL secretariat

A. Assistance in drafting legislation

18. 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),[15] 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)[16] and the Assignment Convention).

19. 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

20. 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

21. Article 1 is based on recommendations 1-7 of the Secured Transactions Guide (see chap. I, paras. 1-4, 13-15 and 101-112). 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

[15] United Nations publication, Sales No. E.14.V.2.
[16] United Nations publication, Sales No. E.97.V.12.

well as to clarify the relationship between the Model Law and other law (see art. 1, paras. 5 and 6). Generally, the Model Law follows the same functional, integrated and comprehensive approach to secured transactions as the Secured Transactions Guide. Thus, the Model Law applies to security rights, that is, to property rights in movable assets, created by an agreement to secure payment or other performance of an obligation, regardless of whether the parties have denominated them as security rights (see art. 1, para. 1, and the definition of the term "security right" in art. 2, subpara. (kk)). However, there are some differences between the scope of the Model Law and the scope of the Secured Transactions Guide (see paras. 22-31 below).

22. Like recommendation 3 of the Secured Transactions Guide and article 1, paragraph 1, of the Assignment Convention, article 1, paragraph 2, of the Model Law also applies to outright transfers of receivables by agreement that are used in financing transactions, such as factoring. The main reason for this approach is the need for the same third-party effectiveness and priority rules to apply to both outright transfers of and security rights in receivables because: (a) financing against receivables is sometimes done by an outright transfer of the receivables rather than the creation of a security right in the receivables; and (b) it is sometimes difficult to determine at the outset of a transaction whether it will be held to involve an outright transfer of or the creation of a security right in the receivables (see Secured Transactions Guide, chap. I, paras. 25-31). While most modern secured transactions laws generally follow this approach, some laws exclude certain types of outright transfers of receivables that do not function as financing transactions, such as: (a) outright transfers of receivables for collection purposes where the transferee essentially acts only as a representative or trustee of the transferor; and (b) outright transfers of receivables as part of the sale of the business out of which they arose (unless the former owner remains in apparent control of the business), where the potential for other outright transferees or secured creditors to be misled is limited.

23. Unlike the Secured Transactions Guide which covered security rights in the right to receive payment under an independent undertaking (see rec. 2 (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, para. 3 (a)). The reason for this exclusion is that implementation of the relevant recommendations of the Secured Transactions Guide would have made the Model Law unduly complex. Enacting States interested in dealing with security rights in those types of asset are encouraged to implement the relevant recommendations of the Secured Transactions Guide (recs. 27, 50, 107, 127, 176 and 212).

24. Like recommendation 4 (b) of the Secured Transactions Guide, to the extent that the provisions of the Model Law are inconsistent with law relating to intellectual property, article 1, paragraph 3 (b), of the Model Law defers to the enacting State's law relating to intellectual property. This limitation is unnecessary if the enacting State has already coordinated the Model Law and its law relating to intellectual property or plans to do so in the context of the overall reform of its secured transactions law.

25. Unlike recommendation 4 (c) of the Secured Transactions Guide which excludes from its scope all types of securities, article 1, paragraph 3 (c), excludes only intermediated securities. The reasons for this approach are that: (a) non-intermediated securities often are part of commercial finance transactions (in which, for example, it is common for the lender to obtain a security right in shares in 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) security rights in non-intermediated securities are not addressed in any other uniform law text and thus no guidance is provided to States with regard to such securities. Conversely, security rights in intermediated securities are excluded as the nature of such securities and their importance for the functioning of financial markets raise a broad range of issues that merit special legislative treatment and are

addressed in other uniform law texts (see Secured Transactions Guide, chap. 1, paras. 37 and 38).[17]

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

27. Combining the policy of recommendations 4 (a) and 7 of the Secured Transactions Guide, article 1, paragraph 3 (e), provides that the enacting State may exclude further types of asset (or transaction) to the extent that the matters that are addressed in the Model Law are governed by other law of the enacting State. The reason for this approach is to avoid inadvertently creating gaps (where that other law does not govern an issue addressed in the Model Law) or overlaps (where that other law governs an issue that is addressed in the Model Law as well). Assets that may be excluded from the scope of the Model Law in article 1, paragraph 3 (e) are, for example, assets that are subject to specialized secured transactions and registration regimes. Enacting States that do have such regimes with respect to assets that may be covered by the Model Law (e.g. ships, vehicles, aircraft or intellectual property) will have to consider a number of issues, including the following: (a) whether registration with respect to security rights in those types of asset should take place in the security rights registry, in the specialized registry or in both; (b) if registration may take place in both registries, coordination of the relevant registries (see Secured Transactions Guide, chap. IV, para. 117, and Registry Guide, paras. 66 and 70) and coordination of the relevant third-party effectiveness and priority rules (see Secured Transactions Guide, recs. 43 and 77, subpara. (a); see also Registry Guide, paras. 23, 30 and 65); (c) the priority of acquisition security rights in consumer goods that are effective automatically (see art. 24; and Secured Transactions Guide, chap. IX, paras. 125-128, and rec. 181); and (d) the determination of law that is applicable to security rights in tangible assets subject to specialized registration (see Secured Transactions Guide, chap. X, paras. 37 and 38, as well as rec. 205).

28. Like recommendation 6 of the Secured Transactions Guide, article 1, paragraph 4, provides that, 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. intermediated securities), except to the extent that other law applies to proceeds of that type and governs the matters addressed in the Model Law.

29. With respect to the relationship with consumer-protection law, in line with the approach followed in the Assignment Convention (see art. 4, para. 4) and in the Secured Transactions Guide (see rec. 2 (b)), article 1, paragraph 5, is intended to preserve the application of consumer-protection law that protects a grantor or a debtor of an encumbered receivable (see also art. 1, para. 6, which preserves statutory limitations in general). For example, under consumer-protection law, it may not be possible to create or enforce a security right in all present and future assets, employment benefits, at least up to a certain amount, or in necessary household items of a consumer, or to collect an encumbered receivable from a debtor that is 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 (e.g. art. 24).

[17] Such as 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").

30. Following the approach of recommendation 18 of the Secured Transactions Guide, article 1, paragraph 6 is intended to preserve limitations on 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 any such limitations based on the sole ground that an asset is a future asset, or a part of an asset or an undivided interest in an asset are overridden (see art. 8, subparas. (a) and (b)). However, paragraph 6 does not apply to contractual limitations on the creation or enforceability of a security right in receivables (see art. 13) or rights to payment of funds credited to a bank account (see art. 15).

31. Finally, like the Secured Transactions Guide, the general provisions of the Model Law apply to security rights in attachments to movable or immovable property, that is, movable assets that are attached to movable or immovable property without losing their separate identity and thus becoming part of the movable or immovable property to which they have been attached (see Secured Transactions Guide, Terminology). However, unlike the Secured Transactions Guide, the Model Law does not include specific provisions on security rights in attachments to movable or immovable property. Such provisions were not included in the Model Law to avoid making it even longer. In view of the importance of attachments, enacting States are encouraged to consider whether 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

32. Article 2 contains definitions and rules of interpretation with respect to most key terms used in the Model Law. [18] Other terms are defined or explained in various articles of the Model Law. For example, the term "judgment creditor" is defined in article 37, paragraph 1, of the Model Law. Comments are not included below on all terms but only on those that are not self-explanatory or those that are not sufficiently explained in the Secured Transactions Guide, on the terminology of which article 2 is based (see Secured Transactions Guide, Introduction, paras. 15-20).

33. The rules of interpretation of the Secured Transactions Guide also apply to the Model Law. For example: (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).

34. It should be noted that time periods set out in the Guide to Enactment are suggestions (not recommendations) for the enacting State to use for its consideration of what would be appropriate for its own circumstances. It should also be noted that issues relating to the measurement of time (e.g. whether only working days are meant) are left to other law of the enacting State. However, depending on how those issues are addressed (e.g. whether official holidays are to be included), the enacting State may wish to consider adjusting the time periods suggested in the Guide to Enactment.

Acquisition security right

35. An acquisition security right is a security right in a tangible asset (other than a tangible asset that embodies an intangible asset, such as a negotiable instrument; see art. 2, subparas. (b) and (ll)), or in intellectual property or the rights of a licensee that secures the grantor's obligation with respect to credit provided by a lender, seller or financial lessor to enable the grantor to acquire title to or the right

[18] Since the Model Registry Provisions may be enacted in a separate statute or other type of legal instrument, the term "registry" is defined both in article 2, subparagraph (ee), of the Model Law and article 1, subparagraph (k), of the Model Registry Provisions. If they are enacted as part of the Model Law, the latter provision will not be necessary.

to use that tangible asset or intellectual property, or those rights of a licensee in intellectual property. This definition, in conjunction with the definition of "security right", results in the security right of any lender, seller or financial lessor extending credit for the acquisition of title to or right to use an asset being treated in the Model Law as an acquisition security right. It should be noted, however, that: (a) for a security right to be an acquisition security right, the credit it secures must in fact be used for that purpose; and (b) where a security right secures both obligations incurred for the grantor to acquire a tangible asset and other obligations, that security right is only an acquisition security right to the extent it secures the obligation to pay the acquisition price, and is a non-acquisition security right to the extent it secures those other obligations.

Bank account

36. 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 an authorized deposit-taking institution to which funds may be credited or debited" (see art. 2, subpara. (c)); (b) the latter term as "an account maintained by an intermediary to whom securities may be credited or debited" (see art. 2, subpara. (ii)); and (c) the term "securities" in a manner that clearly excludes funds (see art. 2, subpara. (hh)). The term "bank account", therefore, includes any type of bank account (e.g. 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 replacing the term "authorized deposit-taking institution" with a generic term broad enough to include any institution authorized to receive deposits in any State whose law may be applicable under article 97 of the Model Law.

Certificated non-intermediated securities

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

Competing claimant

38. The term "competing claimant" is principally used in the context of a potential priority dispute between a security right and the rights of another person claiming rights in the encumbered asset (see art. 2, subpara. (e)). This term includes another creditor of the grantor (secured or not) that has a right in the asset (such as a judgment creditor that has taken the steps necessary under other law of the enacting State to acquire a right in the encumbered asset), an insolvency representative in insolvency proceedings with respect to the grantor, and a buyer or other transferee, lessee or licensee of the asset.

Consumer goods

39. 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 primarily used or intended to be used by the grantor for personal, family or household purposes and only incidentally for business purposes would be treated as consumer goods; and (b) goods primarily used or intended to be used by the grantor for business purposes and only incidentally for personal, family or household purposes would not be treated as consumer goods. Accordingly, it is the primary use or the primary intended use of tangible assets by the grantor that determines whether they will be classified as consumer goods, equipment or inventory. It should also be

noted that the terms “consumer goods”, “equipment” and “inventory” are primarily relevant to the articles on acquisition security rights (see paras. 43 and 47 below).

Control agreement

40. The term “control agreement” refers to an agreement between the grantor, the secured creditor and the issuer (in the case of securities) or the deposit taking institution (in the case of a right to payment of funds credited to a bank account), according to which the issuer or the deposit-taking institution agrees to follow the instructions of the secured creditor without the further consent of the grantor (see art. 2, subpara. (g)). A control agreement can achieve two purposes: (a) to render a security right effective against third parties (see arts. 25 and 27); and (b) to establish the priority of the secured creditor that has control (see arts. 47 and 51). In addition, a control agreement can be useful to a secured creditor as a practical matter, because it can help ensure the cooperation of the deposit-taking institution or the issuer of securities if the secured creditor needs to enforce its security right. 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”. This difference does not reflect a policy change but rather a decision that this matter should be left to the evidentiary requirements of other law of the enacting State. In any case, a control agreement does not need to be in a single written document.

Default

41. The term “default” is defined in a generic way to mean the debtor’s failure to pay or otherwise perform the secured obligation and anything else that constitutes default under the agreement between the grantor and the secured creditor. What exactly constitutes failure to perform (e.g. a day’s or a month’s delay to pay) is a matter for the agreement between the parties and the law applicable to that agreement.

Encumbered asset

42. Any movable asset to which the Model Law applies may be an encumbered asset. In order to apply the provisions of the Model Law to outright transfers of receivables by agreement, the term also includes a receivable that is the subject of an outright transfer by agreement.

Equipment

43. 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 clarify that: (a) goods used or intended to be 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 or intended to be 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 “other than inventory or consumer goods” as, depending on their primary use or primary intended use, the same type of tangible assets may be, at different times, “equipment”, “consumer goods” or “inventory” (see art. 2, subparas. (f), (l) and (q), and paras. 39 above and 47 below).

Grantor

44. The definition of the term “grantor” makes clear that a grantor of a security right may be the debtor of the secured obligation or another person (e.g. the parent company of the debtor-subsidiary if the parent company creates a security right in its assets so that the subsidiary may borrow; see art. 2, subpara. (o) (i)). A person who is not the owner of an asset but has rights in the asset (e.g. rights under a lease or licence agreement; see art. 2, subpara. (o) (i)) may also be a grantor of a security

right, not in the asset, but in the rights that that person has in that asset. A buyer or other transferee of an encumbered asset that acquires the asset subject to a security right is also treated as a grantor, even if that person did not create a security right in the asset (see art. 2, subpara. (o) (ii)). In order to apply the provisions of the Model Law to outright transfers of receivables by agreement, the term "grantor" also includes a transferor under an outright assignment of receivables (see art. 2, subpara. (o) (iii)).

Insolvency representative

45. As the term "insolvency representative" is used only in the definition of the term "competing claimant" it is not defined in the Model Law. For the same reason, the term "insolvency proceedings", which is referred to in articles 2, subparagraph (e) (iii), 35 and 94 (and other insolvency-related terms, such as the term "insolvency estate"), is not defined in the Model Law. Those terms are defined though in the Secured Transactions Guide (see Introduction, para. 20) and the UNCITRAL Legislative Guide on Insolvency Law (the "Insolvency Guide"; see Introduction, para. 12). In particular the term "insolvency representative" is defined in a sufficiently broad manner to include the person responsible for administering insolvency proceedings or supervising the debtor and the debtor's affairs (see Insolvency Guide, part two, chap. III, paras. 11-18 and 35).

Intangible asset

46. 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 other movable asset that is not a tangible asset (see art. 2, subpara. (p)).

Inventory

47. The term "inventory" refers to tangible assets held by the grantor for sale or lease in the ordinary course of the grantor's business. Thus, it is the purpose for which tangible assets are held by the grantor that determines whether they constitute inventory (see paras. 39 and 43 above). The term "work in process" includes "semi-processed materials". 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. (q)).

Mass and product

48. The Model Law distinguishes between a "mass" and a "product". A "mass" is a combination that arises when two or more tangible assets of the same type are commingled in such a way that they lose their separate identity. This could happen, for example, when a quantity of oil from one source is pumped into a storage tanker that already contains some oil from another source, or when a truckload of one farmer's wheat is put into a grain silo that already contains wheat from another farmer. In contrast, a "product" arises when a tangible asset is physically transformed so that it loses its separate identity, or is physically united with one or more tangible assets so that they lose their separate identities, through a production or manufacturing process; for example, when gold is used to make a ring, or when flour and yeast are used to make bread. The distinction is relevant to articles 11 and 33.

Money

49. The term "money" includes not only the national currency of the enacting State but also the currency of any other State (see art. 2, subpara. (t)). However, it does not include virtual currency, as virtual currency is not national currency and is intangible (and money is in principle defined as a tangible asset; see art. 2, subpara. (ll)). Currency must qualify as a legal tender to constitute money. Rights to

payment of funds credited to a bank account and negotiable instruments are distinct concepts in the Model Law. They are not included in the term “money”.

Movable asset

50. The enacting State may wish to ensure that this definition captures anything that its laws consider to be an asset other than immovable property (see art. 2, subpara. (u)). Depending on its legal tradition and the terminology used, the enacting State may also wish to consider whether to replace the terms “movable asset” and “immovable property” with the equivalent concepts in its law (e.g. “personal property” and “land”).

Non-intermediated securities

51. The term “non-intermediated securities” refers to securities (i.e. shares and bonds) that are not credited to a securities account (see art. 2, subparas. (w) and (ii)). This definition is structured around the definition of the term “intermediated securities” in the Unidroit Securities Convention (see art. 1, subpara. (b)). It refers only to “rights”, in contrast to the language used in the Unidroit Securities Convention which refers to “rights or interests”, for reasons of consistency with the terminology of the Model Law in which the term “right” is a broad term that covers any right or interest. It should be noted that, if securities are held by an intermediary directly with the issuer (e.g. the intermediary is registered in the books of the issuer as the holder of the securities), these securities in the hands of the intermediary are non-intermediated, even though equivalent securities credited by the intermediary to a securities account in the name of a customer are intermediated securities in the hands of the customer.

Notification of a security right in a receivable

52. The definition of the term “notification of a security right in a receivable” (see art. 2, subpara. (v)) is based on the definition of the term “notification of the assignment” in the Secured Transactions Guide (see Introduction, para. 20, and rec. 118), which in turn is based on the definition of that term in the Assignment Convention (see art. 5, subpara. (d)). The requirement for the identification of the encumbered receivable and the secured creditor in the definition of that term in the Assignment Convention is reflected in article 62, paragraph 1, of the Model Law 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

53. The definition of the term “possession” (see art. 2, subpara. (z)) is based on the definition of that term in the Secured Transactions Guide. The words “directly or indirectly” that were included in recommendation 28 of the Secured Transactions Guide were not included in this definition or article 16 which is based on that recommendation, because the definition is sufficiently broad to cover situations in which a person holds a tangible asset through another person (e.g. the issuer of a negotiable document may hold it through various persons responsible to perform parts of a multimodal transport contract).

Priority

54. The definition of the term “priority” (see art. 2, subpara. (aa)) is based on the definition of that term in the Secured Transactions Guide, which is in turn partly based on the definition of that term in the Assignment Convention (see art. 5, subpara. (g)). Like the definition in the Secured Transactions Guide, this definition does not include in the concept of “priority” the steps required to establish third-party effectiveness. Like the definition in the Assignment Convention and unlike the definition in the Secured Transactions Guide, however, this definition refers directly to the right of a person in preference to the right of another person.

Proceeds

55. The term “proceeds” in the Model Law (see art. 2, subpara. (bb)) has the same meaning as in the Secured Transactions Guide. 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 (e.g. if receivables are generated by the sale of encumbered inventory and those proceeds are deposited to a bank account, the right to payment of those funds constitutes proceeds of proceeds); and (c) natural fruits (e.g. the calves of encumbered cows) or civil fruits (e.g. rents arising from the lease of encumbered assets). It should be noted that the secured creditor’s right in proceeds is limited by various provisions of the Model Law. For example, under article 10, paragraph 1, the security right extends only to identifiable proceeds (see also art. 19, para. 2). It should also be noted that 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”.

56. The term is not limited to proceeds received by the original grantor but includes proceeds received by a transferee of an encumbered asset when that transferee is treated as a grantor because it acquired the encumbered asset subject to the security right. For example, where A creates a security right in its assets in favour of X and then A transfers the assets to B who acquires its rights in the assets subject to X’s security right and B subsequently sells the assets to C for a price of €1,000 payable at a future date, the receivable arising from the sale by B to C constitutes proceeds covered by X’s security right. The reason for this approach is that, otherwise, a transferee of an encumbered asset that acquired the asset subject to the security right (in the example, B) could sell the asset further (in the example, to C) and keep the proceeds free of the security right (the issue of third-party transferees who are likely to search the registry under the name of their immediate transferor and who do not find a notice about a security right created by the first in a chain of transferors is dealt with in art. 26 of the Model Registry Provisions).

57. It should be noted that proceeds may arise as a result of an action taken by a person other than the grantor or a transferee. Thus, article 10, paragraph 2, applies to funds in a bank account that are transferred to another bank account (even if the transfer takes place at the instigation of the deposit-taking institution) as the funds in the second bank account are “proceeds”.

Receivable

58. The term “receivable” means a contractual or non-contractual right to payment of money (e.g. the right of a seller to the payment of a purchase price, the right of a lender for the payment of a loan or the right of a person for damages for breach of law; see art. 2, subpara. (dd)). However, it 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 creditor

59. The term “secured creditor” refers to the person that has a security right. In order to apply the provisions of the Model Law to outright transfers of receivables by agreement, it includes a transferee of a receivable in an outright transfer by agreement (e.g. a factor in a factoring contract).

Secured obligation

60. The term “secured obligation” includes any obligation secured by a security right, including obligations arising from credit extended by a lender, a retention-of-title seller or a financial lessor (see art. 2, subpara. (gg)). It covers both monetary and non-monetary obligations, obligations already incurred at the time of the extension of the credit and obligations incurred thereafter, if the security agreement

so provides. However, as there is no secured obligation in an outright transfer of a receivable, the provisions that refer to a "secured obligation" do not apply to an outright transfer of a receivable.

Securities

61. 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. (hh)). The reason is that, while a broad definition is appropriate for the purposes of that Convention, a broad definition for the purposes of the Model Law could result in an overlap with the terms "money", "receivable", "negotiable instrument" and other generic intangible assets and thus could cause uncertainty as to the regime applicable to security rights in those types of asset. In any case, the 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 law governing the transfer of securities. It should be noted that the definition of the term "securities" may also differ from the definition of the term as it is used in laws that regulate trading in securities, as the policies that inform the content of that definition may be different from the policies of the Model Law (e.g. the policy behind the definition of that term in those other laws is not to regulate security rights but rather to protect public markets).

Securities account

62. 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. (ii)). It refers to an account, which is maintained with a securities intermediary and to which securities may be credited or debited.

Security agreement

63. The term "security agreement" is defined as an agreement that provides for the creation of a security right (see art. 2, subpara. (jj)). In line with the functional, integrated and comprehensive approach followed in the Model Law (see para. 16 above), the parties need not use any special words; and even if the parties use wording that does not refer to security rights, the agreement is a security agreement if it provides for the creation of a property right in a movable asset that secures the payment or other performance of an obligation. As an example, it should be noted that, under the functional approach that characterises a transaction as a secured transaction if that is its functional effect, a retention-of-title sale *provides for the creation* of a security right in the asset that is the subject of the sale. Similarly, transactions such as transfers of property for security purposes, hire-purchase agreements and financial leases are treated as secured transactions, and an agreement that provides for them is a security agreement. In order to apply the provisions of the Model Law to outright transfers of receivables by agreement, the term "security agreement" also includes an agreement for the outright transfer of receivables.

Security right

64. The term "security right" is defined as a property right that is created by agreement to secure payment or other performance of an obligation. In line with the functional, integrated and comprehensive approach followed in the Model Law (see paras. 16 and 63 above), it is irrelevant whether or not the parties have denominated the right as a security right or whether or not the parties have used wording that refers to a security right. In order to apply the provisions of the Model Law to outright transfers of receivables by agreement, the term "security right" also includes the right of the transferee under an outright transfer of a receivable by agreement.

Tangible asset

65. The term “tangible asset” in the Model Law includes money, negotiable instruments, negotiable documents and certificated non-intermediated securities (some of these being intangible rights embodied in a document) except for the purposes of certain articles that contain rules that are not appropriate for those types of asset. For example, the term “tangible asset” in the definition of the term “mass” (see art. 2, subpara. (s)) does not include negotiable documents because negotiable documents cannot be part of a mass as they are not interchangeable with other documents and are not fungible.

Writing

66. The definition of the term “writing” is intended to ensure that where the term is referred to in the Model Law (see arts. 2 (g) and (x), 6, para. 3, 63, paras. 2 and 9, 65, paras. 1 and 2, 77, para. 2 (a), 78, para. 4 (b) and 80, paras. 1, 2 (b), 4 and 6, of the Model Law, as well as arts. 2, paras. 1-3, and 20, para. 5, of the Model Registry Provisions), this reference will include electronic communications (see art. 2, subpara. (nn)). The definition is based on recommendation 11 of the Secured Transactions Guide, which in turn is based on article 9, paragraph 2, of the United Nations Convention on the Use of Electronic Communications in International Contracts (the “Electronic Communications Convention”). However, the Model Law does not include an article on the electronic equivalent of signature along the lines of recommendation 12 of the Secured Transactions Guide, which is in turn based on article 9, paragraph 3, of the Electronic Communications Convention. For the purpose of those articles of the Model Law that refer to signature (see arts. 6, para. 1, and 65, paras. 1 and 2), the enacting States may wish to consider whether to include in their enactment of the Model Law an article along the lines of recommendation 12 of the Secured Transactions Guide.

International obligations of the enacting State

67. The Model Law leaves to the enacting State the issue whether international treaties (such as the United Nations Convention on Contracts for the International Sale of Goods (“CISG”) or the Assignment Convention when it enters into force) 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 (e.g. the creation, third-party effectiveness, priority and enforcement of a security right in movable assets). 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

68. Article 3 is based on article 6 of the Assignment Convention (the first sentence of which is based on art. 6 of CISG) and recommendation 10 of the Secured Transactions Guide. Paragraph 1 is intended to reflect the principle that, with the exception of the provisions listed in paragraph 1, parties are free to vary by agreement the effect of the provisions of the Model Law as between them. An agreement derogating from the provisions of the Model Law or varying its terms may be between any two parties whose rights are affected by the Model Law (e.g. between the secured creditor and the grantor, between the secured creditor and a competing claimant, between the secured creditor and the debtor of an encumbered receivable, or between the grantor and the debtor of the receivable).

69. The provisions listed in paragraph 1 are not subject to contrary agreement as permitting such an agreement with respect to these issues could result in abuse or uncertainty. In particular, article 4 sets out the general standard of conduct with which the parties have to comply when exercising their rights and performing their obligations under the Model Law; article 6 deals with the creation of a security right and sets out the requirements for the creation of a security right; article 9 deals with the standard for the description of encumbered assets and secured obligations; articles 53 and 54 deal with obligations of the party in possession to exercise reasonable care and the obligation of the secured creditor to return the encumbered assets; and article 72, paragraph 3, deals with the variation of rights under the enforcement provisions of the Model Law, and only permits variation by the grantor or the debtor after default, in order to avoid abuse at the time of the conclusion of the security agreement. Articles 85-87, in the chapter of conflict of laws, deal with the law applicable to property law matters; determination of the law applicable to such matters is generally not left to a choice of law by the parties, in order to ensure certainty with regard to the law applicable to property law matters, which are bound to involve rights of third parties.

70. Paragraph 2 reiterates the general principle of contract law that an agreement between two parties cannot affect the rights of a third party. For example: (a) if there are two debtors of a receivable that is an encumbered asset, and one of the two debtors agrees, pursuant to article 65, not to raise certain defences against a secured creditor, that agreement does not bind the other debtor of the receivable; and (b) if there are three secured creditors with a security right in the same encumbered assets whose order of priority is A, B and C, and secured creditor A agrees to subordinate its security right to that of secured creditor C, the rights of secured creditor B cannot be affected. The reason for reiterating this 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 otherwise appear to have an undue impact on the rights of third parties. It should be noted, however, that, under article 61, the impact of an agreement between the grantor of a security right in a receivable and the secured creditor is limited in the sense that, for example, the debtor of a receivable may have to pay a person other than the initial creditor.

71. Paragraph 3 makes clear that, if other law allows the parties to a security agreement to agree to resolve any dispute with respect to their security agreement or a security right created by that agreement by arbitration, mediation, conciliation and online dispute resolution, nothing in the Model Law affects that agreement. Paragraph 3 is based on the understanding that, the use of alternative dispute resolution mechanisms to resolve such disputes is important, in particular for developing countries and countries with inefficient judicial enforcement mechanisms, to attract investment, as inefficient judicial enforcement mechanisms are likely to have a negative impact on the availability and the cost of credit. It should be noted that paragraph 3 is intended to recognize the importance of alternative dispute resolution mechanisms and does not prejudice the resolution of questions relating to arbitrability, the protection of rights of third parties or access to justice.

Article 4. General standards of conduct

72. Article 4 is based on recommendation 131 of the Secured Transactions Guide (see chap. VIII, 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 standards 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. A breach of this obligation may result in liability for damages and other consequences that are left to the relevant law of the enacting State.

73. The concept of “commercial reasonableness” is not defined in the Model Law but it typically refers to actions that a reasonable person might take in circumstances that would be similar to those encountered in a particular case by any person that had rights and obligations under the Model Law. Inasmuch as there is typically no single course of action that all reasonable persons would take in a particular situation, depending on the circumstances and the type of right or obligation involved, a range of actions may meet the objective standard of “commercial reasonableness”. It should be noted that meeting the specific standards referred to in other provisions of the Model Law (e.g. art. 78, para. 4, according to which notice is to be given within a short period of time) should generally be sufficient to meet the general standards of conduct referred to in this article. It should also be noted that, 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

74. 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 provide guidance in the interpretation of the Model Law. The expected effect of article 5 is to limit the extent to which the Model Law, once incorporated in national law, would be interpreted only by reference to concepts of the national law.

75. The purpose of paragraph 1 is to draw the attention of any person that might be called to interpret and apply the Model Law (or a national law implementing the Model Law) to the fact that the provisions of the Model Law, while implemented as part of a national law, should be interpreted by reference to its international origin in order to ensure uniformity in the interpretation of the Model Law and the observance of good faith in all enacting States. It should be noted that the term “good faith” in paragraph 1 identifies a consideration to be taken into account in the interpretation of the Model Law. In contrast, in article 4, the term sets a standard to be complied with by parties in the exercise of their rights and the performance of their obligations under the Model Law.

76. Under paragraph 2, gaps in a law implementing the Model Law are to be filled by reference to the general principles on which the Model Law is based. As already noted (see para. 15 above), the overall economic objective of the Model Law is the same as that of the Secured Transactions Guide, to promote low-cost credit by enhancing the availability of secured credit (for a complete statement and discussion of the key objectives of an effective and efficient secured transactions law, see Secured Transactions Guide rec. 1 and Introduction, paras. 43-59).