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Draft Technical Legislative Guide on the Implementation of a Security Rights Registry

Note by the Secretariat

Addendum

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Introduction (*continued*)

E. Overview of secured transactions law and the role of registration (*continued*)

5. Priority of a security right (*continued*)

(b) Buyers or other transferees of encumbered assets

1. As a general rule, the *Secured Transactions Guide* recognizes that a secured creditor that has complied with the requirements for third-party effectiveness with respect to its security right has a “right to follow” the encumbered asset into the hands of a buyer or other transferee from the grantor that acquires rights in the encumbered asset (see *Secured Transactions Guide*, chap. II, paras. 72-89, chap. III, paras 15, 16 and 89, and rec. 79). Conversely, a transferee will take free of a security right that has not been made effective against third parties by registration or by some other method even if it has actual knowledge of the existence of the security right. This approach is not unfair to secured creditors since they could have protected themselves by timely registration or by otherwise making their security right effective against third parties.

2. However, the *Secured Transactions Guide* recognizes a number of exceptions to this general rule. The following paragraphs summarize the principal exceptions.

3. First, a buyer or lessee or licensee that acquires an encumbered asset with the consent of the secured creditor acquires the asset free of the security right or takes its rights unaffected by the security right (see *Secured Transactions Guide*, rec. 80). This approach facilitates transactions that have been approved by a secured creditor typically after some arrangement has been made to provide other security to the secured creditor.

4. Second, a buyer or lessee or licensee that acquires an encumbered asset in the ordinary course of the grantor’s business takes free of any security right in that asset even if the secured creditor has registered a notice of the security right or otherwise complied with the requirements for third-party effectiveness (see *Secured Transactions Guide*, rec. 81). This approach is consistent with the reasonable commercial expectations of the parties involved. It is not realistic to expect buyers dealing with a commercial enterprise which routinely sells the types of asset in which the buyer is interested, for example, computer equipment, to check the registry before entering into the transaction. Moreover, a secured creditor that takes a security right in a grantor’s inventory will normally have done so on the understanding that the grantor may dispose of the inventory free of the security right in the ordinary course of the grantor’s business. After all, for the grantor to be able to generate the revenue necessary to pay back the secured loan, its customers need to be assured that they will acquire unencumbered title in any inventory sold to them in the grantor’s ordinary course of business.

5. Third, the same policy of preserving negotiability that justifies awarding a special priority to secured creditors that take physical possession of encumbered assets in the form of money or negotiable documents (such as a bill of lading) or negotiable instruments (such as a cheque) also justifies awarding priority to outright

transferees of these types of encumbered asset (see *Secured Transactions Guide*, recs. 101, 102, 108 and 109).

6. Fourth, as already mentioned, the *Secured Transactions Guide* may apply to assets that are subject to a specialized registration regime, such as motor vehicles, ships, aircraft and intellectual property (see *Secured Transactions Guide*, chap. I, paras. 32-36, and rec. 4, subparas. (a) and (b)). These registries typically serve broader goals than simply publicizing security rights in the relevant assets, notably, also recording ownership or transfers of ownership. Accordingly, to the extent that the *Secured Transactions Guide* applies to security rights in these types of asset, it recommends that priority be given to a buyer or other transferee that registered in the specialized registry as against a security right registered in the general security rights registry; and where the security right is also registered in the specialized registry, priority should be determined by the order of registration (see *Secured Transactions Guide*, recs. 77 and 78).

7. Fifth, a similar approach is taken to priority competitions involving security rights in attachments to immovable property. The *Secured Transactions Guide* recommends that priority should be given to a buyer or other transferee of the relevant immovable property that registered in the immovable property registry as against a security right in the attachment that is registered only in the general security rights registry; and where the security right in the attachment is also registered in the immovable property registry, priority should be determined by the order of registration (see *Secured Transactions Guide*, recs. 87 and 88).

(c) Unsecured creditors of the grantor

8. One of the principal advantages of taking security is that it entitles the secured creditor to claim the value of the encumbered assets in preference to the claims of the grantor's unsecured creditors. Accordingly, the *Secured Transactions Guide* recommends that a security right has priority over the rights of an unsecured creditor provided that the secured creditor registers or otherwise makes its security right effective against third parties before the unsecured creditor obtains a judgement or provisional court order against the grantor and takes the steps necessary under other law of the enacting State to acquire rights in the encumbered assets (see *Secured Transactions Guide*, rec. 84). This approach enables unsecured creditors to determine the extent to which their debtors' assets may be encumbered in order to decide whether it is worthwhile to obtain a judgement and pursue judgement enforcement proceedings. This priority rule, however, is subject to an important caveat. Even if the secured creditor registers a notice of its security right or otherwise achieves third-party effectiveness after the unsecured creditor acquires rights in its debtor's encumbered assets, the secured creditor will have priority to the extent of credit that it advances before it has actual knowledge that the unsecured creditor has acquired rights in the encumbered assets or that it advances pursuant to a prior irrevocable commitment to extend credit to the grantor (see *Secured Transactions Guide*, chap. V, paras. 94-106, and rec. 84).

9. The *Secured Transactions Guide* discusses but does not make any recommendation with respect to the steps that an unsecured creditor must take to acquire rights in its debtor's assets so as to potentially prevail over a secured creditor that has failed to achieve third-party effectiveness at all or in time (see *Secured Transactions Guide*, chap. V, paras. 94-106). This is left to the

judgement enforcement and execution law of the enacting State. In some States, an unsecured creditor acquires rights in its debtor's assets only once the judgement enforcement process is completed by seizure and sale and the judgement creditor's rights attach to the proceeds of the sale. In other States, an unsecured creditor upon obtaining judgement can obtain the equivalent of a general security right in the judgement debtor's present and future movable assets simply by registering a notice of the judgement in the general security rights registry. Accordingly, States enacting the general recommendations of the *Secured Transactions Guide* will need to take into account their existing law on this issue and decide on the most appropriate approach.

(d) The insolvency representative

10. Modern insolvency laws generally respect the priority to which secured creditors are entitled under other law in the event that insolvency proceedings are commenced against the grantor. This is the approach recommended in the *Secured Transactions Guide* (see *Secured Transactions Guide*, rec. 239) in line with the UNCITRAL Legislative Guide on Insolvency Law (the "Insolvency Guide"). It follows that a secured creditor generally will have priority over the claims of an insolvent grantor's unsecured creditors, provided that it registered or otherwise satisfied the third-party effectiveness requirements of secured transactions law before the commencement of the insolvency proceedings. Conversely, the failure of the secured creditor to register a notice or otherwise make its security right effective against third parties before the commencement of the insolvency proceedings generally results in the secured creditor being effectively demoted to the status of an unsecured creditor. This approach encourages timely registration or the taking of other third-party effectiveness steps by secured creditors. It also enables the grantor's insolvency representative to determine efficiently which of the grantor's assets may have been effectively encumbered.

11. Timely registration does not, however, protect a secured creditor from challenges on the basis of general insolvency law policies, such as rules avoiding preferential or fraudulent transfers and rules giving priority to certain protected classes of creditors (see *Secured Transactions Guide*, chap. XII, and rec. 239; see also *Insolvency Guide*, recs. 88 and 188).

12. A security right that was effective against third parties at the time of the commencement of the insolvency proceedings might lapse thereafter, for example, because it was made effective against third parties by registration and the period of effectiveness of the registration is due to expire. To address this risk, the *Secured Transactions Guide* recommends that a secured creditor should be entitled to take any action required by the secured transactions law to preserve the effectiveness of its security right against third parties even after the commencement of insolvency proceedings (see *Secured Transactions Guide*, rec. 238). This recommendation is designed to ensure that a secured creditor is not denied the ability to maintain its priority status as a result of the automatic stay typically imposed on enforcement action by creditors upon the commencement of insolvency proceedings.

13. Where the insolvency proceeding takes the form of a reorganization, modern insolvency laws generally authorize the insolvent grantor to create a security right to obtain post-commencement finance (see *Insolvency Guide*, rec. 65). Under the *Insolvency Guide*, such a security right does not have priority over any existing

secured creditors unless agreed to by them or authorized by the court with the appropriate protections for them. When post-commencement finance is provided, the rules of the secured transactions law governing the third-party effectiveness of security rights will apply.

(e) Preferential claims

14. For various policy reasons, a State's secured transactions law, insolvency law or both may sometimes award preferential priority status over the claims of secured creditors to specified categories of unsecured creditors. Typical examples include the claims of the enacting State for taxes and of employees for unpaid wages or other employment benefits. In addition, in the insolvency context, some States set aside a specified portion of the value of encumbered assets, particularly business assets, in favour of unsecured creditors in preference to the secured creditor. The *Secured Transactions Guide* discusses preferential claims and recommends that, to the extent an enacting State decides to maintain any, they should be limited in both type and amount and prescribed in the secured transactions law and the insolvency law, as the case may be, in a clear and specific way (see *Secured Transactions Guide*, chap. V, paras. 90-93, and chap. XII, paras. 59-63, and recs. 83 and 239). The reason why the *Secured Transactions Guide* follows this approach is twofold; on the one hand, the *Secured Transactions Guide* is mindful of the social policies enacting States may wish to pursue with preferential claims; on the other hand, the *Secured Transactions Guide* recognizes that preferential claims may have an impact on the cost and availability of credit.

15. In some States, preferential claims may be registered in the general security rights registry although in those States, the same registration and priority rules that apply to security rights may not necessarily apply to preferential claims. The *Secured Transactions Guide* discusses but does not make any recommendation with respect to whether preferential claims should have to be registered and what the priority implications of registration should be (see *Secured Transactions Guide*, chap. V, para. 90).

6. Broad transactional scope of the registry

(a) Outright assignments

16. As already explained (see A/CN.9/WG.VI/WP.52, paras. 27-29), the secured transactions law contemplated by the *Secured Transactions Guide* is comprehensive in scope, covering all transactions that in substance function to secure an obligation regardless of the formal character of the secured creditor's property right, the type of encumbered asset, the nature of the secured obligation or the status of the parties (see *Secured Transactions Guide*, chap. I, paras. 101-112, and recs. 2 and 10).

17. In addition to applying to all secured transactions defined in the functional, integrated and comprehensive sense just outlined, the *Secured Transactions Guide* recommends that the secured transactions law should also apply, at least to some extent, to outright assignments of receivables. However, bringing outright assignments within the scope of the secured transactions law does not mean that these transactions are re-characterized as secured transactions. Rather, it is intended to ensure that an outright assignee of receivables is subject to the same rules relating to creation, third-party effectiveness and priority (but generally not enforcement) as

the holder of a security right in receivables. It also ensures that the outright assignee has the same rights and obligations vis-à-vis the debtor of the receivable as a secured creditor (see *Secured Transactions Guide*, chap. I, paras. 25-31, and recs. 3 and 167).

18. Under this approach, an assignee generally will have to register a notice of its right in the security rights registry for the assignment to be effective against third parties; and priority among the rights of successive competing assignees or secured creditors that have acquired rights in the same receivables from the same assignor/grantor will be determined by the order of registration (see *Secured Transactions Guide*, chap. III, para. 43). The reason for this approach is that outright assignments of receivables not only perform a financing function but also create the same problem of information inadequacy for third parties as security rights in receivables. Unless a notice is registered in the security rights registry as a condition of third-party effectiveness, a potential secured creditor or assignee or other third party would have no efficient means of verifying whether the receivables owed to a business have already been assigned or, if assigned, whether the assignment is an outright assignment or an assignment for security purposes. While inquiries could be made of the debtors of the receivables, this is not practically feasible if the debtors of the receivables have not been notified of the assignment or the transaction covers present and future receivables generally.

(b) Additional non-security transactions

19. True long-term leases and consignment sales of movable assets do not operate to secure the acquisition price of assets and consequently do not qualify as security rights so as to fall within the secured transactions law contemplated by the *Secured Transactions Guide*. However, they create the same publicity problems for third parties as non-possessory security rights since they necessarily involve a separation of a property right (the ownership of the lessor or consignor) from actual possession (which is with the lessee or consignee). To address this concern, some States expand the scope of their secured transactions regime (other than enforcement) as it applies to acquisition security rights to these types of transaction. In addition to ensuring adequate publicity to third parties, this approach also diminishes the risk of litigation concerning whether a transaction in the form of a lease or a consignment is actually a secured transaction and thus ineffective if a notice with respect to it is not registered or subordinate in priority if the rules governing the special priority given to acquisition security rights do not apply. The *Secured Transactions Guide* discusses but makes no recommendation on this matter (see *Secured Transactions Guide*, chap. III, para. 44). It may be noted, however, that, if a lessor or a consignor is concerned about the risk to its third-party effectiveness or priority status where its right is characterized as a security right, it can always register a precautionary notice so as to avoid any challenges to the effectiveness of its rights against third parties.

7. Conflict-of-laws considerations

20. In situations where a secured transaction is connected to more than one State, secured creditors and third parties need clear guidance as to which State's law applies to the transactions. Under the conflict-of-laws approach recommended in the *Secured Transactions Guide*, the applicable law depends on the nature of the

encumbered assets. For example, the law applicable to the creation, third-party effectiveness and priority of a security right in tangible assets is generally the law of the State in which the encumbered asset is located (see *Secured Transactions Guide*, rec. 203). This means that, where a secured creditor wishes to make its security right effective against third parties by registration, it must register a notice of its security right in the registry of the State where the encumbered asset is located. It follows that, where the encumbered assets are located in multiple States, multiple registrations will generally be necessary. With respect to security rights in intangible assets and mobile assets that are ordinarily used in multiple jurisdictions, the applicable law is the law of the State in which the grantor is located (see *Secured Transactions Guide*, rec. 208). As a result, the secured creditor must register a notice of its security right in the registry of the State where the grantor is located if it wishes to achieve third-party effectiveness by registration.

21. The rules outlined above are the general baseline rules. the *Secured Transactions Guide* recommends different specialized conflict-of-laws rules for security rights in specific types of asset. These types of asset include: (a) assets rights in which are subject to a specialized registration regime; (b) receivables arising from a transaction relating to immovable property; (c) rights to the payment of funds credited to bank accounts; (d) rights to receive the proceeds under an independent undertaking; and (e) intellectual property rights (see *Secured Transactions Guide*, recs. 204-207, 209-215 and 248). For example, where the encumbered asset is an intellectual property right, the applicable law is primarily the law of the State under which the intellectual property is protected, although a security right that is created and made effective against third parties only under the law of the State in which the grantor is located may still be effective against the grantor's insolvency representative and judgement creditors (see *Supplement*, rec. 248).

8. Notice registration

22. Most States have established registries for recording title and encumbrances on title on immovable property. Many States have also established similar title registries for a limited number of high-value movable assets, such as ships and aircraft. It is essential to the successful implementation of the kind of general security rights registry contemplated by the *Secured Transactions Guide* that its very different characteristics be well understood by those responsible for its design and operation, as well as by its potential clientele.

23. First, unlike the typical land, ship or aircraft registry, the general security rights registry contemplated by the *Secured Transactions Guide* does not purport to record the existence or transfer of title to the encumbered asset described in the notice or to guarantee that the person named as grantor in the notice is the true owner. It simply provides a record of potentially existing security rights on whatever property right the grantor has or may acquire in the assets described in the notice as a result of off-record transactions or events (see *Secured Transactions Guide*, chap. IV, paras. 10-14).

24. Second, title registries typically require registrants to file or tender for scrutiny the underlying documentation. This is because registration generally is considered to constitute evidence or at least presumptive evidence of title and any property rights affecting title.

25. While, the security rights registries in some States also require submission of the underlying security documentation, the *Secured Transactions Guide* recommends that States adopt a notice registration rather than a document registration system (see *Secured Transactions Guide*, recs. 54, subpara. (b), and 57). A notice registration system does not require the actual security documentation to be registered or even tendered for scrutiny by registry staff. All that need be registered is a notice that provides the basic information necessary to alert a searcher that a security right may exist in the assets described in the notice. It follows that registration does not mean that the security right to which the notice refers necessarily exists; only that one may exist at the time of registration or may come into existence later. As already explained (see A/CN.9/WG.VI/WP.52, paras. 30 and 36), registration of a notice is irrelevant to the creation of a security right; it simply makes any security right created by an off-record security agreement between the parties effective against third parties provided the other requirements for creation outlined earlier are satisfied (see *Secured Transactions Guide*, recs. 32, 33 and 67).

26. The *Secured Transactions Guide* recommends notice registration rather than document registration because notice registration:

(a) Reduces transaction costs for registrants (as they do not need to register or provide evidence of the security documentation in order to register) and third-party searchers (as they do not need to peruse what may be voluminous security documentation to determine if a security right may exist in the relevant assets);

(b) Reduces the administrative and archival burden on registry system operators;

(c) Reduces the risk of registration error (since the less information that must be submitted, the lower the risk of error); and

(d) Enhances privacy and confidentiality for secured creditors and grantors (the less the information that must be registered, the less the information that is available to searchers).

27. As registration in a notice registration system does not necessarily mean that a security right actually exists, third parties with a competing property right in the encumbered assets will normally wish to demand proof of the existence of an effective security agreement between the parties and the scope of the assets covered by it. The same is true even where the alleged security right has been made effective against third parties by some other method, such as a transfer of possession, since possession by the putative secured creditor may be for a purpose other than security.

28. Some States provide a procedure whereby a third party with a property right in the encumbered asset may demand this information directly from the person named as a secured creditor in a registration or who is otherwise claiming this status. The same right is extended to unsecured creditors of the grantor so as to enable them to assess whether it is worthwhile to undertake the expense of obtaining a judgement and pursuing enforcement against the debtor's assets. While the *Secured Transactions Guide* does not make a recommendation on this matter, it is always open to the debtor to request the secured creditor to send the relevant information directly to a third party. However, the debtor or the secured creditor may not be

cooperative in which event the third party will need to seek a judicial order under other law.

29. Even in States that allow third parties to demand verification of the existence of a security right and its scope directly from the secured creditor, this right does not apply to potential buyers or potential secured creditors. They can protect themselves simply by refusing to buy or extend secured credit unless the registration relating to the security right is cancelled or the putative secured creditor is willing to undertake to them that it is not asserting and will not assert in the future a security right in the asset in which they are interested.

30. The grantor may also need to obtain up-to-date information about the scope and value of the security right claimed by its secured creditor and a copy of any written security agreement under which the security right is claimed. In some States, the grantor is entitled to demand this information free of charge although limits are usually placed on the frequency with which requests may be made so as to discourage demands that are unjustified or intended to harass.

31. A notice registered in the registry record contains minimum information about a security right that may not even exist at the time of registration and the amount of the secured obligation or the encumbered assets may change from time to time (see *Secured Transactions Guide*, rec. 57, A/CN.9/WG.VI/WP.52/Add.4, paras. 1-23, and draft Registry Guide, rec. 21). Thus, in certain circumstances, the grantor may need to request additional information about the security right. While the *Secured Transactions Guide* does not take a position on this issue, in some States, secured transaction law provides that the grantor is entitled to request the person identified in the notice as the secured creditor to provide to the searcher additional information about the security right. This information includes: (a) a list of the assets in which the person identified as the secured creditor is claiming a security right; and (b) the current amount of the obligation secured by the security right to which the registration relates, including the amount needed to pay off the secured obligation. The ability of a third party to obtain information from the secured creditor takes account of the fact that registration does not create or evidence the creation of a security right but merely signals that a security right may exist in a particular asset. Whether the security right has been created, and the scope of the assets which it covers, depends on off-record evidence. Consequently, prospective buyers and secured creditors and other third parties with whom the grantor is dealing may wish to have independent verification directly from the person identified in the notice as the secured creditor as to whether it is in fact currently claiming a security right in an asset in which they are interested under an existing security agreement with the named grantor. In some States, the grantor is entitled to one request free of charge every few months. For additional requests for information, the secured creditor may charge a fee. This approach protects the secured creditor from having to respond to frequent requests of the grantor that may not be justified or be intended to harass.

9. The role of registration and its legal consequences

(a) Creation, third-party effectiveness and registration

32. As already mentioned (see A/CN.9.WG.VI/WP.52, paras. 30 and 36), the *Secured Transactions Guide* recommends that registration should not be an element of the creation of a security right (see *Secured Transactions Guide*, rec. 33). Rather

the security right takes effect and becomes enforceable between the grantor and the secured creditor as soon as a security agreement is concluded (see *Secured Transactions Guide*, recs. 13-15). Registration is purely a precondition to the third-party effectiveness of the security right. The only sanction for a secured creditor's failure to register a notice of its security right is that the security right will not be effective against third parties (unless another method of third-party effectiveness is followed).

(b) Registration and enforcement

33. Some legal regimes require secured creditors to register in the general security rights registry a notice that they have initiated or propose to initiate an enforcement action. The goal of this approach is to enable the registry to notify third parties that have registered a competing right in the encumbered assets in the registry of the details of the pending enforcement. The *Secured Transactions Guide* does not recommend this approach. Instead, the *Secured Transactions Guide* recommends that the enforcing secured creditor should be required to search the registry and send out the required notices to interested third parties (including competing claimants) of the particular enforcement remedy that it seeks to exercise (see *Secured Transactions Guide*, rec. 151). Such notification will provide these third parties with an opportunity (should they choose to avail themselves of it) to remedy the default that has given rise to the enforcement proceeding.

10. Coordination with specialized movable property registries

34. Where specialized registries exist and permit the registration of security rights in movable assets with third-party effects (as is the case with the international registries under the Convention on International Interests in Mobile Equipment and its Protocols), modern secured transactions regimes must deal with matters related to the coordination of registrations in the two types of registry. The *Secured Transactions Guide* and the *Supplement* discuss coordination of registries in detail (see the *Secured Transactions Guide*, chap. III, paras. 75-82, chap. IV, para. 117; and the *Supplement*, paras. 135-140).

35. For example, the *Secured Transactions Guide* provides that a security right in an asset subject to specialized registration may be made effective against third parties by registration in the general security rights registry or in the specialized registry. It addresses the issue of coordination between the two types of registry through appropriate priority rules, giving priority to a security right, a notice of which is registered in the relevant specialized registry, over a security right in the same asset, a notice of which is registered in the general security rights registry, irrespective of the time of registration (see *Secured Transactions Guide*, recs. 43 and 77, subpara. (a)).

36. The *Secured Transactions Guide* also discusses other ways of coordinating registries, including the automatic forwarding of information registered in one registry to another registry and the implementation of common gateways to the various relevant registries. This approach raises complexities with respect to the design of the general security rights registry where the specialized registry organizes registrations by reference to the asset as opposed to the grantor-based indexing system used in the general security rights registry (see *Secured*

Transactions Guide, chap. III, paras. 77-81; see also A/CN.9/WG.VI/WP.52/Add.2, paras. 30-35).

11. Coordination with immovable property registries

37. Immovable property registries exist in most, if not in all, States. Typically, the general security rights registry is separate from the immovable property registry owing to differences as to what is registered (that is, document or notice), the requirements for the description of the encumbered asset (that is, specific or generic), indexing structures (that is, asset-based or debtor-based indices; see also A/CN.9/WG.VI/WP.52/Add.2, paras. 30-35) and legal consequences of registration.

38. However, some coordination of the two types of registry may be necessary with respect to assets, rights in which may be registered in either type of registry. Thus, a State implementing a general security rights registry will need to provide potential secured creditors and third-party financiers with guidance as to where notices relating to security rights in attachments to immovable property should be registered. The *Secured Transactions Guide* recommends that such registrations may be made either in the general security rights registry or in the immovable property registry (see *Secured Transactions Guide*, rec. 43). The choice between the two types of registration has priority consequences. In this regard, the *Secured Transactions Guide* recommends that an encumbrance registered in the immovable property registry has priority as against a security right a notice of which was registered only in the security rights registry (see *Secured Transactions Guide*, rec. 87). The *Secured Transactions Guide* also recommends that the security right in an attachment to immovable property will be ineffective against a buyer (or other third party) that acquires a right in the immovable property unless a notice with respect to the security right is registered in the immovable property registry in advance of the sale (see *Secured Transactions Guide*, rec. 88).

39. It should also be noted that the asset description requirements as to notices relating to security rights in an attachment to immovable property may differ depending on whether the notice is to be registered in the security rights registry or in the immovable property registry. The *Secured Transactions Guide* recommends that an attachment to immovable property, just like any other encumbered asset, should be described in a manner that reasonably allows its identification when registering a notice in the security rights registry (see *Secured Transactions Guide*, rec. 57, subpara. (b)). Thus, a description of the tangible asset that is or will be attached without a description of the immovable property is sufficient for the purposes of registering such a notice in the security rights registry. In contrast, registering such a document or notice in the immovable property registry will generally require that the immovable property to which the tangible asset is or will be attached be described sufficiently under the law of immovable property. Such description must be sufficient to allow the indexing of the notice in the immovable property registry.

I. Establishment and functions of the security rights registry

A. General remarks

1. Establishment of the security rights registry

40. As already mentioned, chapter IV of the *Secured Transactions Guide* contains commentary and recommendations on many aspects related to the establishment of a security rights registry and the registration and search process. The recommendations in chapter IV cover both legal issues that are typically dealt with in the principal secured transactions law and design and operational issues that are typically addressed in a supplementary body of administrative rules, referred to in the draft Registry Guide as the “regulation”. This approach enables the rules relating to the registration and search functions of the registry to be more easily revised from time to time to accommodate technological improvements and the like. As already elaborated (see A/WG.VI/WP.52, paras. 35-40), the *Secured Transactions Guide* clarifies that the purpose of the security rights registry is to provide: (a) a method by which a security right may be made effective against third parties; (b) an efficient point of reference for determining the ordered of priority of security rights with respect to which a notice has been registered; and (c) an objective source of information for third parties (see *Secured Transactions Guide*, chap. IV, purpose). Typically, the opening provisions of the regulation provide for the establishment of the registry and reiterate briefly that, in line with its purpose as set out in the law, the purpose of the registry is to receive, store and make available to the public, information relating to security rights in movable assets (see draft Registry Guide, rec. 1).

2. Appointment of the registrar

41. The appointment of the person that is to supervise and administer the operation of the registry (the “registrar”) is another of the matters that is usually dealt with in the initial provisions of the regulation. The regulation typically identifies, either directly or by reference to the relevant law, the authority that is empowered to appoint the registrar, determine his or her duties and generally supervise the registrar in the exercise of those duties. To ensure flexibility in the administration of the registry, the term registrar should be understood as referring either to a single person or to a group of persons appointed and supervised by the registrar to perform his or her duties (see draft Registry Guide, rec. 2).

3. Functions of the registry

42. The opening provisions of the regulation might also include a provision that lists the various functions of the registry that are dealt with in detail in the later provisions of the regulation with a cross-reference to the relevant provision of the regulation in which these functions are addressed. This is the approach recommended in the draft Registry Guide (see draft Registry Guide, rec. 3). The advantage of this approach is clarity and transparency as to the nature and scope of the issues that are dealt with in detail later in the regulation. The possible disadvantage is that the list may not be comprehensive or may be read as implying unintended limitations on the detailed provisions of the regulation to which

cross-reference is made. Accordingly, implementation of this approach requires special care to avoid any omissions or inconsistencies.

4. Additional implementation considerations

43. It is critical that the technical staff responsible for the design and implementation of the registry are fully apprised of the legal and practical objectives that it is designed to fulfil, as well as of the practical needs of the registry personnel and of potential registry users. Consequently, it is necessary at the very outset of the design and implementation process to constitute a team that reflects technological, legal and administrative expertise, as well as user perspectives.

44. It will also be necessary at an early stage in the registry design and implementation process to determine whether the registry is to be operated in-house by a governmental agency or in partnership with a private sector firm with demonstrated technical experience and financial accountability. While the day-to-day operation of the registry may be delegated to a private entity, the enacting State should always retain the responsibility to ensure that the registry is operated in accordance with the applicable legal framework (see *Secured Transactions Guide*, chap. IV, para. 47, and rec. 55, subpara. (a)). Accordingly, for the purposes of establishing public trust in the registry and preventing commercialization and fraudulent use of information in the registry record, the enacting State should retain ownership of the registry record and, when necessary, the registry infrastructure.

45. The design team will need to plan the storage capacity of the registry record. This assessment will depend in part on whether the registry is intended to cover consumer as well as business secured financing transactions. If this is the case, a much greater volume of registrations can be anticipated and thus the storage capacity should be increased. Capacity planning will need to take into account the potential for additional applications and features to be added to the system. For example, designers will need to take into account the need to expand the registry database at a later point to accommodate the registration of judgements or non-consensual security rights or the addition of linkages to other governmental records such as the State's corporate registry or its other movable or immovable registries. Capacity planning will depend as well on whether registered information is stored in a computer database or a paper record. Ensuring sufficient storage capacity is less of an issue if the record is in electronic form since recent technological developments have greatly decreased storage costs (the *Secured Transactions Guide* recommends that the registry be electronic "if possible"; see rec. 54, subpara. (j), and paras. 48-55 below).

5. Registry terms and conditions of use

46. As already mentioned, registry-related matters are typically dealt with in the secured transactions law and the registry regulation. They may also be addressed in the registry "terms and conditions of use". The registry terms and conditions of use are the terms and conditions of the contract that is entered into by people who file, modify or delete notices, on the one hand, and the contract governing the terms of access for searchers, on the other. For example, the registry terms and conditions of use may offer the opportunity to a regular user of the registry to open an account. Such an account could offer practical benefits such as quick access and a simplified mechanism for the payment of any fees. In addition, the registry terms and

conditions of use should address the issues of the security and confidentiality of information and user data (such as, for example, user name and password, or other modern security technique).

47. Some registry systems, upon request, make available to users additional services. These services include, for example, the following: (a) search audit, which provides information as to how a search was performed with the exact and similar match list indicating which similar matches were requested as a follow-up search; (b) transaction inquiry, which allows a user to track by his or her name or account information as to his or her transactions that occurred during a specified period of time; (c) secured creditor searches, which allow a searcher to search by secured creditor identifier; (d) advance search, which provides the ability to recover and make available all active and inactive registrations on the bases of a specified search criterion; (e) verification statement reprint, which provides reprints of a verification relating to a specific transaction; and (f) statistical reports.

6. Electronic or paper-based registry

48. The *Secured Transactions Guide* recommends that, if possible, the registry record should be electronic in the sense that information in notices is stored in electronic form in a computer database (see *Secured Transactions Guide*, chap. IV, paras. 38-41 and 43, and rec. 54, subpara. (j)(i)). An electronic registry record is the most efficient and practical means of enabling enacting States to implement the recommendation of the *Secured Transactions Guide* that the registry record must be centralized and consolidated to include all registrations made under the secured transactions law of the enacting State (see *Secured Transactions Guide*, chap. IV, paras. 21-24, and rec. 54, subpara. (e)).

49. The *Secured Transactions Guide* further recommends that, if possible, the registry should be electronic in the sense of permitting the direct electronic submission of notices and search requests by users over the Internet or via direct networking systems as an alternative to the submission of paper registration notices and search requests (see *Secured Transactions Guide*, chap. IV, paras. 23-26 and 43 and rec. 54, subpara. (j)(ii)). This approach is the most effective means of implementing the recommendation of the *Secured Transactions Guide* that the system should be designed to minimize the risk of human error (see *Secured Transactions Guide*, chap. IV, rec. 54, subpara. (j)(iii)-(iv)) since it eliminates the need for registry staff to enter the information contained in a paper notice or search request into the registry record and the risk of error associated with the transcription task.

50. Direct electronic registration and searching also contributes to a speedier registration and search process. When information is submitted to the registry in paper form, registrants must wait until the registry staff has entered the information into the registry record and the information is searchable by third parties before the registration becomes legally effective. Search requests transmitted by paper, fax or telephone also give rise to delays since searchers must wait until the registry staff member carries out the search on their behalf and transmits the results.

51. In addition to eliminating these delays and reducing the risk of human error, a registry system in which registrants and searchers have the option to electronically

enter the information directly into the registry record offers the following other advantages:

- (a) A very significant reduction in the staffing and other day-to-day costs of operating the registry;
- (b) Reduced opportunity for fraudulent or corrupt conduct on the part of registry personnel;
- (c) A corresponding reduction in the potential liability of the registry to users who otherwise might suffer loss as a result of the failure of registry staff to enter registration information or search criteria at all, or to enter it accurately; and
- (d) User access to the registration and searching services outside of normal business hours.

52. If this approach is implemented, the registry should be designed to permit registry users to submit a registration and conduct searches from any private computer facility, as well as from computer facilities made available to the public at branch offices of the registry or other locations. In addition, owing to the reduced costs of direct electronic access, the conditions governing access to the services of the registry should permit third-party private sector service providers to carry out registrations and searches on behalf of their clientele.

53. If the registry record is computerized, the hardware and software specifications should be robust and employ features that minimize the risk of data corruption, technical error and security breach. Even in a paper-based registry, measures should be taken to ensure the security and integrity of the registry record but this is more efficiently and easily accomplished if the registry record is in electronic form. In addition to database control programmes, software will also need to be developed to manage user communications, user accounts, payment of fees and financial accounting, computer-to-computer communication and the gathering of statistical data.

54. The necessary hardware and software needs will need to be evaluated and a decision made as to whether it is appropriate to develop the software in-house by the registry implementation team or purchase it from private suppliers. In making that determination, the team will need to investigate whether an off-the-shelf product is available that can easily be adapted to the needs of the implementing State. It is important that the developer/provider of the software is aware of the specifications for the hardware to be supplied by a third-party vendor, and vice versa.

55. Consideration should also be given to whether the registry should be designed to provide an electronic interface with other governmental databases. For example, in some States, registrants can search the company or commercial registry in the course of effecting a registration to verify and automatically input grantor or secured creditor identifier information (for a discussion of electronic matching of names, see A/CN.9/WG.VI/WP.52/Add.3, para. 10).

B. Recommendations 1-3

[*Note to the Working Group: The Working Group may wish to consider recommendations 1-3, as reproduced in document A/CN.9/WG.VI/WP.52/Add.5. The Working Group may also wish to note that, for reasons of economy, recommendations 1-3 are not inserted here at this stage but will be inserted in the final text.*]

II. Access to the registry services

A. General remarks

1. Public access

56. The *Secured Transactions Guide* recommends that any person may register a notice of a (potentially existing) security right or search the publicly available registry record (not the archives; see *Secured Transactions Guide*, chap. IV, paras. 25-30 and rec. 54, subparas. (f) and (g)). This approach is in line with one of the key objectives of the *Secured Transactions Guide* which is to enhance certainty and transparency by providing for registration of a notice of a security right in a general security rights registry (see *Secured Transactions Guide*, chap. IV, para. 25, and rec. 1, subpara. (f)). Because of the importance of the principle of public access to the registry services, it should be restated in the regulation (see draft Registry Guide, rec. 5).

57. Public access is facilitated to the extent that users with access to computers and the Internet are able to submit notices and conduct searches electronically without the need for the assistance or intervention of registry personnel. As already discussed (see A/CN.9/WG.VI/WP.52/Add.1, paras. 48-55), registration of paper forms is associated with cost, delay and potential for error and liability for the registry. In any case, even if the registry system permits or requires the use of paper forms, the registry record should be computerized and made accessible remotely by the Internet. In addition, public access to the registry's registration services is facilitated to the extent that the registry does not establish unnecessary conditions to access by registrants (see A/CN.9/WG.VI/WP.52/Add.2, paras. 1 and 2), nor requires verification of the identity of a registrant, evidence of existence of authorization for registration or conduct any scrutiny of the content of the notice (see A/CN.9/WG.VI/WP.52/Add.2, paras. 3-7).

58. Citing privacy concerns, some States require searchers to indicate that they have justifiable reasons for conducting a search. To facilitate access to the registry's search services, the *Secured Transactions Guide* recommends that the registry may not require a searcher to give reasons for the search (see *Secured Transactions Guide*, rec. 54, subpara. (g)). The privacy of the grantor is sufficiently protected by a regime that requires only a limited amount of information about the relevant security agreement to be included in a notice. The privacy of the secured creditor is sufficiently protected by the registry not allowing third-party searches according to the secured creditor identifier and by permitting the secured creditor to enter the name and address of a representative as the secured creditor in the notice, as well as by the limited amount of transaction information required. In addition, requiring

searchers to give reasons for a search would undermine the efficiency and functionality of the search process, as the registry would have to scrutinize the reasons given and determine that they are sufficient to justify a search. Moreover, depending on the exact reasons required, open access to information in the registry as part of an efficient and transparent market may be impeded, at least to the extent that some parties dealing with the grantor may not have the information available to other parties.

2. Operating days and hours of the registry

59. The approach to the operating days and hours of the registry recommended in the *Secured Transactions Guide* depends on the extent to which the registry is designed to permit direct electronic registration and searching by users or requires their in-person attendance at a physical office of the registry. In the former case, the registry should be accessible continuously except for brief periods to undertake scheduled maintenance; in the latter case, it should operate during reliable and consistent hours compatible with the needs of the potential registry users (see *Secured Transactions Guide*, chap. IV, para, 42, and rec. 54, subpara. (1)). In view of the importance of this issue to users, it should be addressed in the regulation or in administrative guidelines published by the registry (see draft Registry Guide, rec. 5).

60. Where the registry provides services through a physical office, the minimum operating days and hours should be the usual business days and hours in the enacting State. To the extent that the registry requires or permits the registration of paper notices or the submission of paper search requests, the time for receiving the paper notices, information in which will be entered in the registry record and made available to searchers on the same business day, may be set independently from the business hours. For example, the regulation or administrative guidelines of the registry may stipulate that, while the registry office is open between 09:00 and 17:00, all forms must be received by an earlier time (e.g. 16:30) so as to ensure that the registry staff has sufficient time to enter the information on notices into the registry record or conduct the search. Alternatively, the office might receive paper notices during all business hours, but set a “cut off” time, after which information in notices received may not be entered into the registry record until the next business day.

61. The registry regulation or administrative guidelines could also enumerate in an exhaustive or indicative way the circumstances in which access to the registry services may temporarily be suspended. An exhaustive list would provide more certainty but there is a risk that it may not cover all possible circumstances. An indicative list would provide more flexibility but less certainty. Circumstances justifying a suspension of the registry services might include any event that makes it impossible or impractical to provide users with access to the registry services (for example, where the registry provides users with direct electronic access to its services, force majeure, due, for example, to fire, flood, earthquake, war, or a breakdown in Internet or network access).