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Draft Model Law on Secured Transactions

Note by the Secretariat

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Chapter I. Scope of application and general provisions

Article 1. Scope of application

1. This Law applies to security rights in movable assets.
2. With the exception of articles 66, paragraphs 1-3, to 75,* this Law applies to outright transfers of receivables [and, in such a case, references in this Law to a grantor apply to the transferor, references to a secured creditor apply to the transferee, references to a security agreement apply to the agreement for the outright of a receivable, references to a security right apply to the right of the transferee and references to an encumbered asset apply to the receivable, but references to a secured obligation do not apply to the right to payment of the price of the receivable].
3. Notwithstanding paragraph 1, this Law does not apply to security rights in:
 - (a) The right to request payment under or to receive the proceeds of an independent guarantee or letter of credit;
 - (b) Intellectual property in so far as this Law is inconsistent with [the law relating to intellectual property to be specified by the enacting State];¹
 - (c) Intermediated securities;
 - (d) Payment rights arising under or from financial contracts governed by netting agreements, except a payment right arising upon the termination of all outstanding transactions; and
 - (e) [Other types of asset that the enacting State wishes to exclude, such as those that are subject to specialized secured transactions and asset-based registration regimes under other law to the extent that that other law governs matters addressed in this Law].²
4. This Law does not apply to security rights in proceeds of encumbered assets if the proceeds are a type of asset, to which this Law does not apply, to the extent that [any other law to be specified by the enacting State] applies to security rights in those types of asset and governs the matters addressed in this Law.]
5. Nothing in this Law affects the rights and obligations of the grantor and the secured creditor under laws governing the protection of parties to transactions made for personal, family or household purposes.
6. Nothing in this Law overrides a provision of any other law that limits the creation or enforcement of a security right in, or the transferability of, specific types of asset, with the exception of a provision that limits the creation or enforcement of a security right in or the transferability of an asset on the sole ground that it is a future asset, or a part or undivided interest in an asset.

* The reference is to these articles as they appear in document A/CN.9/WG.VI/WP.65/Add.3.

¹ This provision may not be necessary if the enacting State has coordinated, or has otherwise addressed the relationship between this Law and any secured transactions provisions of its law relating to intellectual property.

² If the enacting State decides to introduce any other exception(s), they should be limited and set out in the Law in a clear and specific way.

[Note to the Working Group: The Working Group may wish to consider which of the alternative bracketed texts should be retained, the text in article 1(2) or the texts in article 2 (j), (n), (cc), (dd), (gg) and (hh), prepared pursuant to its decision (A/CN.9/865, para. 40). The Working Group may also wish to consider whether, unlike recommendation 4(d) of the UNCITRAL Legislative Guide on Secured Transactions (the “Secured Transactions Guide”) and article 4(2) of the United Nations Convention on the Assignment of Receivables in International Trade (the “Assignment Convention”) on which it is based, article 1(3)(d) should exclude not only “payment rights” but “rights” in general arising from or under such financial contracts before close-out. Alternatively, the draft Guide to Enactment could explain that: (a) security rights in any rights arising before close-out would interrupt the mutuality of obligation that is necessary to ensure that close-out netting is fully enforceable even in the event of the grantor’s insolvency; (b) if a security right in rights arising before close-out were to be created (e.g. in the case of a security right in all the assets of a grantor), the relevant financial contract should include a broad prohibition to the creation of a security right in such rights by one party without the prior written consent of the other party; and (c) the draft Model Law does not affect such a prohibition, as article 13 applies only to trade receivables and payment rights arising after close-out, and article 15 applies only to rights to payment of funds credited to a bank account (while under article 63(1), the creation of a security right does not affect the rights and obligations of the depositary institution without its consent).]

Article 2. Definitions and rules of interpretation

For the purposes of this Law:

- (a) “Acquisition secured creditor” means a secured creditor that has an acquisition security right;
- (b) “Acquisition security right” means a security right in a tangible asset, intellectual property or the rights of a licensee under a licence of intellectual property, which secures the obligation to pay any unpaid portion of the purchase price of the asset or other credit extended to enable the grantor to acquire it to the extent the credit is used for that purpose;
- (c) “Bank account” means an account maintained by [a financial institution authorized to receive deposits from the public] [an authorized deposit-taking institution] [any institution to be specified by the enacting State] to which funds may be credited or debited;
- (d) “Certificated non-intermediated securities” means non-intermediated securities represented by a certificate that:
 - (i) Provides that the person entitled to the securities is the person in possession of the certificate; or
 - (ii) Identifies the person entitled to the securities;
- (e) “Competing claimant” means a creditor of a grantor or other person with rights in an encumbered asset that may be in competition with the rights of a secured creditor in the same encumbered asset. The term includes:

- (i) Another secured creditor of the grantor that has a security right in the same encumbered asset;
- (ii) Another creditor of the grantor that has a right in the same encumbered asset [the enacting State to specify creditors that have a right in the encumbered asset under other law];
- (iii) The insolvency representative in insolvency proceedings in respect of the grantor; or
- (iv) A buyer or other transferee, lessee or licensee of the encumbered asset;
- (f) “Consumer goods” means goods primarily used or intended to be used by the grantor for personal, family or household purposes;
- (g) “Control agreement”:
 - (i) With respect to uncertificated non-intermediated securities means an agreement in writing among the issuer, the grantor and the secured creditor, according to which the issuer agrees to follow instructions from the secured creditor with respect to the securities without further consent from the grantor; and
 - (ii) With respect to rights to payment of funds credited to a bank account means an agreement in writing among the depository institution, the grantor and the secured creditor, according to which the depository institution agrees to follow instructions from the secured creditor with respect to the payment of funds credited to the bank account without further consent from the grantor;
- (h) “Debtor” means a person that owes payment or other performance of a secured obligation, whether or not that person is the grantor of the security right securing payment or other performance of that obligation, including a secondary obligor such as a guarantor of a secured obligation;
- (i) “Debtor of the receivable” means: (i) a person that owes payment of a receivable that is subject to a security right, including a guarantor or other person secondarily liable for payment of the receivable; and (ii) a transferor of a receivable;
- (j) “Encumbered asset” means: (i) a movable asset that is subject to a security right; [and (ii) a receivable that is the subject of an outright transfer;]
- (k) “Equipment” means a tangible asset other than inventory or consumer goods that is primarily used or intended to be used by the grantor in the operation of its business;
- (l) “Financial contract” means any spot, forward, future, option or swap transaction involving interest rates, commodities, currencies, equities, bonds, indices or any other financial instrument, any securities repurchase or lending transaction, and any other transaction similar to those transactions entered into in financial markets and any combination of those transactions;
- (m) “Future asset” means a movable asset, which does not exist or which the grantor does not have rights in or the power to encumber at the time the security agreement is concluded;

(n) “Grantor” means: (i) a person that creates a security right to secure either its own obligation or that of another person; [and] (ii) a buyer or other transferee, lessee, or licensee of an encumbered asset that acquires its rights subject to a security right; [and (iii) a transferor in an outright transfer of a receivable;]

(o) “Insolvency representative” means a person or body, including one appointed on an interim basis, authorized in insolvency proceedings to administer the reorganization or the liquidation of the insolvency estate;

[Note to the Working Group: The Working Group may wish to note that this term is only referred to in the definition of “competing claimant” and thus consider whether it should be retained in article 2 or rather explained in the draft Guide to Enactment. In any case, the Guide to Enactment may clarify that the term includes an insolvency representative that may be appointed to supervise, rather than only administer, the reorganization of the insolvency estate, for example, in the context of debtor-in-possession insolvency proceedings, and/or simply refer to the discussion in UNCITRAL Legislative Guide on Insolvency Law (the “Insolvency Guide”) on the supervision of the debtor by the insolvency representative and the various functions performed by the insolvency representative (see part two, chap. III, paras. 11-18 and 35). The Working Group may also wish to consider whether the term “insolvency proceedings”, which is referred to in this definition and in articles 33 (priority chapter) and 91 (conflict-of-laws chapter), and the term “insolvency estate”, which is referred in the definition of this term and the definition of the term “competing claimant”, should also be defined in article 2 or explained in the draft Guide to Enactment by reference to the definitions of those terms contained in the Secured Transactions Guide, which are based on the relevant definitions of the Insolvency Guide.]

(p) “Intangible asset” means all types of movable asset other than tangible assets;

(q) “Inventory” means tangible assets held by the grantor for sale or lease in the ordinary course of the grantor’s business, including raw and semi-processed materials (work-in-process);

(r) “Knowledge” means actual knowledge;

(s) “Mass or product” means tangible assets that are so physically associated or united with other tangible assets that they have lost their separate identity;

(t) “Money” means currency authorized as legal tender by any State;

(u) “Non-intermediated securities” means securities other than securities credited to a securities account and rights in securities resulting from the credit of securities to a securities account;

(v) “Netting agreement” means an agreement between two or more parties that provides for one or more of the following:

(i) The net settlement of payments due in the same currency on the same date whether by novation or otherwise;

(ii) Upon the insolvency or other default by a party, the termination of all outstanding transactions at their replacement or fair market values, conversion

of such sums into a single currency and netting into a single payment by one party to the other; or

(iii) The set-off of amounts calculated as set forth in subparagraph (ii) under two or more netting agreements;

(w) “Notice” means a communication in writing;

(x) “Notification of a security right in a receivable” means a notice by the grantor or the secured creditor informing the debtor of the receivable that a security right has been created in the receivable;

(y) “Possession” means the actual possession of a tangible asset by a person [directly or indirectly] or its representative, or by an independent person that acknowledges holding it for that person;

[Note to the Working Group: The Working Group may wish to note that the bracketed words have been added pursuant to its decision to address situations in which the issuer of a negotiable document held it through various persons responsible to perform parts of a multimodal transport contract (A/CN.9/865, para. 62), and consider whether they should be retained.]

(z) “Priority” means the right of a person in an encumbered asset in preference to the right of another person;

(aa) “Proceeds” means whatever is received in respect of an encumbered asset, including what is received as a result of sale or other transfer, lease, licence or collection of an encumbered asset, civil and natural fruits, insurance proceeds, claims arising from defects in, damage to or loss of an encumbered asset, and proceeds of proceeds;

(bb) “Receivable” means a right to payment of a monetary obligation, excluding a right to payment evidenced by a negotiable instrument, a right to payment of funds credited to a bank account and a right to payment under a non-intermediated security;

(cc) “Secured creditor” means: (i) a person that has a security right; [and (ii) a transferee in an outright transfer of a receivable;]

(dd) “Secured obligation” means an obligation secured by a security right. The term does not include the obligation of the transferee to pay the price in an outright transfer of a receivable;

(ee) “Securities” means:

[(i)] An obligation of an issuer or any share or similar right of participation in an issuer or in the enterprise of an issuer that:

a. Is one of a class or series, or by its terms is divisible into a class or series; [and]

b. Is of a type dealt in or traded on a recognized market, or is issued as a medium for investment [and]

(ii) The enacting State to specify any additional rights that should qualify as securities even if they do not satisfy the requirements expressed in subparagraphs (i) a. and (i) b.;

(ff) “Securities account” means an account maintained by an intermediary to which securities may be credited or debited;

(gg) “Security agreement” means[: (i)] an agreement, regardless of whether the parties have denominated it as a security agreement, between a grantor and a secured creditor that provides for the creation of a security right; [and (ii) an agreement that provides for the outright transfer of a receivable;]

(hh) “Security right” means[: (i)] a property right in a movable asset that is created by an agreement to secure payment or other performance of an obligation, regardless of whether the parties have denominated it as a security right, and regardless of the type of asset, the status of the grantor or secured creditor, or the nature of the secured obligation; [and (ii) the right of the transferee in an outright transfer of a receivable;]

(ii) “Tangible asset” means all types of tangible movable asset. Except in articles [2, subparagraphs (b), (j), (q) and (s), 11, 32, 36-40, and ...], the term includes money, negotiable instruments, negotiable documents and certificated non-intermediated securities; and

(jj) “Uncertificated non-intermediated securities” means non-intermediated securities not represented by a certificate.

Article 3. Party autonomy

1. Except for articles [4, 6, 9, 48, 49, 66, paragraph 4,* and 82-97], the provisions of this Law may be derogated from or varied by agreement.
2. An agreement referred to in paragraph 1 does not affect the rights or obligations of any person that is not a party to the agreement.

Article 4. General standards of conduct

A person must exercise its rights and perform its obligations under this Law in good faith and in a commercially reasonable manner.

Article 5. International origin and general principles

1. In the interpretation of this Law, regard is to be had to its international origin and the need to promote uniformity in its application and the observance of good faith.
2. Questions concerning matter governed by this Law which are not expressly settled in it are to be settled in conformity with the general principles on which this Law is based.

[Note to the Working Group: The Working Group may wish to note that article 5, which has been added pursuant to its decision (A/CN.9/865, para. 47), is based on article 3 of the UNCITRAL Model Law on Electronic Commerce, article 4 of the UNCITRAL Model Law on Electronic Signatures, and art. 2A of the UNCITRAL Model Law on International Commercial Arbitration.]

* The reference to articles 48, 49 and 66, paragraph 4, is a reference to those articles as they appear in document A/CN.9/WG.VI/WP.65/Add.3.

Chapter II. Creation of a security right

A. General rules

Article 6. Creation of a security right

1. A security right is created by a security agreement, provided that the grantor has rights in the asset to be encumbered or the power to encumber it.
2. A security agreement may provide for the creation of a security right in a future asset, but the security right in that asset is created only at the time when the grantor acquires rights in it or the power to encumber it.
3. Except as provided in paragraph 4, a security agreement must be [concluded in] [evidenced by]³ a writing that is signed by the grantor and:
 - (a) Identifies the secured creditor and the grantor;
 - (b) Except in the case of an agreement that provides for the outright transfer of a receivable, describes the secured obligation;
 - (c) Describes the encumbered assets as provided in article 9[; and
 - (d) Indicates the maximum monetary amount for which the security right may be enforced].⁴
4. A security agreement may be oral if the secured creditor has possession of the encumbered asset.

Article 7. Obligations that may be secured

A security right may secure any type of obligation, present or future, determined or determinable, conditional or unconditional, fixed or fluctuating.

Article 8. Assets that may be encumbered

A security right may encumber:

- (a) Any type of movable asset, including future assets;
- (b) Parts of assets and undivided rights in movable assets;
- (c) Generic categories of movable assets; and
- (d) All of a grantor's movable assets.

Article 9. Description of encumbered assets

1. The assets encumbered or to be encumbered must be described in the security agreement in a manner that reasonably allows their identification.

³ The enacting State may wish to choose the option that best fits its legal system.

⁴ The enacting State may wish to include this subparagraph in the draft Model Law if it determines that an indication of the maximum monetary amount for which the security right may be enforced would be helpful to facilitate lending from another creditor.

2. A description that indicates that the encumbered assets consist of all the grantor's movable assets, or of all the grantor's movable assets within a generic category satisfies the standard in paragraph 1.

Article 10. Right to proceeds and commingled funds

1. A security right in an encumbered asset extends to its identifiable proceeds.
2. Where proceeds in the form of funds credited to a bank account or money are commingled with other assets of the same kind:
 - (a) The security right extends to the commingled assets, notwithstanding that the proceeds have ceased to be identifiable;
 - (b) The security right in the commingled assets is limited to the value of the proceeds immediately before they were commingled; and
 - (c) If at any time after the commingling, the value of the balance credited to the bank account or of the commingled money is less than the value of the proceeds immediately before they were commingled, the obligation secured by the security right that is enforceable against the commingled assets is limited to the lowest value between the time when the proceeds were commingled and the time the security right in the proceeds is claimed.

Article 11. Tangible assets commingled in a mass or product

1. A security right in a tangible asset that is commingled in a mass of assets of the same kind or product extends to the mass or product.

Option A

2. A security right that continues in a mass or product is limited to the value of the encumbered assets immediately before they became part of the mass or product.

Option B

2. A security right that continues in a mass is limited to the same proportion of the value of the mass as the value of the encumbered assets bore to the value of the mass at the time of commingling.
 3. A security right that continues in a product is limited to the value of the encumbered assets immediately before they became part of the product.
- [3][4.] Where more than one security right continues in the same mass or product and each was a security right in a separate tangible asset at the time of commingling, the secured creditors are entitled to share in the mass or product according to the ratio that the obligation secured by each security right bears to the sum of the obligations secured by all security rights.

Article 12. Extinguishment of a security right

A security right is extinguished upon the extinguishment of all present and future secured obligations, including conditional obligations, by payment or otherwise.

B. Asset-specific rules

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

1. A security right in a receivable is effective as between the grantor and the secured creditor and as against the debtor of the receivable notwithstanding any agreement between the initial or any subsequent grantor and the debtor of the receivable or any subsequent secured creditor limiting in any way the grantor's right to create a security right.
2. Nothing in this article affects any obligation or liability of the grantor for breach of the agreement referred to in paragraph 1, but the other party to the agreement may not avoid the contract giving rise to the receivable or the security agreement on the sole ground of the breach of that agreement, or raise against the secured creditor any claim it may have as a result of such a breach against the grantor, as provided in article 58, paragraph 2.*
3. A person that is not a party to the agreement referred to in paragraph 1 is not liable for the grantor's breach of the agreement on the sole ground that it had knowledge of the agreement.
4. This article applies only to receivables:
 - (a) Arising from a contract that is a contract for the supply or lease of goods or services other than financial services, a construction contract or a contract for the sale or lease of immovable property;
 - (b) Arising from a contract for the sale, lease or licence of industrial or other intellectual property or of proprietary information;
 - (c) Representing the payment obligation for a credit card transaction; or
 - (d) Arising upon net settlement of payments due pursuant to a netting agreement involving more than two parties.

[Note to the Working Group: The Working Group may wish to consider whether the words "initial or any subsequent" in paragraph 1 should be deleted as the definition of the term "grantor" covers both an initial and a subsequent grantor-transferee. The Working Group may also wish to consider whether the word "avoid" in paragraph 2 should be replaced by the word "terminate".]

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

1. A secured creditor with a security right in a receivable or other intangible asset, or a negotiable instrument has the benefit of any personal or property right that secures or supports payment or other performance of the encumbered asset without a new act of transfer.

* The reference to article 58, paragraph 2, is a reference to that article as it appears in document A/CN.9/WG.VI/WP.65/Add.3.

2. If the right referred to in paragraph 1 is transferable only with a new act of transfer, the grantor is obliged to create a security right in it in favour of the secured creditor.

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

A security right in a right to payment of funds credited to a bank account is effective notwithstanding an agreement between the grantor and the depositary institution limiting in any way the grantor's right to create a security right.

[Note to the Working Group: The Working Group may wish to note that the draft Guide to Enactment will explain that, under article 63(1) (in document A/CN.9/WG.VI/WP.65/Add.3), the depositary institution is not obliged to pay the secured creditor or provide any information about the bank account to any third party.]

Article 16. Tangible assets covered by negotiable documents

A security right in a negotiable document extends to the tangible asset covered by the document, provided that the issuer of the document is in possession of the asset at the time the security right in the document is created.

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

A security right in a tangible asset with respect to which intellectual property is used does not extend to the intellectual property and a security right in the intellectual property does not extend to the tangible asset.

Chapter III. Effectiveness of a security right against third parties

A. General rules

Article 18. Primary methods for achieving third-party effectiveness

1. A security right in an encumbered asset is effective against third parties if a notice with respect to the security right is registered in the general security rights registry (the "Registry").
2. A security right in a tangible asset is also effective against third parties if the secured creditor has possession of the asset.

Article 19. Proceeds

1. If a security right in an asset is effective against third parties, a security right in any proceeds of that asset remains effective against third parties without any further act if the proceeds are in the form of money, receivables, negotiable instruments or rights to payment of funds credited to a bank account.
2. If a security right in an asset is effective against third parties, a security right in any type of proceeds of that asset other than the types of proceeds referred to in paragraph 1 is effective against third parties:

(a) For [a short period of time to be specified by the enacting State] days after the proceeds arise; and

(b) Thereafter, if the security right in the proceeds is made effective against third parties by one of the methods applicable to the relevant type of encumbered asset referred to in this chapter before the expiry of the time period provided in subparagraph (a).

[Note to the Working Group: The Working Group may wish to consider whether an article should be inserted in this place of the draft Model Law to implement recommendation 44 of the Secured Transactions Guide providing for the automatic third-party effectiveness of a security right in tangible assets commingled in a mass or product (for creation issues, see art. 11, and for priority issues, see art. 40).]

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

A security right that is effective against third parties remains effective against third parties despite a change in the method for achieving third-party effectiveness, provided that there is no time when the security right is not effective against third parties.

Article 21. Lapse in third-party effectiveness

If the third-party effectiveness of a security right lapses, it may be re-established, but the security right is effective against third parties only as of that time.

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

1. If a security right is effective against third parties under the law of another State and this Law becomes applicable as a result of a change in the location of the encumbered asset or the grantor, whichever determines the applicable law under the provisions of chapter VIII, the security right remains effective against third parties under this Law until the earlier of:

(a) The time when third-party effectiveness would have lapsed under the law of the other State; and

(b) [A short period of time to be specified by the enacting State] days after the change and, thereafter, only if the third-party effectiveness requirements of this Law are satisfied before the expiry of that time period.

2. If the security right remains effective against third parties under paragraph 1, the time of third-party effectiveness is the time when it was achieved under the law of the other State.

[Note to the Working Group: The Working Group may wish to consider whether a buyer or judgment creditor, who acquired a right in an encumbered asset when the security right was effective against third parties and thus acquired its right subject to the security right, would remain subordinated even after the security right ceased to be effective against third parties under subparagraph (a) or (b) of this article.]

Article 23. Acquisition security rights in consumer goods**Option A**

An acquisition security right in consumer goods is effective against third parties, other than a buyer or other transferee, upon its creation without any further step.

Option B

An acquisition security right in consumer goods [below a value to be specified by the enacting State] is effective against third parties upon its creation without any further act.

[Note to the Working Group: The Working Group may wish to consider whether the exception to the rule in option A is too broad and should thus be limited to consensual transferees and/or transferees for value.]

B. Asset-specific rules**Article 24. Rights to payment of funds credited to a bank account**

A security right in a right to payment of funds credited to a bank account may also be made effective against third parties by:

- (a) The creation of the security right in favour of the depositary institution;
- (b) The conclusion of a control agreement; or
- (c) The secured creditor becoming the account holder.

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

1. If a security right in a negotiable document is effective against third parties, the security right that extends to the asset covered by the document in accordance with article 16 is also effective against third parties.
2. During the period when a negotiable document covers an asset, a security right in the asset may also be made effective against third parties by possession of the document.
3. A security right in a negotiable document that was effective against third parties by possession of the document remains effective against third parties for [a short period of time to be specified by the enacting State] after the document has been returned to the grantor or other person for the purpose of ultimate sale or exchange, loading or unloading, or otherwise dealing with the assets covered by the document.

Article 26. Uncertificated non-intermediated securities

A security right in uncertificated non-intermediated securities may also be made effective against third parties by:

- (a) The [notation of the security right] [entry of the name of the secured creditor as the holder of the securities] in the books maintained by or on behalf of the issuer for the purpose of recording the name of the holder of the securities;⁵ or
 - (b) The conclusion of a control agreement.
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⁵ The enacting State may wish to choose the method that best suits its legal system.