United Nations A/CN.9/SR.840

General Assembly

Distr.: General
10 July 2007

Original: English

United Nations Commission on International Trade Law
Fortieth session

Summary record of the 840th meeting
Held at the Vienna International Centre, Vienna, on Wednesday, 27 June 2007, at 9.30 a.m.

Chairperson: Ms. Sabo (Chairperson of the Committee of the Whole)..... (Canada)

Contents

V.07-85520 (E)

The meeting was called to order at 9.45 a.m.

Adoption of a draft UNCITRAL Legislative Guide on Secured Transactions and possible future work (*continued*) (A/CN.9/617, 620, 631 and Add.1-11, 632 and 633)

XII: Acquisition financing rights (continued) (A/CN.9/631 and Add.9)

B. Non-unitary approach to acquisition financing rights (continued) (recommendations 184 to 201)

1. **The Chairperson** noted that some delegations had voiced concern that the absence of references to property-based concepts made the recommendations on the non-unitary approach to acquisition financing rights less accessible to the reader. She invited members to suggest possible courses of action to resolve the matter promptly and effectively.

2. **Mr. Riffard** (France) said that it had emerged from informal consultations that greater clarity could be achieved through redrafting. However, it would first be necessary to decide whether it was wise to use the concept of priority in the non-unitary approach.

3. Consensus had been achieved on the purpose of acquisition financing rights, namely to confer preferential status on the acquisition financier. In the context of the unitary approach, which treated all secured creditors equally, the objective of conferring such status could be achieved only by proposing that the lawmaker should accord super-priority to acquisition financiers. In the context of the non-unitary approach, preferential status resulted simply from the acquisition financier's retention of title to the asset. An acquisition financier in a non-unitary system must thus acquire a security right giving it a right to the title either through a retention-of-title clause or indirectly through the assignment of a receivable with a security right attached.

4. The sole remaining stumbling-block was whether, in the context of the non-unitary system, a secured lender that financed the acquisition of tangible property should be accorded preferential status. If so, it would be necessary to introduce the concept of priority into the non-unitary approach. There would then be two categories of acquisition financiers with preferential status, those who derived that status from their retention of title and those who had been given super-priority, and it would be necessary to determine how conflicts between them should be settled.

5. He proposed that the recommendations should be redrafted without changing the substance as soon as the Committee reached agreement in principle.

6. **Mr. Voulgaris** (Greece) said that another pending issue was the formalities to be completed in order to establish third-party effectiveness in the case of retention-of-title transactions, which should be registered in the same way as other security rights. The principle was laid down in recommendation 186 in the unitary approach section.

7. **Mr. Macdonald** (Canada) said that some of the language used in the draft Guide might lack transparency for first-time users, who might be confused to find that rules apparently governing security rights were equally applicable to retention-of-title rights. The recommendations should therefore be elaborated to make it clear how they were to be applied in an ownership regime and in a security rights regime and how the principle of functional equivalence was to be upheld. He therefore strongly supported the proposal made by the representative of France.

8. **Mr. Burman** (United States of America) said that he also supported that proposal.

9. **Mr. Voulgaris** (Greece) expressed support for the proposal provided that the substance of recommendation 189 (a) and (b) was retained.

10. **The Chairperson** said she took it that the Committee wished to redraft the recommendations concerning acquisition financing rights in the non-unitary approach section.

11. *It was so decided.*

Recommendation 191 (continued)

12. **Mr. Macdonald** (Canada) said that the idea expressed in the second paragraph of the note to the Commission following recommendation 191 should be reflected in the non-unitary approach section of the draft Guide so that readers understood how the principle of equivalence should be applied in practice.

13. **Mr. Burman** (United States of America) said that it was unclear why a third-party acquisition financier should be limited to acquiring an acquisition security right or an acquisition financing right through assignment. One of the benefits of creating the notion of a third-party acquisition financier was to give buyers a competitive choice, i.e. either to borrow money from a bank or obtain credit from the seller. Restricting the third-party financier's possibilities in the aforementioned manner precluded competition and placed sellers in a position where they could request a

share in the interest chargeable by the bank, because they would be able to withhold the assignment.

14. Furthermore, the scope of application of recommendation 191 would be relatively limited, since it would involve concurrent acquisition financing from a third party and a seller. Moreover, such a rule, while acceptable, would tend to favour the seller.

15. **Mr. Macdonald** (Canada) said that the second paragraph of the note to the Commission clearly stated that lenders were free to acquire either an acquisition security right or an acquisition financing right, the latter through an assignment from the seller. Lenders could thus avail themselves of the full range of options and he had not intended to suggest that they should be barred from acquiring acquisition security rights.

16. **Mr. Kohn** (Observer for the Commercial Finance Association) cautioned the Committee against deleting subparagraph (b) of the "Purpose" section, as suggested in the third paragraph of the note to the Commission. The subparagraph stated the key concept of functional equivalence and should be retained irrespective of any redrafting of recommendation 191.

17. **The Chairperson** said she took it that the Committee was satisfied with the policy expressed in recommendation 191 and supported the inclusion of the second paragraph of the note to the Commission, on the understanding that lenders would have the full range of options at their disposal.

18. *It was so decided*.

19. *Recommendation 191 was adopted on that understanding*.

Recommendation 192

20. **Mr. Kemper** (Germany) said that the additional requirements imposed by recommendation 192 on an acquisition financier, particularly a retention-of-title seller, were unjustified if the goods constituted inventory for the buyer. Such cases should be dealt with according to the rule set out in recommendation 189 for tangible property other than inventory or consumer goods.

21. **The Chairperson** said that paragraphs 114 to 118 of the commentary to chapter XII might require further elaboration since they failed to explain adequately the reasoning behind the different treatment accorded to tangible property and inventory.

22. **Mr. Schneider** (Germany) asked whether the term "inventory" was to be defined from the seller's or the buyer's perspective. Tangibles might constitute inventory for the seller but not for the buyer, or vice versa. The delegation of the United States might be able to provide some enlightenment on that point, since the recommendation appeared to be based on article 9 of the United States Uniform Commercial Code. He would also appreciate an explanation of how a seller was supposed to establish whether any earlier-registered non-acquisition security right existed in the buyer's country. The seller would have to inspect the country's registry, probably with the assistance of a lawyer, and then notify the holder of the earlier-registered acquisition security right, all of which would delay delivery of the goods.

23. **Mr. Cohen** (United States of America) noted that the term "inventory" was used extensively throughout the draft Guide. Recommendation 87 in chapter VII on priorities, for example, stated that a buyer of inventory in the ordinary course of the seller's business took free of the security right. He agreed with the representative of Germany that problems might arise where goods constituted inventory in the hands of the seller but equipment in the hands of the buyer. In the case of recommendation 87, the commentary and the terminology guide in document A/CN.9/631/Add.1 made it clear how the term inventory was to be interpreted. The same approach could be adopted in the case of recommendation 192.

24. Problems pertaining to international sales of goods, international acquisition finance and conflict-of-law situations also arose throughout the draft Guide. Those difficulties should not prevent the Commission from recommending rules that were appropriate for domestic transactions, and as more and more States followed those rules, the problems arising in an international context should diminish.

25. **Mr. Kemper** (Germany) said that the draft Guide was intended for States wishing to enact legislation that covered both domestic trade and international trade transactions involving, for example, imports of goods under retention-of-title arrangements. Such legislation would also spell out the requirements for obtaining priority through registration. However, he considered that the policy choice made in recommendation 192 was unsound. As currently worded, it favoured financial institutions to the detriment of retention-of-title sellers. The latter needed a reasonable and uncomplicated registration system to ensure speedy trade transactions.

26. **Mr. Mitrović** (Serbia) said that if the recommendations in the draft Guide were modelled on existing national legislation, as in the example cited by Germany, the commentary might usefully include a cross-reference to that legislation.

27. **Mr. Sigman** (United States of America) said that the draft Guide was not based on policy choices but on economic efficiency. It did not focus on exporters or importers but on the buyer as debtor. For instance, where a buyer purchased machinery from suppliers in six different countries, the six sellers that exported their goods would be competing in the event of the buyer's insolvency with the buyer's other creditors. The draft Guide, by advocating a modern efficient electronic registry, should speed up trade dramatically because the seller would be able to access information about the registry in the buyer's country in order to determine where it must register and who prior registrants were.

28. **Mr. Kemper** (Germany) said that by policy choice he had meant the choice of a legislator who had to balance policies and interests. It was not merely a technical issue.

29. **Mr. Bazinas** (Secretariat) said he gathered that the main objection to recommendation 192 was that it seemed to make a policy choice in favour of general financiers to the detriment of sellers of goods on credit with retention of title because of the registration and notification requirements. However, in recommendation 191 sellers were accorded priority over general financiers, a situation that reflected to some extent the current practice in countries where retention of title was the main non-possessory security interest.

30. Although registration would be required, the burden on the supplier would depend on the registry concerned. If it was well organized, registration could be speedy and inexpensive and notification could be provided for all transactions likely to take place over a period of years.

31. With regard to international trade, sellers that sold goods subject to retention of title to buyers in countries where retention-of-title rights were currently not recognized would be comforted to know that, once legislation modelled on the draft Guide had been enacted in the country of destination of the goods, the retention-of-title seller would have a security right and would be recognized in the event of insolvency provided that the necessary steps for third-party effectiveness had been taken.

32. **Mr. Schneider** (Germany) said that the first important issue to address was how to define inventory. He welcomed the implication in an earlier statement by a representative of the United States that inventory should be defined from the point of view of the seller and not of the buyer since inventory could be equipment in the hands of the buyer. He proposed that the commentary should reflect such a definition. While he understood why notification should be provided to an inventory financier, he saw no reason why a financier of equipment should expect to receive notification.

33. Under recommendation 192, while the seller could retain ownership, such retention was being made unnecessarily difficult and fast delivery was being impeded by the registration and notification requirements. While his delegation had come to accept the need for registration, it still saw no need for notification.

34. **Mr. Kemper** (Germany) said that the draft Guide was becoming increasingly sophisticated and lengthy. He therefore proposed merging recommendations 189 and 192 so that one rule along the lines of recommendation 189 would apply to both inventory and tangible property other than inventory.

35. **Mr. Kohn** (Observer for the Commercial Finance Association) said that one of the virtues of the non-unitary approach section was that it protected all the parties and provided a simple way for the seller of goods to acquire super-priority. Sellers already had to understand import and export laws, to make credit decisions regarding buyers and to perform other due diligence activities when making a sale, especially to a buyer in another country. While it was true that additional registration and notification were required under the non-unitary approach, they were essentially simple administrative acts that would not slow down the process. Another virtue of the approach was that existing inventory financiers would be protected, since they would be notified in cases where they were financing inventory subject to a prior super-priority claim. Although the terminology section of the draft Guide defined inventory in terms of property held in the ordinary course of the grantor's business, it should be a simple matter for the seller to determine the facts as part of its due diligence when making a decision to sell goods to a particular buyer.

36. **The Chairperson** noted the concerns expressed by the representatives of Germany regarding recommendation 192 and suggested that its proposal should be reflected in the commentary so that legislators were at least aware of it.

37. **Mr. Kemper** (Germany) said that a legislative guide was normally less stringent than a model law and he felt that the draft Guide should offer more options to legislators. He therefore proposed presenting two options with respect to the current issue: the first option would be to maintain differential treatment for inventory and tangible property other than inventory,

along the lines of recommendations 189 and 192; the second option would be to treat both in the same way, along the lines of recommendation 189. In the latter case, recommendation 192 would be deleted and the commentary would explain the choices proposed in recommendation 189. He added that his proposal also applied to the unitary approach section.

The meeting was suspended at 11.15 a.m. and resumed at 11.45 a.m.

38. **Mr. Ghia** (Italy) expressed support for the proposed optional approach since it offered more flexibility.

39. **Ms. McCreath** (United Kingdom) said that, as far as she was aware, the electronic registration system mentioned by a representative of the United States was not yet available throughout Europe and was unlikely to be available to speed up registration for some time.

40. She expressed support for the flexible option proposed by the representative of Germany.

41. **Ms. Kaller** (Austria), **Mr. Bellenger** (France), **Ms. Kolibabska** (Poland), **Mr. Voulgaris** (Greece) and **Mr. Brink** (Observer for Europafactoring) also expressed support for the proposal.

42. **Mr. Smith** (United States of America) said that he wished to defer a decision on the proposal until all the recommendations in the non-unitary section had been discussed, since the proposal needed to be considered in the light of the entire chapter.

43. **Mr. Patch** (Australia) said that the Commission needed to show leadership to jurisdictions that were contemplating implementing the draft Guide and should therefore leave no doubt or ambiguity as to the preferred course of action. Thus, while the draft Guide should express a view, the commentary could forcefully put forward the alternatives.

44. **Mr. Umarji** (India) said that under normal circumstances, even without registration, disclosure by the grantor was required in a retention-of-title transaction where third-party rights were being created. The registration requirement would merely serve as an additional guarantee.

45. **Mr. Kohn** (Observer for the Commercial Finance Association) drew attention to the economic consequences of any decision to move from the current balanced approach that protected all parties to an approach that favoured the seller to the detriment of the inventory financier. Should such a decision be taken, it would be important for the commentary to explain the economic consequences, which would include a widespread contraction of credit.

46. **Mr. Kemper** (Germany) said that if the proposed option was adopted, the commentary would take such consequences into account. However, it would not state that the option to merge the two recommendations into recommendation 189 favoured the seller and that the other option represented a balanced approach.

47. **The Chairperson** agreed that the commentary should instruct the legislator to consider the economic consequences arising from either option and that it should also address considerations pertaining to the efficiency of the registry. While she had noted the request by the representative of the United States to defer a decision, she gathered from the strong support expressed by a number of speakers that the Committee wished to offer an alternative approach to recommendations 189 and 192 in both the unitary and the non-unitary sections. Under that approach, a new recommendation along the lines of recommendation 189 would address the priority position applicable to an acquisition security right or an acquisition financing right in tangible property.

48. *It was so decided.*

Recommendation 193

49. *Recommendation 193 was adopted.*

Recommendation 194

50. **Ms. Stanivuković** (Serbia) noted that in recommendation 194 the word “right” had been omitted after the word “financing” in the fourth line of the English version. Moreover, recommendation 194 (a) was confusing because it seemed to refer to a judgement obtained after a security right was created but before it was made effective against third parties.

51. **The Chairperson** said she took it that the Committee wished to clarify the wording of the recommendation.

52. *It was so decided.*

53. *Recommendation 194 was adopted on that understanding.*

Recommendations 195 to 197

54. *Recommendations 195 to 197 were adopted.*

Recommendations 198 and 199

55. **Mr. Smith** (United States of America) asked whether the alternative approach adopted to recommendations 189 and 192 had implications for recommendations 198 and 199, which dealt, respectively, with proceeds of tangible property other

than inventory or consumer goods and proceeds of inventory.

56. **Mr. Kohn** (Observer for the Commercial Finance Association) said that the representative of the United States had raised a pertinent issue, since the Committee's decision regarding recommendations 189 and 192 would, in his view, reduce the credit provided by inventory financiers. He cautioned against taking a further decision that would have an impact on the credit available from receivables financiers.

57. **Mr. Schneider** (Germany) said that if the second option – involving the merger of recommendations 189 and 192 – was adopted, recommendation 199 would become irrelevant and should be deleted.

58. **Mr. Bazinas** (Secretariat) said that, although many legal systems followed the approach set out in the second option with regard to goods that were subject to retention of title, very few extended priority to the proceeds of goods. Moreover, in some of the latter jurisdictions priority was lost if the proceeds were commingled and no longer identifiable.

59. **Mr. Smith** (United States of America) said that, in his view, recommendation 199 set forth a strong policy of encouraging receivables financing arising from the sale of inventory, because receivables financiers would not have to check the registry constantly. Whatever the fate of recommendations 189 and 192, recommendation 199 should stand on its own as the sole recommendation for dealing with super-priority on proceeds relating to sales of inventory.

60. **Mr. Weise** (Observer for the American Bar Association) said that the Committee's previous decision on whether notice should be given to the inventory-secured lender, which related to the convenience of the seller, had no bearing on the present issue, which related to the financing of the buyer's receivables. If recommendations 189 and 192 were merged, there was nothing to prevent recommendation 198 from being deleted and recommendation 199 becoming the general rule, although he would not necessarily advocate such an approach.

61. **Mr. Schneider** (Germany) said that he had been hesitant about the notification requirement from the outset and the problem would be compounded if it were extended to recommendation 199. Assuming that the second option was adopted, it would be preferable to retain recommendation 198 and delete recommendation 199. The Secretariat had rightly noted that different jurisdictions had different rules regarding proceeds, but proceeds were in all cases substitutes for goods delivered and retention of title should therefore continue.

62. **Mr. Kohn** (Observer for the Commercial Finance Association) said that the notion of extended retention of title, as reflected in recommendation 198, existed, as far as he knew, in only one jurisdiction. It should not therefore be proposed as an option in the draft Guide without very serious consideration. The Working Group had drafted recommendation 199 after lengthy deliberation to provide balance and to maximize the amount of credit available by encouraging both receivables finance and inventory finance. Adoption of recommendation 198, by contrast, would discourage receivables finance. Even presenting it as an option would send out the wrong message, since the purpose of the draft Guide was to promote credit by encouraging certainty for lenders. Recommendation 199 provided that kind of certainty for both acquisition and receivables financiers.

63. **Mr. Smith** (United States of America) concurred. With regard to the question of whether notification was required for proceeds, he had understood that, under the alternative approach, the seller would have obtained priority as to the goods and would be given a grace period for registration. If super-priority extended to the proceeds, however, as envisaged under recommendation 198, the draft Guide's encouragement of receivables financing would be seriously undermined and the seller's rights would exceed those existing in most jurisdictions, in which the seller's retention-of-title rights did not extend to proceeds. The deletion of recommendation 199 would seriously undermine the balance achieved by the compromise agreement reached earlier in the meeting.

64. **Mr. Wezenbeek** (Observer for the European Union) said that it was clear from discussions among member States of the European Union that the observer for the Commercial Finance Association had been wrong to imply that Germany was the only country that wished to retain the provision contained in recommendation 198. On the contrary, the provision had relatively wide support and should be accommodated in the draft Guide. He added that he was not fully convinced that registration was the ideal system.

65. **Mr. Burman** (United States of America) expressed concern that issues previously resolved by the Working Group and the Commission were being raised again at every meeting. If there was a substantial level of support for a given change, his delegation would accept it. In the case of recommendations 189 and 192, for instance, although it had doubted the

strength of support for a change of policy, it had raised no objection in a spirit of compromise. However, it would strongly oppose the continued reconsideration of points on which agreement had already been reached.

66. **Mr. Kemper** (Germany) said that he had no specific proposal to amend either recommendation 198 or recommendation 199. He simply wished to draw attention to the implications, especially for recommendation 198 which echoed the wording of recommendation 189, of the adoption of the second option.

67. **The Chairperson** said that a distinction should be made between drafting changes and policy changes. The decision on the two options would entail drafting changes to recommendations 198 and 199.

68. **Mr. Bazinas** (Secretariat) assured the Committee that recommendations 198 and 199 would be reformulated to take into account the changes that had been agreed.

The meeting rose at 12.30 p.m.