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Draft Security Rights Registry Guide

Note by the Secretariat

Addendum

Contents

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IV. Rules applicable to the registration and search process (*continued*)

F. Effective time of registration

1. Owing to the role that the effective time of registration plays in determining the priority of a security right, it is essential that a date and time of registration be assigned to each notice of a security right. However, if the registry system permits the submission of notices in paper form, it will take time for the information set forth in the notice to be transposed by registry staff into the registry record. This raises the question of whether the effective date and time of registration should be assigned as soon as the notice in paper form is physically received by the registry or only after the information set forth in the notice is entered by registry staff into the registry record so as to be available to searchers of the registry record.

2. If the former approach is followed, there will be a time lag between the effective time of registration and the time when the information will become available to searchers of the registry record. This time lag would create a priority risk for searchers as their rights would be subordinate to security rights, notice of which was registered even though it was yet not available to searchers (assuming that the registry will always process the notices in the order they were received). In some legal systems, to deal with this risk, search results are assigned a "currency date" indicating that the search result is designed to disclose the state of registrations in the registry record only as of the currency date and time (for example, a day before the search) and not as of the real time of the search. Under this approach, a prospective secured creditor, after registering its security right, would then have to conduct a second search to make sure no intervening security rights have been registered before being confident in advancing funds. Prospective buyers and other third parties would similarly need to conduct a subsequent search before parting with value or otherwise acting in reliance on the registry record.

3. Accordingly, the better approach is for the registry system to assign the effective time of registration as of the time when the registration information has been successfully entered into the registry record so as to be available to searchers of the registry record. This is the approach recommended in the *Guide* (see recommendation 70). In States in which information in notices is entered into a computerized registry record (whether directly by the registrant or by the registry staff entering information submitted by the registrant in paper form), the registry software should be programmed to ensure this result. Although highly unlikely, notices may be submitted by competing secured creditors against the same grantor at the same date and time. To address the resulting problem of date and time of third-party effectiveness and priority, the registry system may be designed to assign sequential numbers to each notice that may be part of the registration number or be assigned in addition to the registration number.

4. The approach mentioned in the preceding paragraph does not eliminate the time lag problem but simply shifts responsibility to the registrant that must verify that the information on the notice in paper form has been entered into the registry record and is searchable. Accordingly, the registry system should be designed to enable registrants to themselves enter the information into the publicly available

registry record using any computer facilities, whether their own, those of a service provider or those located at a branch of the registry (see further the discussion on access to the registry record in chapter V below). Even in such cases, there could be a nominal time lag between the time the information was entered into the registry record and the time such information become available to searchers. Nonetheless, this approach would give secured creditors some control over the timing and efficiency with which their registrations would become effective since technological advances should virtually eliminate any time lag between the time of submission of a notice and the point time at which information entered into the registry record become available to searchers.

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 10.*]

G. Amendment of registration

1. General

5. Information entered in the registry record may need to be changed to reflect a change in the relationship between the secured creditor and the grantor. This is typically done by way of an amendment that indicates the changes to the information contained in the registry record (with the exception of errors made by the registry in entering the information in the registry record, once a notice is registered there is no means to edit a notice and all changes must be in the form of a subsequent amendment notice; see recommendation 72). An amendment may be necessary, for example, in order to add, change or delete information in the registry record or to renew the duration of the effectiveness of a notice.

6. Normally, an amendment is not effected by deleting the currently registered information and replacing it with the new information. Instead, an amendment is added to the initial registration information so that the searcher is able to find and examine both the originally registered information as well as the information subsequently registered. Neither registrants nor registrars are able to replace any information from the registry record, and registry systems should be designed accordingly.

7. To effect an amendment a registrant must provide in the appropriate field in the amendment notice certain information (for example, the registration number of the notice to which the amendment relates, the purpose of the amendment, the new information and the identifier of the secured creditor authorizing the amendment). Same as with the information in the initial notice, the information in an amendment notice submitted by the registrant is not subject to verification or substantive change by those administering the registry, as the registry merely serves as a repository of information received by it (and the legal effect of that information is determined by the substantive rules of the secured transactions regime).

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 26.*]

2. Change in grantor identifier

8. A change in the identifier of the grantor indicated in the registered notice (for example, as a result of a subsequent name change) may undermine the publicity function of registration from the perspective of third parties that deal with the grantor after the identifier has changed, as a search of the registry under the new identifier may not reveal the initially registered notice. After all, the grantor's identifier is the principal indexing and search criterion and, at least in the case of a new registration after the name change, a search using the grantor's new name will not disclose a security right registered against the old name. It should be noted that in a registry system that uses identification numbers as the grantor identifier in lieu of the name, it is less likely that similar issues will arise because the identification number is typically permanent and not subject to change.

9. Accordingly, the rules on registration should enable the secured creditor to enter the new grantor identifier with an amendment notice. While failure to submit an amendment should not make the security right generally or retroactively ineffective against third parties, third parties that deal with the grantor after the change in its identifier and before the amendment notice is registered should be protected. Accordingly, the applicable rules should provide that, if the secured creditor does not register the amendment notice within a short "grace period" (for example, 15 days) after the identifier has changed, its security right would be ineffective against buyers, lessees, licensees and other secured creditors that deal with the encumbered asset after the change in the grantor identifier and before the amendment is registered. This is the approach recommended in the *Guide* (see recommendation 61). The rules should specify when the grace period begins to run, whether it is the date of change or when the secured creditor acquired actual knowledge of the change. Guidance should also be provided on what constitutes a change of identifier in the context, in particular, of corporate amalgamations and the effect of not making an amendment in these circumstances.

[*Note to the Working Group: The Working Group may wish to consider whether text should be added to article 26 of the draft model regulations to address an amendment for the purpose of indicating a change in the grantor's identifier.*]

3. Transfer of an encumbered asset

10. When the grantor transfers, leases or licences an encumbered asset, the security right will generally follow the asset into the hands of the transferee (see recommendation 79). In such a case, a search of the registry according to the transferee's, lessee's or licensee's identifier will not disclose a security right registered against the identifier of the grantor (the transferor, lessor or licensor). Accordingly, to protect third parties that deal with the encumbered asset in the hands of the transferee, the registry system should enable the secured creditor to submit an amendment notice (or a new notice) to record the identifier and address of the transferee, lessee or licensee as the new grantor.

11. The *Guide* recommends that the secured transactions law should address the impact of a transfer of an encumbered asset on the effectiveness of registration (see recommendation 62). Thus, the secured transactions law should address whether and to what extent such an amendment is required to preserve the effectiveness of the security right against intervening claimants. Some States adopt

a rule equivalent to that applicable to a change in the identifier of the grantor (see recommendation 61, and paras. 8 and 9 above). Under this approach, failure to amend the registration to disclose the identifier of the transferee does not make the security right ineffective against third parties generally. However, if the secured creditor does not register the amendment within a short "grace period" (for example, 15 days) after the transfer, its security right is ineffective against buyers, lessees, licensees and other secured creditors that deal with the encumbered asset after the transfer and before the amendment is registered. Other States adopt a similar approach subject to the important caveat that the grace period given to the secured creditor to register the amendment begins to run only after the secured creditor acquires actual knowledge of the transfer. In still other States, such an amendment is purely optional and failure to amend does not affect the third-party effectiveness or priority of the security right (see the *Guide*, chap. IV, paras. 78-80).

4. Subordination of priority

12. Under the law recommended in the *Guide*, a competing claimant with priority may at any time subordinate its priority unilaterally or by agreement in favour of any other existing or future competing claimant (see recommendation 94). There is no requirement that the subordinating secured creditor or the beneficiary of the subordination amend the registered notice to reflect this subordination. However, in some cases, a subordinating secured creditor or the beneficiary of the subordination may wish to amend the registry record to reflect the order of priority between them (and, if subordination refers only to certain assets, the relevant assets). In such case, either the subordinating secured creditor or the beneficiary of the subordination with the consent of the subordinating secured creditor could register an amendment notice provided that the security right of the subordinating secured creditor had been made effective against third parties by registration. Accordingly, the registry should be designed so as to accommodate an amendment of the notice to reflect such subordination. In any case, registration of subordination is not necessary, as it affects only the rights of the subordinating secured creditor and the beneficiary of the subordination and it could increase the cost of the registry system to the extent the relevant functions need to be built into the system and amendment forms designed.

5. Assignment of the secured obligation and transfer of the security right

13. A secured creditor may assign the secured obligation. As in most legal systems, the *Guide* recommends that, as an accessory right, the security right follows the secured obligation, with the result that the assignee of the obligation in effect will be the new secured creditor (see recommendations 25 and 48). In the event of an assignment, the original secured creditor will usually not wish to have to continue to deal with requests for information from searchers and the new secured creditor will wish to ensure that it receives any notifications or other communications relating to its security right.

14. Consequently, the original secured creditor (assignor) or the new secured creditor (assignee) with the consent of the original secured creditor should be permitted to update or amend the secured creditor information in the registry record to reflect the identifier and address of the new secured creditor. However, under the approach recommended in the *Guide*, an amendment should not be required in the

sense of it being necessary to preserve the effectiveness of the registration (see recommendation 75). As the identifier of the secured creditor is not an indexing and search criterion, searchers will not be materially misled by the change in the identity of the secured creditor. Nonetheless, if the new secured creditor fails to register the amendment, the original secured creditor will retain the power to alter the record by submitting an effective amendment notice (see the *Guide*, chap. IV, para. 111) In any case, the registry system should be designed so as a search result will show the information of both the original and the new secured creditor, if any.

15. Another issue relevant to the assignment of the secured obligation is the duty of the secured creditor to disclose the identity of the assignee on request. If a notice about the assignment of the secured obligation is registered, under the law recommended in the *Guide*, the registrant is obligated to forward a copy of that notice to the grantor (see recommendation 55, subpara. (c)). However, whether such a notice is registered or not, the secured obligation has an obligation to disclose the assignment and the identity of the assignee to the grantor upon request.

6. Addition of newly encumbered assets

16. After the conclusion of the original security agreement, the grantor may agree to grant a security right in additional assets not already described in the registered notice. In such circumstances, secured transactions law and the registration rules should enable the secured creditor to either amend the initially registered notice so as to add the description of the newly encumbered assets or to register a new notice with respect to the new assets (the only difference between the two options would be that the effectiveness of the amendment notice would expire with the original notice, while in the second case the two notices would have different expiration dates). In either case, the amendment notice or the new notice becomes effective as of the time of registration of the amendment notice or the new notice (see recommendation 70). The reason for this approach is that a search of the registry record by third parties prior to registration of the amendment notice or the new notice would not disclose that a security right has been granted in the newly encumbered assets.

[*Note to the Working Group: The Working Group may wish to consider whether text should be added to the commentary to discuss amendments that purport to delete encumbered assets or grantors (see article 26, para. 6, of the draft model regulations)*.]

7. Extension of the duration of a registration

17. After a registration is made and before its duration expires, a registrant may need to extend its duration. The rules applicable to registration should confirm that the duration of an existing registration may be extended by way of amendment at any point in time before the expiry of the term of the registration (see recommendation 69). If a new registration were instead required, this requirement would undermine the secured creditor's original priority status and the continuity of the effectiveness of its security right against third parties.

18. As already discussed (see A/CN.9/WG.VI/WP.48/Add.1, paras. 55-58), there are several approaches that States can take with respect to the duration of a registration (recommendation 69). In States where the duration of the registration is

established by law, the extension should be an additional period equal to the statutory duration. In States that permit the registrant to self-select the duration of the registration, the registrant should also be permitted to select the duration of the extension period, possibly subject to any applicable maximum limit. Under this approach, a registrant who, for example, selected a five year term for the initial registration should be allowed to select three years for the duration of the extension. In States that do not set any limit to the duration of the registration, there would be no need for an extension and a registration would continue to be effective until it was cancelled.

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 11*.]

8. Correction of erroneous lapse or cancellation

19. In the event that a secured creditor fails to extend the duration of a registration in a timely fashion or inadvertently registers a cancellation, the secured creditor may register a new notice of its security right, re-establishing third-party effectiveness. However, under the law recommended in the *Guide*, the third-party effectiveness and priority status of the security right dates only from the time of the new registration (see recommendation 47). The secured creditor will suffer a loss of priority as against all competing claimants, including those whom it had priority, under the first-to-register rule, prior to the lapse or cancellation (see recommendation 96).

20. Some States adopt a more lenient approach. The secured creditor is given a short grace period after the lapse or cancellation to revive its registration so as to restore the third-party effectiveness and priority status of its security rights as of the date of the initial registration. However, even in States that adopt this approach, the security right is ineffective against or subordinate to competing claimants that acquired rights in the encumbered assets or advanced funds to the grantor after the lapse or cancellation and before the new registration.

9. Global amendment of secured creditor information in multiple notices

21. The registry system may be designed so as to permit the retrieval of information by the registry staff according to the identifier of the secured creditor. This feature of the registry system would enable registry staff to efficiently amend the information of the secured creditor in all or multiple notices associated with that secured creditor, at the request of the person identified in the registration as the secured creditor, through a single global amendment. A single global amendment would be particularly useful in certain case such as a merger or a change of the name of the secured creditor. Such a search could be made only by registry staff, that is, not by searchers, as the name of the secured creditor would not be a search criterion (see paras. 34-37 below).

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 27*.]

H. Cancellation and amendment of notice

1. Mandatory cancellation or amendment

22. A notice may not reflect, or may no longer reflect, an existing or contemplated financing relationship between the secured creditor and the grantor identified in the registration. This may happen because, after the registration, the negotiations between the parties broke down or because the financing relationship represented by the registration came to an end. In such a case, the continued presence of the information on the records of the registry will limit the ability of the person identified as grantor to sell or create a new security right in the assets described in the registration. This is due to the fact that a prospective buyer or secured creditor will be reluctant to enter into any dealings with the person identified as the grantor unless and until the existing notice is cancelled.

23. Ordinarily, the person identified as the secured creditor in a registration will be willing to register a cancellation notice at the request of the person identified as the grantor if it does not have or does not reasonably expect to acquire a security right in the grantor's assets (see recommendation 72, subpara. (a)). However, in the event that cooperation is not forthcoming, a speedy and inexpensive judicial or administrative procedure should be established to enable the grantor to seek cancellation of the notice. This is the approach recommended in the *Guide* (see recommendation 72, subpara. (b)).

24. Similar issues arise when a registration contains inaccurate information that may be prejudicial to the ability of the person identified as the grantor to deal with its assets in favour of other secured creditors or buyers; for example, the description of the encumbered assets in the registration may include items that are not in fact covered, or are no longer covered, by any existing or contemplated security agreement and the grantor has not otherwise authorized such broad description. To address this situation, the procedure should also entitle the person identified as the grantor to seek an amendment of the notice so as to accurately reflect the actual status of the relationship between the parties (see recommendation 72, subpara. (b)). In a situation where the grantor satisfied a portion of the secured obligation that entitles the grantor to seek a release of some encumbered assets from the security right, the secured creditor should register an amendment deleting the affected encumbered assets from the registered notice. If the secured creditor fails to do so, the grantor should be entitled to have access to procedures compelling the amendment (see recommendation 72, subpara. (b)), but not a cancellation. The grantor would be entitled to seek cancellation only in the situations described above (see para. 22).

25. Accordingly, the rules on registration should entitle a person identified as the grantor in a notice (or indeed any person with a right in the assets described in a registration) to send a written notice to the person identified as the secured creditor to cancel or amend the notice, as appropriate, in any of the following circumstances: (a) a security agreement has not been concluded or was not contemplated; (b) the security right has been extinguished by full payment or otherwise; or (c) the grantor did not authorize the registration.

26. The person identified as the secured creditor should be obligated to comply with the request within a specified number of days after the secured creditor's

receipt of a written request from the person identified as the grantor, failing which the person identified as the grantor should be entitled to request a court or other administrative authority to order the cancellation or appropriate amendment of the notice unless it is found that the information in the registry record correctly reflects the existing financing relationship between the parties and was authorized by the person identified as the grantor. In either case, the rules applicable to registration should provide a specified procedure whereby the person identified as the grantor or the court or administrative authority could submit a notice of cancellation or amendment, subject to adequate protections of the secured creditor such as the right to be notified of such a procedure and present evidence.

2. Voluntary cancellation or amendment

27. A secured creditor should be in a position to amend or cancel a notice, to the extent appropriate, at any time. While such amendment or cancellation would require appropriate authorization by the grantor, cancellation of a notice, amendment due to assignment of the secured obligation, subordination or change of address of the secured creditor or its representative should not require authorization by the grantor. Typically, the grantor would authorize registration of an initial notice as well as any amendment in a single authorization document. This single authorization would not require the secured creditor to request individual authorizations for individual amendments (such as, for example, to extend the duration of the registration). This is the approach recommended in the *Guide* (see recommendations 71 and 73).

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 28*.]

3. Consequences of expiration, cancellation or amendment

28. The registry may remove information from the registry record that is accessible to the public only upon the expiry of the duration of registration or pursuant to a judicial or administrative order. However, information in notices that were cancelled may be retained in the registry record with the cancellation notice. Such notices may be removed from the registry record and archived only upon the expiry of the duration of the registration. Information removed from the record available to the public must be archived for a period of time that is long enough for that information to be retrieved when necessary, for example, to determine the order of priority among certain competing claimants at a certain point of time in the past (see recommendation 74).

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 15*.]

I. Copy of registration, amendment or cancellation notice

29. It is essential for the registrant (as well as the secured creditor) to obtain verification that information in a notice has been successfully entered into the registry record and to be informed of any changes thereafter. In this context, it should be clarified that the registrant does not necessarily have to be the secured

creditor, but may be a representative of the secured creditor. A representative may be identified in the notice instead of the secured creditor or as the registrant.

30. Under the approach recommended in the *Guide*, a registrant could obtain a record of the registration as soon as the registration information is entered into the registry record and then, the registrant is obligated to forward a copy of the notice to the grantor (see recommendation 55, subparas. (e) and (c)). However, failure of the registrant to meet this obligation results only in nominal penalties and any proven damages resulting from the failure (see recommendation 55, subpara. (c)). An electronic registry could be designed so as to provide a record of the registration in the form of an acknowledgement of a notice and to send a copy of any notice to the person identified in the notice as the grantor automatically.

31. The registry is only obligated to send promptly a copy of any changes to a registered notice to the person identified as the secured creditor in the notice (see recommendation 55, subpara. (d)). This is important to enable the secured creditor to take prompt steps to protect its position in the event that the cancellation or amendment was erroneous. Again, this may be relevant only in a paper context and not very practical if postal systems are not reliable. In an electronic registry, the secured creditor should be able to run a search to identify those registrations that have received an amendment or cancellation notice. The registry system may also be programmed to inform the person identified in the notice as the secured creditor of such changes automatically, most likely using electronic means of communication.

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 29*.]

J. Searches

1. Entitlement to search

32. Under the approach recommended in the *Guide*, to achieve its publicity objectives, the general security rights registry must be publicly accessible and a searcher should not be required to give any of the reasons for the search (see recommendation 54, subparas. (f) and (g)).

33. In the name of privacy, some States require searchers to demonstrate that they have a justifiable reason for searching the registry record. The *Guide* does not recommend this approach because the purpose of the general security rights registry is to enable third parties that are contemplating the acquisition of a right in a particular asset (by way, for example, of sale, security or judgment enforcement proceedings) or parties that otherwise require information about potential security rights in a person's assets (such as the grantor's insolvency representative) to expeditiously determine the extent to which a person's assets may already be encumbered. Requiring potential searchers to first indicate the reasons for the search and registry staff to make a decision thereon would gravely undermine the efficiency and functionality of the search process since it would interpose a complex and cumbersome adjudicative process into the search process. Transaction costs would also be increased to an unsustainable extent owing to the need to hire expert staff to administer and adjudicate search applications.

34. Privacy concerns are more effectively dealt with by requiring, for example, grantor authorization of a registration and the establishment of a procedure to enable grantors to cancel or amend unauthorized or erroneous notices quickly and inexpensively (see A/CN.9/WG.VI/WP.48/Add.1, paras. 3-9, and paras. 22-28 above).

35. However, whether the registry may request and maintain the identity of the searcher is a different matter. In some States, the registry may not disclose personal (private) information unless the registry knows the identity of the searcher. The *Guide* makes such a recommendation with respect to the identity of the registrant (see recommendation 55, subpara. (b)), but does not include a similar recommendation with respect to the identity of the searcher. In general, there should be no need for the registry to request or maintain the identity of the searcher except for the purposes of collecting search fees, if any.

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 7.*]

2. Search criteria

36. As already explained (A/CN.9/WG.VI/WP.48, paras. 65-67), under the approach recommended in the *Guide*, information in the registry record is indexed by reference to the identifier of the grantor and as such, the identifier of the grantor is the principal criterion by which such information may be searched and retrieved by searchers. However, a searcher should be entitled to rely on the accuracy of a search result only if the searcher used the correct grantor identifier in searching.

37. The approach of the *Guide* with respect to grantor-based indexing is based on two considerations. First, unlike immovable property, most categories of movable asset do not have a sufficiently unique identifier to support asset-based indexing and searching. Second, taking security in future assets and circulating pools of assets such as inventory and receivables would be administratively impractical and prohibitively expensive if the secured creditor had to continuously update its notice to add a description of each new asset acquired by the grantor. A grantor-based indexing and searching system resolves these problems by enabling the secured creditor to make its security right effective against third parties by a single one-time registration covering security rights, whether they exist at the time of registration or are created thereafter, and whether they arise from one or more than one security agreement between the same parties (see recommendation 68).

38. As compared to asset-based indexing and searching, grantor-based indexing and searching has a drawback. Under the law recommended in the *Guide*, if the grantor sells or disposes of an encumbered asset outside the ordinary course of business, the security right will generally follow the asset into the hands of the transferee (see recommendations 79 and 81). Yet the security right will not be disclosed on a search of the registry record against the identifier of the transferee, potentially prejudicing third parties that deal with the asset in the hands of the transferee and that may not be aware of the historical chain of title. Suppose, for example, that grantor B, after granting a security right in its automobile in favour of secured creditor A, sells the automobile to third party C, who in turn proposes to sell or grant security in it to fourth party D. Assuming D is unaware that C acquired the asset from the original grantor B, he or she will search the registry using only C's

identifier. That search will not disclose the security right granted in favour of A because it was registered against the name of the original grantor B. This is generally referred to as the "A-B-C-D" problem (on the question whether a secured creditor should be obligated to amend its registration to add the transferee as a new grantor, see paras. 10 and 11 above).

39. In response to the "A-B-C-D" problem, some secured transactions laws provide for supplementary asset-based indexing and searching to preserve the secured creditor's rights to follow that asset into the hands of a transferee, lessee or licensee from the original grantor. Such rules apply to specific categories of high value and durable movable assets with significant resale market and for which unique and reliable serial numbers or equivalent alphanumerical identifiers are available (for example, road vehicles, trailers, mobile homes, aircraft frames and engines, railway rolling stock, boats and boat motors, hereinafter generally referred to as "serial number assets"). The motor vehicle market is a good example. Motor vehicles are of quite high value with a relatively significant resale market. Moreover, the automotive industry assigns a unique alphanumerical identifier, commonly referred to as a vehicle identification number, to identify individual motor vehicles according to a system based on standards issued by the International Organization for Standardization (ISO). In such a case, the vehicle identification number may be used for indexing and searching so as to be retrievable by searchers rather than the name of the grantor. This approach solves the "A-B-C-D" problem since a search based on the vehicle identification number will disclose all security rights granted in the particular motor vehicle by any owner in the chain of title.

40. The *Guide* discusses but does not recommend the possibility of using the serial number of an asset as a search criterion (see the *Guide*, chap. IV, paras. 34-36). If a State chooses to do so, rules similar to those mentioned above with respect to the use of correct identifier of the grantor would also apply to the use of serial numbers. However, if serial number registration is only mandatory for the purposes of third-party effectiveness and priority as against certain classes of competing claimants (for example, transferees of the encumbered assets), rules applicable to the search process should make it clear that a searcher is entitled to rely on a serial number search only to the extent that the particular searcher falls within the category of competing claimants for which entry of the specific serial number in the registration is required.

41. The registry system could also be designed to allow that notices may be searched and retrieved by reference to a registration number assigned by the registry either to each initial, amendment or cancellation notice or to a single registration number that covers the initial and any subsequent notice. While not generally useful to third parties as a search criterion (as third parties will not have the information), registration numbers would give secured creditors an alternative search criterion to quickly and efficiently retrieve a registration for the purposes of entering an amendment or cancellation (see paras. 22-28 above). Registration numbers could be particularly useful in circumstances where a notice could not be retrieved through the use of the identifier of the grantor due to indexing errors or changes in search logic.

42. Finally, the registry system could be designed so that information could be retrieved by the registry staff according to the identifier of the secured creditor. As already mentioned (see para. 21 above), this would enable registry staff, at the

request of the person identified in the registration as the secured creditor, to efficiently amend the identifier or address information of the secured creditor in all or multiple registrations associated with that secured creditor through a single global amendment.

43. However, the identifier of the secured creditor should not be a search criterion for searching by the public generally. The identifier of the secured creditor has limited relevance to the legal objectives of the registry system (see recommendation 64). Moreover, to allow public searching may violate the reasonable expectations of secured creditors; for example, because of the risk that a credit provider may undertake a search based on the secured creditor identifier to obtain the client lists of its competitors (see the *Guide*, chap. IV, para. 81).

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 31.*]

3. Search results

44. A search result should either indicate that no registrations were retrieved against the specified search criterion or list all registrations that match the specified search criterion along with the full details of the information as it appears in the registry record. Whether the result will reflect information that matches the search criterion exactly or only closely is a matter of the design of the registry system. The registry should issue a search certificate upon request by a searcher and payment of the relevant fee, if any. A search certificate should in principle be admissible as evidence in court that a notice as registered, or not, at a certain date and time. All these issues should be addressed in the registration rules.

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 32.*]

K. Language of registration and searching

45. The rules applicable to registration should clarify the language to be used to enter information in the registry. This language could be the official language or languages of the State under whose authority the registry is maintained or any other language specified by that State. In any case, search results should be displayed in the language in which the information was entered in the registry record (see the *Guide*, chap. IV, paras. 44-46). In addition, where the grantor's name is the relevant identifier and the correct name is in a language other than that used by the registry, the rules should clarify how the characters and any symbols that form the name are to be adjusted or translated to conform to the language of the registry.

46. The law under which a grantor that is a legal person is constituted may entitle the grantor to have and use alternative linguistic versions of its name. To accommodate that possibility, the rules applicable to registration should confirm that all linguistic versions of the name may be entered as separate grantor identifiers since third-party searchers may be dealing or have dealt with the grantor under any of the alternative versions of its name.

47. A way to mitigate the various problems that might arise from the use of multiples languages in the registry in the registration and search process would be to

use personal identification numbers as identifier of the grantor in lieu of the name of grantor.

L. Grantor's entitlement to additional information

48. As already discussed (see A/CN.9/WP.48/Add.1 paras. 15-68), a notice registered in the registry record contains minimum information about a security right that may not even exist at the time of registration. Thus, in certain circumstances, the grantor (in particular if the grantor is not the debtor but a third party) may need to request additional information about the security right. While the *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 grantor additional information about the security right, such as: (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.

49. 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.

[*Note to the Working Group: The Working Group may wish to note that the grantor's entitlement to additional information is not dealt with in the law*.]

V. Registry design, administration and operation

A. Introduction

50. Technical design, administrative and operational issues are crucial components of an effective and efficient registry system. This chapter canvasses the principal issues that must be addressed at this level.

B. Electronic versus paper registry record

51. Registry records traditionally were maintained in paper form and this is still the case in some States. An electronic registry database offers enormous

efficiency advantages over a traditional paper-based record (see the *Guide*, chap. IV, paras. 38-43). These advantages include:

(a) A greatly reduced archival and administrative burden;

(b) A reduced vulnerability to physical damage, theft and sabotage;

(c) The ability to consolidate information in all notices in a single database regardless of the geographical entry point of the information in notices; and

(d) The facilitation of speedy low-cost registration and search processes (see the discussion on modes of access to the registry in paras. 56-59 below).

52. Accordingly, every effort should be made by enacting States to provide for the storage of information contained in a notice in an electronic as opposed to a paper record. This is the approach recommended in the *Guide* (see recommendation 54, subpara. (j)).

53. The *Guide* includes in recommendations 11 and 12 the basic rules to accommodate electronic communications taken from article 9, paragraphs 2 and 3, of the United Nations Convention on the Use of Electronic Communications in International Contracts on written form and signature requirements. The rules applicable to electronic registries should be consistent with these recommendations and the principles of non-discrimination, technological neutrality and functional equivalence on which recommendations 11 and 12 are based (see the *Guide*, chap. I, paras. 119-122, as well as Explanatory Note to the Convention, paras. 133-165).

C. Centralized and consolidated registry record

54. Under the approach recommended in the *Guide*, registrants and searchers will be able to access the registry through multiple modes and access points because registry records will likely be centralized and consolidated (see recommendation 54, subparas. (e) and (k)). This means that all information will be stored in a consolidated database. Otherwise, the transaction costs faced by registrants in having to register and searchers in having to conduct searches in multiple decentralized registry records may deter utilization of the registry system and undermine the success of the secured transactions law. A centralized registry record would especially be effective for multi-unit States (see recommendations 224-227).

55. As noted above, centralization of the registry record can be achieved far more efficiently if information contained in notices is stored in electronic form in a centralized computer database than if the registry record is maintained in paper form. An electronic record enables information submitted to branch offices of the registry to be entered at the branch office and transferred electronically to the centralized registry database. In paper systems, the information flows in a similar way except that the physical document has to be first manually transferred from the branch to the central office where the centralized paper record is maintained (see the *Guide*, chap. IV, paras. 21-22).

D. User access to the registry services

56. An electronic registry record enables users to submit notices and conduct searches directly without the need for the assistance or intervention of registry personnel. If possible, the system should be designed to support the electronic submission of notices and search requests over the Internet or via direct networking systems as an alternative to the submission of paper registration notices and search requests (see the *Guide*, chap. IV, paras. 23-26 and 43).

57. As already discussed (see paras. 1-4 above), 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 the searcher must wait until the registry staff member carries out the search on their behalf and transmits the results. In addition to eliminating these delays, a system in which registrants 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) A reduction in the risk of error and 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.

58. If this approach is implemented, the registry should be designed to permit registry users to enter information and conduct searches from any computer facilities, whether private or public available at branch offices of the registry or other locations. In addition, owing to the reduced costs of direct electronic access, the registry should be designed to permit third-party private sector service providers to provide registry services to interested parties.

59. To preserve the security and integrity of the registry record, users may be issued, for example, unique access codes and passwords (other methods of access and identification may also be used). As a measure of protection against the risk of unauthorized registrations, potential registrants may additionally be required to supply some form of identification (for example, an identification card, driver's licence or passport) as a precondition to submitting a registration (see recommendation 55, subpara. (b)), while the registry is not required to verify the identity of the registrant (see recommendation 54, subpara. (d)). To facilitate access for frequent users (such as financial institutions, automobile dealers, lawyers and other intermediaries acting for registrants and searchers), all users should have the option of setting up a user account with the registry that permits automatic charging of fees to the users' credit account with the registry and institutional control of the user's access rights. It might also be necessary to provide certain frequent users (for example, a bank) with special access codes whereby its multiple

constituents (for example, the branch offices or its staff) could access the registry record.

E. Specific design and operational considerations

1. General

60. This section is intended to provide guidance to States, in line with the *Guide*, as to the specific design of a registry system by discussing examples of possible approaches. It is not intended to prescribe the exact way in which a registry is to be designed.

2. Establishment of an implementation team

61. It is critical that the technical staff responsible for the design and implementation of the registry are fully apprised of the 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 establish a team that reflects technological, legal and administrative expertise, as well as user perspectives.

3. Design and operational responsibility

62. It will 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. Under the *Guide*, while the day-to-day operation of the registry may be delegated to a private entity, the enacting State retains the responsibility to ensure that the registry is operated in accordance with the applicable legal framework (see the *Guide*, chap. IV, para. 47, and recommendation 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.

4. Storage capacity

63. The implementation 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. In this 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, it will need to take into account the need to expand the registry database at a later point to accommodate the registration of judgments or non-consensual security rights or the addition of linkages to other governmental records such as the State's corporate registry or 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.

5. Programming

64. If the registry record is computerized, the programming specifications will depend on whether grantor-based registration, indexing and searching will be supplemented by serial number registration, indexing and searching. In any event, the hardware and software specifications should be robust and secure employing features that minimize the risk of data corruption, technical error and security breach. 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, electronic links between registries, computer-to-computer communication and the gathering of statistical data.

65. 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 which event 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.

66. Consideration should also be given to whether the registry should be designed to function as an electronic interface to 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.

67. Another issue that should be considered is whether the registry system would allow one or more than one type of search. In some States, there is only one type of search that is based on the official search logic (the program applied by a registry system to the search criteria provided by the searcher to retrieve information from the registry record). In those States, all that the searcher has to do is enter the correct grantor identifier and the registry system will automatically apply the official search logic and produce an official search result.

68. In other States, there is also an unofficial search. This type of search allows users to expand their search and for this purpose uses non-standard characters. For example, if the official search logic is strict returning only exact matches and a registrant registered a notice against “John Macmillan” misspelling the name as “John Macmallan”, an official search using the correct grantor identifier “John Macmillan” may not retrieve the notice and thus the registration may be ineffective. However, an unofficial search against the name “John Macm*” will most likely retrieve the notice with the misspelled name. However, this does not change the fact that the registration is ineffective because only an official search would allow a searcher to retrieve the relevant notice. A searcher cannot rely on the result retrieved using this type of search. In any case, a searcher must know which search logic is official, that is, in the case of an electronic registry, which button to select or in which field to enter the correct identifier and then the registry system will apply the search logic automatically.

6. Reducing the risk of error

69. The registry can be designed to ensure a basic level of information quality, while also preventing registrants from committing errors by, for example,

incorporating mandatory fields, edit checks, drop-down menus and online help resources. The registry may also be designed to enable a registrant to conduct a review of the information it has entered as a final step in the registration process.

7. Loss of data, unauthorized access and duplication of registry records

70. An electronic registry record may be inherently less vulnerable to physical damage than a paper registry record but more vulnerable in other respects such as loss of data, unauthorized access and duplication. In that context, measures to prevent loss of data, unauthorized access to and duplication of registry records need to be considered and implemented. Ways to ensure uninterrupted service of the registry system and to recover quickly from natural and artificial disasters need to be developed as well.

8. Role of registry staff and liability

71. The role of registry staff should essentially be limited to managing and facilitating access by users, processing fees and overseeing the operation and maintenance of the registry system. It should be made clear to staff and to registry users that registry staff are not allowed to give legal advice on the legal requirements for effective registration and searching or on the legal effects of registrations and searches.

72. Registry staff should also be responsible for ongoing monitoring of the way the registry is working (or not working) in practice, including gathering statistical data on the quantity and types of registrations and searches that are being made, in order to be in a position to suggest any necessary adjustments to the registration and search processes and the relevant regulations.

73. The potential for registry staff corruption should be minimized by designing the registry system to: (a) make it impossible for registry staff to alter the time and date of registration or any other information entered by a registrant; (b) eliminate any discretion on the part of registry staff to reject access to the registry services; (c) institute financial controls that strictly limit staff access to cash payments of fees (for example, by making it possible for payments of fees to be made to and confirmed by a bank or other financial institution); and (d) maintaining the archived copy of the original data submitted as previously outlined.

9. Liability for loss or damage suffered by secured creditors or third-party searchers

74. As already noted, the registry should be designed, if possible, to enable registrants and searchers to submit information for registration and conduct a search directly and electronically as an alternative to having registry staff do this on their behalf (see recommendation 54, subpara. (j)). If this approach is adopted, the registration rules should make it clear that users bear sole responsibility for any errors or omissions they make in the registration or search process and carry the burden of making the necessary corrections or amendments.

75. This point aside, the enacting State will need to assess how responsibility for loss or damage due to any of the following causes is to be allocated: (a) incorrect or misleading advice or information or unjustified denial of registry services by the registry staff; and (b) delay or erroneous or incomplete registrations or search

results caused by a system malfunction or failure. While in cases where the registry permits direct registration and searching by registry users the law recommended in the *Guide* limits the responsibility of the registry to system malfunction, it generally leaves this matter to enacting States (see recommendation 56). In some States, part of the registration and search fees is put into a fund to cover possible liability of the registry for loss or damage suffered by secured creditors or third-party searchers. In other States, there are other insurance schemes aimed at covering such liability of the registry.

10. Registration and search fees

76. Under the law recommended in the *Guide*, registration and search fees, if any, should be set at a cost-recovery level as opposed to being used to extract tax revenue (see recommendation 54, subpara. (i)). In some States, in which the registry is established and managed by the government, no fee is charged for registration or searching. In any case, excessive fees and transaction taxes will significantly deter utilization of the registry, thereby undermining the overall success of the enacting State's secured transactions law. However, in assessing the level of revenue needed to achieve cost-recovery, account should be taken of the need to fund the operation of the registry, including: (a) salaries of registry staff; (b) replacement of hardware; (c) upgrading of software; (d) ongoing staff training; and (e) promotional activities and training on the registry operations for the users.

77. Consideration should be given to whether registration fees should be set on a per transaction basis or based on a sliding tariff related to the duration of the registration (in systems that permit registrants to self-select the registration term). The latter approach has the advantage of discouraging registrants from selecting an inflated term out of an excess of caution. Whatever approach is adopted, fees should not be related to the maximum amount specified for which the security right can be enforced (in systems that require this information to be included) since this would discourage registration, depress credit overall and undermine the benefits of an otherwise modern and efficient secured transactions law.

78. Consideration should also be given to whether searches and cancellations should be free of charge (at least in the case of an electronic registry) so as to encourage searching by the public and the prompt registration of cancellations by secured creditors.

[*Note to the Working Group: The Working Group may wish to note that the relevant article in the draft model regulations is article 33.*]

11. Financing initial acquisition, development and operational costs

79. The implementation of a modern electronic registry requires an initial capital investment to cover the cost of implementation of the registry, including hardware and software acquisition and development costs. However, the comparatively low cost of operation of an electronic security rights registry means that this investment should be recoverable out of service fees within a relatively short period after start-up through registration and search fees. The cost can be kept low, especially if the registry record is computerized and direct electronic registrations and searches are permitted.

80. If a State decides to develop and operate the registry in partnership with a private entity, it may be possible for the private entity to make the initial capital investment in the registry infrastructure on the understanding that it will be entitled to recoup its investment by taking a percentage of the fees charged to registry users once the registry is up and running.

12. Education and training

81. To ensure a smooth implementation of the registry system and its active take up by potential users, the implementation team will need to develop education and awareness programmes, disseminate promotional and explanatory material, and conduct training sessions. The implementation team should also develop instructions on entering information into paper registration forms and electronic screens.

F. Transition

82. The law recommended in the *Guide* may well constitute a significant departure from old law. In view of this fact, the law recommended in the *Guide* contains a set of fair and efficient rules governing the transition from the prior law to the new law. In particular, the law recommended in the *Guide* addresses two important transition issues, the date as of which the new law will come into force (the "effective date") and the extent to which the new law will apply to transactions or security rights that existed before the effective date.

83. Specifically with respect to the third-party effectiveness of a security right, the law recommended in the *Guide* provides that a security right that was effective against third parties under prior law remains effective until the earlier of: (a) the time it would cease to be effective against third parties under prior law; and (b) the expiration of a period of time specified in the law after the effective date (the "transition period") (see recommendation 231).

84. If the enacting State does not have a registry for security rights in movable assets, the establishment of a new registry would give all existing secured creditors a quick, easy and inexpensive way of maintaining their priority status. The new registry would also allow grantors to use more easily than under prior law the full value of their assets as security for credit as they would be able to create security rights in the same assets in favour of more than one secured creditor as long as the priority status of each secured creditor is clear.

85. If the enacting State already has in place a registry for security rights in movable assets, additional transitional considerations will need to be addressed. For example, if the new registry is intended to cover security rights previously within the scope of an existing registry, the following approaches may be considered. First, the enacting State or the private entity responsible for implementing the registry may assume responsibility for migrating the information in the existing records into the new registry record. Alternatively, the burden of migration can be placed on secured creditors that would be given a transitional period (for example, one year) to themselves re-enter the information in the new registry record. This latter approach has been used with considerable success in a number of States (especially, when such "re-registration" is free of charge). If this option is chosen, a space or

field on the registration form should be provided for entering a note that the registration is a continuation of a registration made prior to the coming into operation of the new registry (for transition issues with respect to matters addressed in the secured transactions law, see chap. XI of the *Guide*).

G. Dispute resolution

86. A dispute resolution mechanism may be considered to settle controversies between the parties involved in registrations relating to security rights. The mechanism should include summary judicial or administrative procedures of the type discussed with regard to the cancellation or amendment of registration (see paras. 22-26 above).