

V. MOVABLES REGISTRY OPERATIONS: EFFECTIVENESS OF REGISTRATION OF REGISTRY CLIENTELE

A. Introduction

150. This chapter is focused on the day-to-day operation of movables registry from the perspective of registry clientele, primarily secured creditor registrants or their agents, and interested members of the public, such as other creditors, insolvency administrators and prospective purchasers and secured creditors. In particular, this chapter identifies and analyzes policy questions relating to the requirements for an effective registration, and the impact on the

¹⁹ For example, see section 142 of the *New Zealand Personal Properties Security Act, 1999* reproduced in Appendix B.

effectiveness of a registration of errors or omissions in the entry of registration data and of unauthorized amendments and discharges.

B. Advance Registration

151. In a document filing registry system, it is clearly not possible for a secured creditor to effect registration until the charge agreement has actually been concluded with the debtor. However, in a notice-registration system, advance registration becomes a practical possibility.

152. Although the charge does not actually take effect until it is granted, modern movables registry systems typically authorize advance registration.²⁰ Advance registration offers important advantages for both secured creditors and debtors. Since priority among charge-holders in a movables registry system is ordered by reference to the time of registration, advance registration enables a secured creditor to establish a first-ranking priority position against subsequent charge holders at an early stage in the negotiation process. This enables the prompt advance of credit to the debtor as soon as the charge agreement is concluded.

153. In a system that does not permit advance registration, the secured creditor runs the risk that by the time negotiations are concluded, an intervening secured creditor will have taken and registered a charge against the same collateral. Such a system also promotes litigation on the precise time when a particular charge took effect legally since third parties would be able to challenge the validity of a registration on the basis that it was made prematurely.

154. The scenario that follows illustrates the operation of the general first-to-register priority rule explained in Chapter II in a system that permits advance registration.

Box V-1
Scenario 10: Advance Registration and Priority Ordering
<p>On 1 June, (Prospective) Secured Creditor 1 registers notice of a charge that potentially covers certain described movable assets owned by Debtor. At this time, no charge agreement yet exists between the parties.</p>
<p>On 1 June, (Prospective) Secured Creditor 2 registers notice of a charge that potentially covers certain described movable assets owned by Debtor. At this time, no charge agreement yet exists between the parties.</p>
<p>On 1 August, Secured Creditor 1 enters into a charge agreement with Debtor giving Secured Creditor 1 a charge on the assets described in Secured Creditor 1's registered notice.</p>
<p>In a system that permits advance registration, priority among competing secured creditors holding a charge in the same assets is determined by the order of the registration, not the order in which the competing charges were actually granted. It follows that although Secured Creditor 2 was the first to obtain a charge on the relevant assets, Secured Creditor 1 has priority because it was the first to effect a registration relating to the same assets.</p>

155. Advance registration carries a risk of false registrations in cases where the credit negotiations between the debtor and the registering party are aborted and no charge is ever granted. The fact that a registered charge still subsists on the record may adversely affect other

²⁰ For example, see section 146 of the *New Zealand Personal Property Securities Act, 1999*, reproduced in Appendix B.

creditors' perceptions of the creditworthiness of the alleged debtor. Imposing a legal obligation on registrants to discharge any registrations that do not represent an extant charge can effectively control this risk. To ensure compliance, this obligation should be backed up by a financial penalty for breach and a summary procedure whereby the named debtor can unilaterally compel discharge of the registration.²¹

C. A Single Registration for Successive Security Agreements

156. A notice registration system that permits advance registration carries with it a related benefit. If registration can be effected before any charge agreement has been concluded, there can be no objection to allowing parties in an on-going credit relationship to use a single registration to protect charges created under a succession of charge agreements entered into by them.²²

157. This facility dramatically reduces registration costs for the parties and gives them flexibility to amend and change their financing arrangement to meet changing circumstances without fear of loss of priority. Third persons searching the registry are not prejudiced provided that the secured transactions law makes it clear that a single registration is effective in relation to multiple charge agreements only if the registered information, including the collateral description, accurately reflects the terms of all related charge agreements. So long as this qualification is satisfied, it is immaterial that the registered information may reflect the terms of a series of charge agreements, rather than a single agreement. Either way, the third party searcher is alerted to the existence or potential existence of a charge.

D. Effective Time of Registration

158. If a movables registry system contemplates the submission of paper notices, there will inevitably be some delay between receipt of the completed notice in the registry office and the time when the notice or the information on it is entered into the registry record by the registry staff so as to be searchable. The same potential for delay exists, though less acutely, if the registration process allows for the electronic submission of the registration data, but requires that it be first checked or verified by registry staff before being entered in the record.

159. When should the registration be considered legally effected? Should this be on receipt of the notice in the registry, or only after the charge information becomes searchable by third parties?

160. If a registration is treated as legally effective as soon as the information is received in the registry office, third parties searching the registry must accommodate the possibility that any search result they obtain will not necessarily disclose all legally effective registrations. This burden is more easily dealt with if the system is programmed to disclose the latest processing date on all search results.²³

161. The alternative approach, under which a registration is effected only when the registration information is entered into the record so as to be searchable²⁴ allocates to the

²¹ For example, see sections 161-169 of the *New Zealand Personal Property Securities Act, 1999*, reproduced in Appendix B.

²² For example, see section 147 of the *New Zealand Personal Property Securities Act, 1999*, reproduced in Appendix B.

²³ This approach is used in the Ontario (Canada) Personal Property Registry. See further the Ontario Personal Property Security Act and regulations at www.e-laws.gov.on.ca/home.

²⁴ Articles 19(2)-(3) of the Convention on International Interests in Mobile Equipment, 2001, Appendix G.

registering secured creditor the risk and inconvenience associated with any delay in entry on the part of the registry staff. This allocation of risk can be justified on the basis that the secured creditor is in the best position to manage it by refusing to advance credit until a search result is obtained demonstrating that the registration has been successfully entered into the record.

162. If the registration process is very efficiently administered, secured creditors are unlikely to object to implementation of the latter approach since the delay between receipt of the registration information and its entry into the record will be negligible. Thus, in systems that have fully computerized the registration and searching process to enable registrants to directly enter their own data, the effective time of registration is invariably the time at which the registration data is entered by the registrant into the database so as to be searchable.²⁵ However, even in the most efficiently designed and operated systems, the potential for delay resulting from labor action or other events beyond the direct control of the registrar cannot be wholly eliminated.

E. Legal Effect of Unauthorized Amendments and Discharges

163. Chapter VI of the Guide addresses the range of possible administrative and technological measures that can be adopted to alleviate the risk for secured creditors of an unauthorized amendment or discharge of a registered notice.²⁶ However, it is administratively unworkable to oblige the registrar to verify or guarantee the background legal authority of registrants. Consequently, it is necessary to provide substantive guidance on the legal effect of entry into the record of an unauthorized amendment or discharge.

164. One possible approach would be to deny any conclusive legal effect to the entry of an amendment or discharge, thereby requiring searchers to obtain verification of the validity of the amendment or discharge directly from the secured creditor. A variant of this approach would delay the legal effectiveness of the amendment or discharge for a set time period after initial entry.

165. These solutions presume that registry searchers are sufficiently sophisticated to appreciate the limited information disclosure role of the system. They must understand that even though a search of the registry might disclose that a registration has been discharged or amended, they cannot legally rely on that information. Even if one assumes that the target users possess this level of legal sophistication, their inability to rely on amendment and discharge information disclosed in the registry results in serious inefficiencies. In addition to having to search the registry record, a third party searcher would also need to contact the named secured creditor in every case to obtain confirmation that registration of a recorded amendment or discharge had in fact been authorized. This would create delay and might even prevent the debtor from being able to deal with the relevant asset if confirmation could not be obtained because the secured creditor could no longer be located or had ceased to exist.

166. These transactional inefficiencies are eliminated if all registered discharges and amendments are treated as legally effective from the perspective of third party searchers even if it turns out later that the registrant had acted fraudulently or without the authority of the secured creditor of record. Under this approach, there would be no need for searchers to incur the delay and cost associated with having to obtain verification of discharges and amendments through direct contact with secured creditors. Since all registered amendments and discharges would be

²⁵ For example, see section 141 of the New Zealand Personal Properties Securities Act, reproduced in Appendix B.

²⁶ The liability of the registry for the consequences of error, or even deliberate fraud, on the part of its staff is a separate issue that is also addressed in Chapter VI of the Guide.

considered *ipso facto* effective, searchers would not have to go beyond or behind the information disclosed on the public record.

167. This second approach preserves the ability of the public to rely on the integrity of the information disclosed on a registry search. On the other hand, it transfers to the secured creditor the risk that its charge will be defeated or subordinated through no fault of its own. Nonetheless, as a frequent volume player in the credit market, the secured creditor is in a better position to absorb and redistribute that loss than the equally innocent searcher who may be a one-time buyer, particularly since the experience to date indicates that the incidence of unauthorized or fraudulent entries is very small. In any event, even this relatively minor risk can be all but eliminated if the registry system is programmed to immediately notify the secured creditor of record of any changes made to its registration, and the secured creditor is then given the legal right to promptly reinstate its registration, subject only to intervening third party interests acquired in the collateral.²⁷

F. Adequacy of Registered Collateral Description

168. Chapter IV of the Guide explained the utility of adopting a collateral identifier as a supplementary or alternative registration-search criterion for limited categories of tangible, relatively high-value, items of collateral. In systems that adopt this approach, a specific description in accordance with the registry regulations or guidelines will be necessary to ensure a legally effective registration for charges granted on the relevant types of collateral. Moreover, to ensure that the collateral will be indexed properly so as to be searchable, secured creditors will have to take care to enter the prescribed description on the appropriate line or electronic field of the notice to be registered.

169. Explicit guidance should be given—either in the regulations or in the statute establishing the registry—on what constitutes a legally adequate description. Otherwise, at least some secured creditors will feel compelled, out of an excess of caution, to enter highly itemized collateral descriptions, thereby unnecessarily increasing their transaction costs.

170. Explicit legal approval of the use of generic collateral descriptions greatly enhances the extent of the collateral that can be effectively charged.²⁸ A single registration can cover future and after-acquired assets, and circulating funds or pools of assets (for example, “all accounts” or “all inventory”). Indeed, to the extent the underlying secured transactions law permits charges on all of the movable assets of the debtor, there is no reason to require even generic descriptions of the collateral. A simple one-line description—“all present and after-acquired property of the debtor”—provides adequate and accurate guidance to third party searchers: clearly everything in the debtor's possession or control is potentially subject to the registered charge.

171. Although most modern movables registry systems authorize the use of generic descriptions, different approaches are taken on the issue of whether the description must define the exact scope of the collateral actually covered by the charge. In some systems, the registrant is required merely to indicate the generic nature of the charged assets, for example; “tangible movables”, or “automobiles” even if the actual charge only covers a specific thing within that category; for example, a single automobile. In others, the registered description must reveal the

²⁷ This solution has been adopted by most of the Canadian Personal Property Security Acts. See, for example, section 35(7) of the Saskatchewan *Personal Property Security Act*, 1993.

²⁸ Generic descriptors of this kind may be used under most Canadian systems. See, e.g., section 12 of the British Columbia Personal Property Registry Regulations, Reg. 279/90 reproduced at: www.qp.gov.bc.ca.

particular kind and quantity of collateral subject to the charge; for example, “2 Ford Ranger trucks, 2002 Model.”

172. On the one hand, a less precise description requirement reduces the registration burden for secured creditors and the risk of description errors. On the other hand, it has limited disclosure value for third persons. In order to ascertain the precise scope of the charge, searchers must obtain details from the secured creditor directly or through the debtor.²⁹ Moreover, in systems that permit a single registration to cover successive agreements,³⁰ third party searchers will need to secure a waiver of priority from the secured creditor who has effected the registration in order to be protected against the risk that the parties will later enter into a more expansive security arrangement, even if at the time of the search, the existing charge agreement does not cover the specific assets of interest to the searcher.

G. Effect of Errors or Omissions in Registered Particulars

173. As explained in Chapter IV of the Guide, notices in a movables registry are indexed according to specified registration-search criteria set out in the notice in order to facilitate retrieval by searchers. In general, this is the debtor's name or some other type of unique debtor identifier. However, some systems adopt a collateral identifier—e.g., serial number—as an alternative or supplementary criteria for limited categories of collateral.

174. What is or should be the legal impact on the effectiveness of a registration if the secured creditor fails to submit the registration criterion or criteria in accordance with the applicable registry rules.³¹ The error or omission might involve an error in the spelling of the debtor's name or in the transcription of his or her identifying number, or, in the case of a collateral identifier, an error in the serial number. Is perfect accuracy necessary, or is there some tolerance for error?

175. Most modern movables registry regimes focus, appropriately, on the impact that the particular error or omission has on the practical retrievability of registered notices by third party searchers. Under this approach, an error or omission in the registration criteria submitted results in an invalid registration only if the error or omission is seriously misleading.³²

176. The test as to what is seriously misleading is objective. The extent to which an actual searching party has been misled or has suffered loss because of the error or omission is irrelevant. What matters is whether the error or omission likely would have misled a reasonable, hypothetical person searching the registry. In cases of doubt in the application of this test, the system assumes that the parties will have recourse to some judicial or arbitral body for a definitive ruling.

177. Under the seriously misleading test, a registered notice will be treated as invalid or a nullity if a searcher using the prescribed registration-search criterion could not reasonably discover the notice. If the system is paper based, a slight error in spelling or numbering is unlikely to mean that a reasonable searcher would not have discovered the charge.

178. However, the situation with respect to an electronic registry is a little more complicated. Everything depends on how the search software is programmed. If only exact matches to the

²⁹ On access to further off-record information about a registered charge, see the discussion in Chapter III of the Guide.

³⁰ On this issue, see the discussion in Chapter V of the Guide.

³¹ On the need for the Registry regulations to provide explicit guidance on this point, see Chapter IV of the Guide.

³² For example, see sections 149-151 of the *New Zealand Personal Property Securities Act, 1999*, reproduced in Appendix B.

search criteria entered will be returned, then even the slightest of errors on the part of the registrant will mean that the registered notice is a nullity.

179. In some regimes, policy makers have concluded that a system programmed to disclose only "exact matches" is too unforgiving from the secured creditor's perspective. The solution arrived at was for registry designers to adopt a computer search program that results in the retrieval of registrations that exactly match the registration-search criterion used by a searching person, and any registrations that are "similar matches" according to the coding system incorporated in the program software.³³ The determination of what constitutes a seriously misleading error in a system of this kind depends on the form and number of similar matches disclosed when the correct search criterion is used. The fact that a defective registration is disclosed as a similar match on a search using the correct registration-search criterion does not invariably mean that the registration is valid despite the error. This depends on the determination of whether a reasonable searcher would recognize that the registration, disclosed in the result only as a similar match, related to the collateral or debtor identified by the correct search criterion.

180. In considering whether to adopt a similarly flexible search programme, countries should beware of simply purchasing off the shelf software. The appropriateness and scope of similar matches that will be disclosed depends on customizing the program to accommodate local similar name variations and spellings.