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# FINANCIAL INCLUSION, ACCESS TO CREDIT, AND SUSTAINABLE FINANCE: WHAT ROLE FOR THE UNCITRAL MODEL LAW ON SECURED TRANSACTIONS?

ORKUN AKSELI\*

## I INTRODUCTION

There is a causality between financial inclusion, access to credit, and the way modern and efficient secured transactions law principles facilitate these concepts for the benefit of small business.<sup>1</sup> Predictable and effective secured transactions law principles, complemented by insolvency frameworks, may improve inclusive access to credit in both economically developed and developing countries by reducing the cost of credit and assisting economic and business growth.<sup>2</sup>

Financial inclusion encompasses widespread deposit-account ownership and access to payments services. Access to credit requires adequate loan funding on reasonable terms, especially for aspiring entrepreneurs from underserved groups. These two terms are gathered under the umbrella concept of sustainable finance, which can be defined as the continuous provision of financial inclusion and access to credit to both individuals and small and medium-sized enterprises (SMEs). In order to achieve sustainable finance, a widespread modernization of secured transactions law principles is needed. This is necessary to support individual entrepreneurs and SMEs. Sustainable finance is, therefore, an ultimate goal for both individuals and small businesses.

Financial inclusion, access to credit, and sustainable finance concepts have been at the forefront of law reform activities that aim to modernize secured transactions laws. The World Bank defines financial inclusion as a basic right that

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1. In this article, the term “small business” will be used to denote both micro and small and medium-sized enterprises (MSMEs and SMEs). There is no agreed or uniform definition of small businesses. For comparative definitions of small businesses, see, for example, Louise Gullifer & Ignacio Tirado, *A Global Tug of War: A Topography of Micro-Business Financing*, 81 *LAW & CONTEMP. PROBS.*, no. 1, 2018, at 109, 110; Orkun Akseli, *SMEs and Access to Finance: A Vulnerability Perspective*, in *LAW AND FINANCE AFTER THE FINANCIAL CRISIS: THE UNTOLD STORIES OF THE UK FINANCIAL MARKET* 116–34 (Abdul Karim Aldohni ed., 2017).

2. For similar arguments, see WORLD BANK GRP., *SECURED TRANSACTIONS, COLLATERAL REGISTRIES AND MOVABLE ASSET-BASED FINANCING KNOWLEDGE GUIDE* 9–10 (2019).

“individuals and businesses have access to useful and affordable financial products and services that meet their needs – transactions, payments, savings, credit, and insurance – delivered in a responsible and sustainable way.”<sup>3</sup>

For small businesses, a number of socio-economic policies have been established by governments and international financial institutions.<sup>4</sup> These policies largely seek to achieve financial inclusion and access to credit through four mechanisms. These are: (1) establishing credit reporting systems,<sup>5</sup> (2) modernizing insolvency regimes, (3) streamlining payment systems, and (4) modernizing secured transactions law and establishing electronic collateral registries.<sup>6</sup> Particularly, modernizing secured transactions laws and establishing electronic collateral registries are important to enable small businesses’ access to credit as they are engines for growth. Modernization will enable legal systems to respond effectively to finance devices and schemes geared to small business such as factoring, assignment of receivables, asset-based lending, and credit guarantee schemes.

In this process, modern principles of secured transactions law, and particularly the UNCITRAL Model Law on Secured Transactions Law (the

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3. *Financial Inclusion Overview*, WORLD BANK GRP., <https://www.worldbank.org/en/topic/financialinclusion/overview> [<https://perma.cc/656J-K9AK>].

4. See, e.g., OECD, MEETING OF THE OECD COUNCIL AT MINISTERIAL LEVEL: ENHANCING THE CONTRIBUTIONS OF SMES IN A GLOBAL AND DIGITALISED ECONOMY (2017), <https://www.oecd.org/industry/C-MIN-2017-8-EN.pdf> [<https://perma.cc/XL94-JB7L>]; TILMAN EHRBECK, MARK PICKENS & MICHAEL TARAZI, CONSULTATIVE GROUP TO ASSIST THE POOR [CGAP], FINANCIALLY INCLUSIVE ECOSYSTEMS: THE ROLES OF GOVERNMENTS TODAY (2012), <https://www.cgap.org/sites/default/files/Focus-Note-Financially-Inclusive-Ecosystems-The-Roles-of-Government-Today-Feb-2012.pdf> [<https://perma.cc/PGX8-RZRC>]. For an overview of secured transactions law reforms in response to socio-economic challenges, see generally Symposium, *Secured Transactions in the Twenty-First Century* 81 LAW & CONTEMP. PROBS., no. 1, 2018.

5. Pratibha Chhabra, Shalini Sankaranarayanan & Collen Masunda, *Why Credit Reporting matters in formulating policy during COVID-19 response and recovery*, WORLD BANK: BLOGS (June 3, 2020), <https://blogs.worldbank.org/psd/why-credit-reporting-matters-formulating-policy-during-covid-19-response-and-recovery> [<https://perma.cc/GBL5-822S>] (noting that access to credit reporting and data by all types of financiers (banks, asset-based financiers) is crucial in lending decisions, which need reliable credit information about the creditworthiness of businesses, but also highlighting that this creates competition among financiers which leads to the reduction of cost of credit).

6. For the work of the World Bank on secured transactions law reforms, see, for example, WORLD BANK GRP., *supra* note 2; WORLD BANK GRP., DISTRIBUTED LEDGER TECHNOLOGY & SECURED TRANSACTIONS: LEGAL, REGULATORY AND TECHNOLOGICAL PERSPECTIVES - GUIDANCE NOTES SERIES, NOTE 1: COLLATERAL REGISTRY, SECURED TRANSACTIONS LAW AND PRACTICE (2020); WORLD BANK GRP., DISTRIBUTED LEDGER TECHNOLOGY & SECURED TRANSACTIONS: LEGAL, REGULATORY AND TECHNOLOGICAL PERSPECTIVES - GUIDANCE NOTES SERIES, NOTE 2: REGULATORY IMPLICATIONS OF INTEGRATING DIGITAL ASSETS AND DISTRIBUTED LEDGERS IN CREDIT ECOSYSTEMS (2020); WORLD BANK GRP., DISTRIBUTED LEDGER TECHNOLOGY & SECURED TRANSACTIONS: LEGAL, REGULATORY AND TECHNOLOGICAL PERSPECTIVES - GUIDANCE NOTES SERIES NOTE 3: DISTRIBUTED LEDGER TECHNOLOGY AND SECURED TRANSACTIONS FRAMEWORK (2020).

UNCITRAL Model Law),<sup>7</sup> may play an important role. This Article will discuss the possible role of the UNCITRAL Model Law in the facilitation and implementation of financial inclusion, access to credit, and sustainable finance. To this end, the Article will particularly focus on some of the fundamental principles of the UNCITRAL Model Law and the way in which the rules based on these principles can assist credit markets as well as SMEs in accessing credit.

## II

### FINANCIAL INCLUSION AND CREDIT AVAILABILITY

Financial inclusion is the ability of individuals and corporations to have effective access to a wide range of appropriate financial services.<sup>8</sup> Credit is one of the most important vehicles for financial growth, and access to credit—the ability to access adequate loan funding on reasonable terms—is thus a specific focus of financial inclusion. Since the 2007–08 financial crisis, financial inclusion of small businesses has been in the agenda of governments, independent bodies,<sup>9</sup> and international financial institutions.<sup>10</sup> The United Nations Sustainable Development Goals 1 (No Poverty) and 8 (Decent Work and Economic Growth) are clear examples of supranational interest in achieving inclusive finance for both individuals and businesses.<sup>11</sup> Small businesses account for about 90% of businesses worldwide with 50% of employment around the world.<sup>12</sup> And, in the United Kingdom, small businesses account for 99.9% of businesses and employ more than 16.5 million people.<sup>13</sup> For small businesses, lack of a credit history or collateral are significant problems in access to finance.

While a credit infrastructure supports digitalized inclusive finance, lack of it limits small businesses' ability to deal with cash or check and prevents them from

7. U.N. COMM'N ON INT'L TRADE L., UNCITRAL MODEL LAW ON SECURED TRANSACTIONS, U.N. Sales No. E.17.V.1 (2016) [hereinafter MODEL LAW]. The UNCITRAL Model Law was supplemented by a Guide to Enactment.

8. Asli Demirgüç-Kunt, Leora Klapper & Dorothe Singer, World Bank Grp., *Financial Inclusion and Inclusive Growth: A Review of Recent Empirical Evidence 2* (WBG Dev. Rsch. Grp., Policy Research Working Paper No. 8040, 2017).

9. See FIN. INCLUSION COMM'N, FINANCIAL INCLUSION: IMPROVING THE FINANCIAL HEALTH OF THE NATION (2015) (detailing the Financial Inclusion Commission's findings and aspirations regarding the issue of financial inclusion in the United Kingdom).

10. See *Financial Inclusion*, WORLD BANK, [http://www.worldbank.org/en/topic/financial\\_inclusion](http://www.worldbank.org/en/topic/financial_inclusion) [<https://perma.cc/GSM2-XCJE>] (featuring The World Bank's resources and information on financial inclusion).

11. U.N. Dept. of Econ. & Soc. Affs., *The 17 Goals*, U.N., <https://sdgs.un.org/goals> [<https://perma.cc/JY4L-LV2A>].

12. *Small and Medium Enterprises (SMEs) Finance*, WORLD BANK GRP., <https://www.worldbank.org/en/topic/smefinance> [<https://perma.cc/2CLL-PN87>]. In the OECD areas, small businesses account for 99% of all enterprises and employ half of the work force. ORG. FOR ECON. COOP. & DEV. [OECD], IMPACT OF THE GLOBAL CRISIS ON SME AND ENTREPRENEURSHIP FINANCING AND POLICY RESPONSES 6 (2009), <https://www.oecd.org/cfe/smes/43183090.pdf> [<https://perma.cc/BHM6-TAUT>].

13. *UK Small Business Statistics*, FED'N OF SMALL BUS., <https://www.fsb.org.uk/uk-small-business-statistics.html> [<https://perma.cc/JC66-E34R>].

generating credit data which can be used for lending decisions.<sup>14</sup> Credit availability is possible if individuals have a bank account which enables them to accumulate savings and establish a trace of financial history.<sup>15</sup> This will enable the unbanked and the unincorporated to have access to low-cost financial services and low-cost credit. One way to achieve this is to create a robust credit infrastructure and support digitalization of financial services.

Similarly, the World Bank regards the creation of a robust credit infrastructure as the starting point for effective and sustainable access to credit for small businesses. Credit infrastructure has been defined as:

[T]he set of laws and institutions that enables efficient and effective access to finance through modern insolvency frameworks, secured lending on movable property, which enhances financial stability through diversification of financial products and services and improves risk management, assessment and mitigation through information asymmetry and supports socially responsible economic growth.<sup>16</sup>

There are a number of justifiable grounds for including small businesses in the finance circle through increased access to credit. First, small businesses' ability to access credit has a direct link with the creation of jobs.<sup>17</sup> This may lead to less dependency on public sector jobs or benefits. Less dependency on public sector jobs and benefits and increased employment may, in turn, renew confidence in the markets and the financial system, thereby regenerating the economy of a country.<sup>18</sup>

Second, small businesses' ability to access credit and protection from vulnerability to market changes—such as a financial crisis—work towards social

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14. See generally LEORA KLAPPER & DOROTHE SINGER, WORLD BANK DEV. RSCH. GRP. ET AL., THE OPPORTUNITIES OF DIGITIZING PAYMENTS (2014) [https://docs.gatesfoundation.org/documents/g20%20report\\_final.pdf](https://docs.gatesfoundation.org/documents/g20%20report_final.pdf) [<https://perma.cc/AJC5-J7ER>] (describing the effects of digitizing payments, transfers, and remittances on financial inclusion); Peter Zetterli & Rashmi Pillai, *Digitizing Merchant Payments: What Will It Take?*, CGAP (Sept. 2017), <https://www.cgap.org/research/slide-deck/digitizing-merchant-payments-what-will-it-take> [<https://perma.cc/K8DP-5NJ3>] (exploring the necessary conditions for digitizing merchant payments).

15. U.N. SEC'Y GEN.'S SPECIAL ADVOC. FOR INCLUSIVE FIN. FOR DEV. [UNSGSA] ET AL., IGNITING SDG PROGRESS THROUGH DIGITAL FINANCIAL INCLUSION 6 (Sept. 2018) (noting that according to the Global Findex, 39% of the poorest 40% of households worldwide lack an account); see generally ASLI DEMIRGÜÇ-KUNT, LEORA KLAPPER, DOROTHE SINGER, SANIYA ANSAR & JAKE HESS, WORLD BANK GRP., THE GLOBAL FINDEX DATABASE 2017: MEASURING FINANCIAL INCLUSION AND THE FINTECH REVOLUTION (2018) (discussing how digitization of payments and remittances is key to financial inclusion).

16. *Credit Infrastructure*, WORLD BANK GRP., <https://www.worldbank.org/en/topic/creditinfrastructure> [<https://perma.cc/MY2E-2JAQ>].

17. SMEs contribute to 67% of the full time and permanent employment worldwide and 85% to net employment growth. For SMEs contribution to job creation, see, for example, JAN DE KOK ET AL., EIM BUS. & POL'Y RES., DO SMES CREATE MORE AND BETTER JOBS? 5–6 (2011); see also Meghana Ayyagari, Asli Demirgüç-Kunt & Vojislav Maksimovic, *Small vs. Young Firms Across the World* (WBG Dev. Rsch. Grp., Policy Research Working Paper No. 5631, 2011).

18. Obviously, there are other methods to renew confidence in markets and one of them is the ability of “markets to demonstrate that they are more competent to regulate themselves either collectively or through bilateral contracting arrangements.” Julia Black, *Rebuilding the Credibility of Markets and Regulators*, 3 LAW & FIN. MKTS. REV. 1, 1–2 (2009).

well-being, financial inclusion, and social mobility. As a result, people improve their socio-economic levels through their entrepreneurships and contribute to the country's overall growth.<sup>19</sup> Rising income and confidence in financial markets could have a positive impact on social renewal.

Third, and in relation to small businesses' contribution to economic growth, although "weak legal and financial institutions in developing countries prevent SMEs from growing into large firms"<sup>20</sup> thus affecting growth negatively, access to finance remains crucial for growth.<sup>21</sup>

Fourth, access to credit for both individuals and small businesses is a basic equality requirement. If there is a system that enables both individuals and small businesses to have fair access to credit, then business growth may be promoted. That does not mean that too much debt or too much credit should be promoted by societies.<sup>22</sup>

Fifth, small businesses' access to inclusive finance is linked to social inclusion.<sup>23</sup> The limited availability and cost of credit make small businesses vulnerable to market uncertainties such as financial crises and pandemics.<sup>24</sup>

There are a number of reasons why small businesses and individuals are excluded from access to credit. Typically, in developing economies, individuals are excluded from financial services because they have lower incomes. These same individuals also might live in geographically isolated and rural areas. In certain cases, they have lower levels of education. Predominantly, female entrepreneurs are excluded from accessing credit, which signals underlying cultural and social problems in these countries.<sup>25</sup>

19. See, e.g., FRANK-BORGE WIETZKE & CATRIONA MCLEOD, *JOBS, WELL-BEING AND SOCIAL COHESION: EVIDENCE FROM VALUE AND PERCEPTION SURVEYS 2* (2013) ("[J]obs can contribute to social cohesion through their effects on personal wellbeing, identities, and political and social preferences.").

20. Meghana Ayyagari, Asli Demirgüç-Kunt & Vojislav Maksimovic, *SME Finance 4* (WBG Dev. Rsch. Grp., Policy Research Working Paper No. 8241, 2017).

21. *Id.* at 3.

22. See generally John Linarelli, *Debt in Just Societies: A General Framework for Regulating Credit*, 4 REG. & GOVERNANCE 409 (2020).

23. Agustín Carstens, gen. Manager, Bank for Int'l Settlements, Speech at the Rsrv. Bank of India: Central Banking and Innovation 2 (Apr. 25, 2019). For a discussion of social inclusion and SMEs, see, for example, Akseli, *supra* note 1, at 116.

24. For the effects market liberalisation on development and SMEs, see, for example, JOSÉ ANTONIO OCAMPO & JOSEPH E. STIGLITZ, *CAPITAL MARKET LIBERALIZATION AND DEVELOPMENT* (2008). As a response to COVID 19, there are certain measures to increase SME resilience such as OECD Policy Response to Coronavirus (COVID 19). *Coronavirus (COVID-19): SME policy responses*, OECD, <https://www.oecd.org/coronavirus/policy-responses/coronavirus-covid-19-sme-policy-responses-04440101/> [<https://perma.cc/F7NA-Q7TH>]; European Bank for Reconstruction and Development, *State Credit Guarantee Schemes: Supporting SME Access to Finance amid the COVID 19 Crisis*, EUR. BANK FOR RECONSTR. & DEV., <https://www.ebrd.com/what-we-do/economic-research-and-data/cse-economists/state-credit-guarantee-schemes.html> [<https://perma.cc/CQT5-R3VA>].

25. According to the World Bank figures, 56% of unbanked world is female. Access to finance for women is more challenging in economically underdeveloped countries. See, e.g., WORLD BANK GRP., *THE GLOBAL FINDEX DATABASE 36* (2017), <https://globalindex.worldbank.org> [<https://perma.cc/>

To understand why small businesses as well as individuals lack access to credit, one must have a clear picture of the difficulties they face.<sup>26</sup> First, access to credit is an acute problem for SMEs in emerging markets and developing economies, where trust in the financial system is especially low. Moreover, increased cost of credit enlarges the access to credit problem. Individuals and SMEs face higher cost of credit due to information asymmetry arising from a lack of credit history, lack of documentation necessary to open bank accounts, insufficient funds to provide collateral or entice financiers, lack of other members of the entrepreneur's family having accounts which would allow the entrepreneur to use that account, and non-incorporation (which is a problem for small businesses which cannot attain access to secured lending).<sup>27</sup>

In order to mitigate operational risks and facilitate access to credit, financial technology (fintech) aims to lower the costs of credit and other financial transactions through new technologies and alternative forms of credit. These new technologies and alternative forms of credit include blockchain technology, peer-to-peer lending, and crowdfunding. Fintech's purpose is to expand financial inclusion by offering services to businesses and individuals that are otherwise excluded due to the limitations of their business structures—unincorporated small businesses, partnerships, or sole proprietorships—or lack of access to banking or acceptable collateral. These new technologies are also believed to reduce moral hazards which are linked to the use of intermediaries.<sup>28</sup> The World Bank supports the use of these digital technologies in financial transactions “to deepen financial markets, enhance responsible access to financial services, and improve cross-border payments and remittance transfer systems.”<sup>29</sup>

The use of blockchain and cryptoassets could act as a cure to financial exclusion in jurisdictions where there is a need for even the basic access to

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W7WP-8Z9P]. In Afghanistan, only 7% of Afghan women have a bank account. Press Release, Int'l Fin. Corp., IFC Supports Afghan Women's Access to Financial and Non-Financial Services, INT'L FIN. CORP., <https://ifcextapps.ifc.org/IFCExt/Pressroom/IFCPressRoom.nsf/0/0A30395C06E7D446852585C20026C6F3> [https://perma.cc/SWC7-96X2]; see also M. Miller et al., *How can digital financial services help a world coping with COVID-19?*, WORLD BANK: BLOGS (Aug. 3, 2020), <https://blogs.worldbank.org/psd/how-can-digital-financial-services-help-world-coping-covid-19> [https://perma.cc/UN5J-B8J7]; INT'L FIN. CORP., STRENGTHENING ACCESS TO FINANCE FOR WOMEN-OWNED SMEs IN DEVELOPING COUNTRIES 40 (Oct. 2011), [https://www.ifc.org/wps/wcm/connect/2a9123b3-d369-4115-8cbf-19083218ce64/G20\\_Women\\_Report.pdf?MOD=AJPERES&CVID=jqeI-xk](https://www.ifc.org/wps/wcm/connect/2a9123b3-d369-4115-8cbf-19083218ce64/G20_Women_Report.pdf?MOD=AJPERES&CVID=jqeI-xk) [https://perma.cc/2VRM-Q6PS].

26. Carstens, *supra* note 23, at 3.

27. This last barrier is significant in England where English law suggests only companies can create floating charges under Companies Act 2006 Part 25, whereas an unincorporated entity cannot as the Bills of Sale Act requires all the assets to be described specifically, and the grantor to be the true owner of the asset at the time of creation. Bills of Sale Act 1878 applies for assignments by individuals and requires a complex registration process.

28. International Monetary Fund [IMF], *Virtual Currencies and Beyond: Initial Considerations*, IMF Staff Discussion Note, SDN/16/03 (Jan. 2016).

29. Press Release, IMF Policy Paper, The Bali Fintech Agenda: A Blueprint for Successfully Harnessing Fintech's Opportunities 3, Press Release No. 18/388 (Oct. 11, 2018).

banking.<sup>30</sup> However, there is no clear and convincing evidence that eliminating intermediaries and using cryptocurrencies could help financial inclusion. Financial inclusion or exclusion denotes a “socioeconomic problem.”<sup>31</sup> And, in any case, conventional currency, access to banking and financial services, and a bank account are necessary to be able to purchase cryptocurrencies.<sup>32</sup> Thus, improving access to conventional credit must at least complement fintech innovations.

### III

#### INCREASING FINANCIAL INCLUSION AND THE MODERNIZATION OF SECURED TRANSACTIONS LAWS: THE ROLE OF THE UNCITRAL MODEL LAW

The ability to give security against the loss of investment influences both the cost and availability of credit. This applies equally in both developed and developing economies. Since the 1990s, many jurisdictions have embarked upon modernizing secured transactions laws.<sup>33</sup> Some of these modernization activities have evolved from within domestic legal systems—as a result of autopoietic evolution of law<sup>34</sup>—intended either to increase a country’s credit rating,<sup>35</sup> or to emulate the successful implementation of secured transactions reform by a neighboring country.<sup>36</sup> Some modernization activities have instead been recommended by international financial institutions, as where a national government invites assistance to modernize its activities or a country goes through austerity measures to meet the conditions of finance offered by international financial institutions.<sup>37</sup> Modern principles of secured transactions law may, therefore, assist small businesses and individual entrepreneurs in obtaining inclusive access to finance. In this process, the UNCITRAL Model Law plays a crucial role in the modernization of domestic secured credit legislations. The UNCITRAL Model Law, similar to the key objective and fundamental principles recommended by the UNCITRAL Legislative Guide on Secured Transactions (Legislative Guide), aims to increase the availability of credit at

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30. HOUSE OF COMMONS TREASURY COMMITTEE, CRYPTOASSETS, 2017-9, HC 910, ¶¶ 26–7 (UK).

31. *Id.* at ¶ 28.

32. *Id.* at ¶ 27.

33. See Louise Gullifer & Orkun Akseli, *Secured Transactions Law Reform: Principles, Policies and Practice*, SING. J. LEGAL STUD. (2016) (examining reforms in secured transactions law).

34. Law as an autopoietic system is the idea that law works as a self-regulating system. For autopoiesis in law, see generally GUNTHER TUEBNER, *LAW AS AN AUTOPOIETIC SYSTEM* (1993).

35. See WBG, *DOING BUSINESS 2019 TRAINING FOR REFORM* (16th ed. 2019).

36. Examples of these can be experienced in African jurisdictions. See generally MAREK DUBOVEC & LOUISE GULLIFER, *SECURED TRANSACTIONS LAW REFORM IN AFRICA* (2019).

37. This was particularly the case in financial crises in the 1990s and post-2008.



affordable rates by providing predictable and efficient secured transactions law rules.<sup>38</sup> This is fundamental to the growth of the economy.<sup>39</sup>

The primary objective of the UNCITRAL Model Law is to promote low-cost credit by enhancing the availability of secured credit. The UNCITRAL Model Law achieves this objective by establishing clear rules aimed to facilitate access to low-cost credit in cross border assignments and loan transactions for specific equipment, and by creating models for countries to modernize their domestic credit and security laws. A secured credit law should provide predictable and clear rules so that parties can establish certainty about the consequences of their transactions. This certainty and predictability allow for more parties to lend and borrow, thereby increasing competition in the credit market, and decreasing the cost of credit. Thus, these rules will provide benefits from otherwise-unavailable access to credit.<sup>40</sup> If secured credit is available at a reasonable cost, debtors, creditors, and the economy can benefit.

Further, the transposition of the fundamental principles and key policies of the UNCITRAL Model Law into domestic laws will provide more certainty to financiers, leading to more favorable lending terms and greater access to credit. Uncertainty about a lender's rights in default leads the lender to include a risk premium in interest rates and demand shorter maturities. High interest rates and short-term maturities deter borrowers from expanding their businesses. When lenders and borrowers operate in a legal environment where both parties to a loan transaction can ascertain the consequences of their transaction, the lender does not include the risk premium in the interest rate and lends with longer maturities. These favorable terms may increase borrowers' access to affordable credit and, in turn, business development.

Some of the fundamental policies of the UNCITRAL Model Law that can assist the achievement of financial inclusion can be summarized as follows.<sup>41</sup> First, borrowers should be enabled to use the full value inherent in their assets to support credit. Second, the law should provide for equal treatment of diverse sources of credit and of diverse forms of secured transactions. All transactions that secure the payment or performance of an obligation should be governed as

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38. See U.N. COMM'N ON INT'L TRADE LAW, UNCITRAL LEGISLATIVE GUIDE ON SECURED TRANSACTIONS, rec. 1(a), U.N. Sales No. E.09.V.12 (2011) [hereinafter LEGISLATIVE GUIDE] (recommending that the law be designed "to promote low-cost credit by enhancing the availability of secured credit").

39. See generally Larry E. Ribstein & Bruce H. Kobayashi, *An Economic Analysis of Uniform States Laws*, 25 J. LEGAL STUD. 131 (1996) (presenting economic efficiency arguments related to harmonisation and unification activities); Ross Levine, *Finance and Growth: Theory and Evidence* (National Bureau of Econ. Research, Working Paper No. 10766, 2004).

40. See Richard Calnan, *What makes a good law of security?*, in RESEARCH HANDBOOK ON SECURED FINANCING IN COMMERCIAL TRANSACTIONS 451–86 (Frederique Dahan ed. 2015) (describing the objectives of a simple and modern secured transactions law).

41. See U.N. COMM'N ON INT'L TRADE LAW, UNCITRAL MODEL LAW ON SECURED TRANSACTIONS GUIDE TO ENACTMENT, 5–8 [hereinafter ENACTMENT GUIDE] (providing the "key objectives" of the UNCITRAL Model Law).

a single security interest. Thus, the economic function, or the substance, of these devices should be the basis.<sup>42</sup> Third, parties should be enabled to obtain security rights in a simple and efficient manner. Fourth, the law should recognize non-possessory security rights in all types of assets. Fifth, registration of a notice in a general security rights registry should be expanded to all types of borrowers and not just incorporated businesses. Sixth, subject to certain exceptions—such as purchase money security interest—super-priority and priority rules should be based on a first-in-time, first-in-right basis among competing claimants such as insolvency administrators, other secured creditors, and third-party transferees. Seventh, efficient and extra-judicial enforcement of a secured creditor's rights also should be enabled. Finally, parties should be allowed the maximum flexibility to negotiate the terms of their security agreements.<sup>43</sup>

The UNCITRAL Model Law, by adopting a *functional* approach, applies to all types of rights in movable property that parties create consensually which secure the payment or performance of an obligation. The underlying idea of having a unitary, functional, and comprehensive approach under the UNCITRAL Model Law is to eliminate the inherent problem of fragmentation in national laws. That suggests that the UNCITRAL Model Law applies to, for example, a transfer of title for security purposes, a retention-of-title sale, or a financial lease, which, under English Law, are not regarded as traditional security rights but rather treated as quasi-security rights. A small business' main collateral, generally, is its receivables. Small businesses borrow on a secured basis unlike large firms that borrow on an unsecured basis.<sup>44</sup> In some cases, where the small business is not in the form of a company, it may not be able to grant charge over its inventory. That is why it is important to recognize all types and forms of assets to be used as collateral.

The UNCITRAL Model Law has a comprehensive approach. The security right secures all types of obligations, which may be present or future, determined or determinable.<sup>45</sup> It can encumber assets described specifically or generally, or even all of the assets of a grantor, which may be present and future, including a changing pool of assets. Furthermore, it may be created or acquired by any legal or natural person, including a consumer, subject to consumer protection law.<sup>46</sup> Security should be taken on any asset with economic value to secure any obligation. A security right may encumber any type of movable asset, a part of or an undivided right in a movable asset, a generic category of movable assets, and

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42. For more information on functional approach see, for example, Michael G. Bridge, *Formalism, Functionalism and Understanding the Law of Secured Transactions*, 44 MCGILL L.J. 567 (1999).

43. See generally, Catherine Walsh, *The Role of Party Autonomy in Determining the Third Party Effects of Assignments: Of "Secret Laws" and "Secret Liens"*, 81 LAW & CONTEMP. PROBS., no. 1, 2018, at 181 (arguing for an exception to unmitigated deference to autonomy where it might injure third parties).

44. LAW COMM'N, COMPANY SECURITY INTERESTS, 2005, Cm. 6654, ¶ 1.2 (UK).

45. LEGISLATIVE GUIDE, *supra* note 38, rec. 16; MODEL LAW, *supra* note 7, at ch. II, art. 7.

46. LEGISLATIVE GUIDE, *supra* note 38, rec. 2; MODEL LAW, *supra* note 7, at ch. I, art. 1.

all of a grantor's movable assets.<sup>47</sup> The debtor should be allowed to dispose of the assets, such as its inventory, free of charge in the ordinary course of business. The modern secured transactions rules allow this by enabling the creation of security interests in all assets of the business by a single agreement which covers both the future and the existing assets.<sup>48</sup> A security interest automatically extends to any identifiable proceeds of the encumbered assets as well as the identifiable proceeds of the proceeds.<sup>49</sup> This is particularly important to protect the interests of the secured creditor. This is because "a grantor could effectively deprive a secured creditor of its security by disposing of the encumbered assets either to a person who would take them free of the security right or to a person from whom those assets could not easily be recovered."<sup>50</sup>

Parties should be able to create security interests in a simple and efficient manner.<sup>51</sup> This is particularly important to reduce the cost of credit. In cross border loan transactions, certainty and predictability in the creation of security interests potentially lead to the reduction of risk premiums. A security right under the UNCITRAL Model Law is a property right—as opposed to a personal right—in movable assets created by agreement—as opposed to by statute or judgment. A security agreement will create a security interest provided that the grantor has rights in the asset to be encumbered or the power to encumber it.<sup>52</sup> As the UNCITRAL Model Law applies to security devices, such as outright assignment of receivables and financial leases, the grantor may have the power to create security in favor of other secured creditors.<sup>53</sup> Creation has *inter partes* effect. A security interest fastens onto the asset so as to give the creditor *rights in rem* against the debtor himself, but not necessarily against third parties. Until that security interest is perfected, it will not be effective against third parties. Therefore, creation is also a necessary element of priority. The grantor has the right to use its future assets as collateral too. This is a normal feature of modern secured transactions laws. Future assets are those assets on which the grantor acquires rights or the power to encumber after the time of the conclusion of the security agreement. In this case, the security interest is created at that later time.<sup>54</sup>

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47. MODEL LAW, *supra* note 7, at ch. II, art. 8.

48. LEGISLATIVE GUIDE, *supra* note 39, at ch. II, ¶¶ 63–69.

49. Proceeds is defined under the Model Law as follows: "Proceeds" means whatever is received in respect of an encumbered asset, including what is received as a result of a sale or other transfer, lease, license or collection of an encumbered asset, civil and natural fruits, insurance proceeds, claims arising from defects in, damage to or loss of an encumbered asset, and proceeds of proceeds." MODEL LAW, *supra* note 7, at ch. I, art. 2(bb).

50. ENACTMENT GUIDE, *supra* note 41, ¶ 97.

51. LEGISLATIVE GUIDE, *supra* note 38, rec. 1(c).

52. For a comparison to another model code, see U.C.C. § 9-203(a) (AM. LAW INST. & UNIF. LAW COMM'N 1977) ("A security interest attaches to collateral when it becomes enforceable against the debtor, with respect to the collateral, unless an agreement expressly postpones the time of attachment.")

53. ENACTMENT GUIDE, *supra* note 41, ¶¶ 83–85.

54. LEGISLATIVE GUIDE, *supra* note 38, recs. 13–14; MODEL LAW, *supra* note 7, at ch. II, art. 6(2); ENACTMENT GUIDE, *supra* note 41, ¶ 87; *see also* U.C.C. § 9-204; New Zealand Personal Property

Registration of an effectively created security interest in a publicly accessible registry is an important method. This provides a neutral, cost- and time-efficient method of ascertaining the rights and positions of other creditors—or potential creditors—of the grantor. It is also instrumental in enabling potential creditors in deciding whether to lend or not.<sup>55</sup> Registration as a method of achieving third party effectiveness, or perfection, is a feature of modern secured transactions laws.<sup>56</sup> The UNCITRAL Model Law separates creation from the third party effectiveness of a security interest. Therefore, an additional step needs to be taken in order to make a validly created security interest effective against third parties. These third parties include other secured creditors, buyers of the encumbered assets, judgement creditors, and the insolvency administrator. While creation may not necessarily be known by third parties, transparency is also achieved with an additional step such as registration in a general rights registry or possession or registration in a specialized registry. By putting third parties on notice with the performance of the additional step, potential third party creditors are given the opportunity to decide whether to extend credit or not.<sup>57</sup> The UNCITRAL Model Law's registration rules apply to all types of debtors irrespective of their status as incorporated, unincorporated, or as individuals.<sup>58</sup>

A created security right will become effective against third parties if a notice of it is registered in the general security rights registry. Modern principles stipulate that registration of such a notice does not create a security right and is not necessary for the creation of a security right. Therefore, the registry system is (1) a method by which an existing or future security right in a grantor's existing or future assets may be made effective against third parties, (2) a basis for priority rules that depend on when third party effectiveness of a security right is achieved through registration, and (3) an objective source of publicly-accessible information for third parties dealing with a grantor's assets to assess whether such assets may be encumbered by a security right. The registry system should provide simple, time- and cost-efficient, user-friendly, and publicly-accessible registration and searches. Under different systems, registration can either be done on a notice

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Securities Act 1999, §§ 43–44 [hereinafter NZPPSA]; *Holroyd v. Marshall* [1862] 11 Eng. Rep. 999; *Tailby v. Official Receiver* (1888) 13 App. Cas. 523.

55. See also L. COMM'N, REGISTRATION OF SECURITY INTERESTS: COMPANY CHARGES AND PROPERTY OTHER THAN LAND, 2002, CP No. 164 (UK); L. COMM'N, REGISTRATION OF SECURITY INTERESTS: COMPANY CHARGES AND PROPERTY OTHER THAN LAND, 2004, CP No. 176 (UK); WORLD BANK, *supra* note 2.

56. See, e.g., U.C.C. art. 9, pt. 3; NZPPSA, pt. 4; Ontario Personal Property Security Act, R.S.O. 1990, c. P. 10, pt. III (Can.).

57. See LEGISLATIVE GUIDE, *supra* note 38, recs. 1(c), 1(f) (recommending that secured transactions law “enable[s] parties to obtain security rights in a simple and efficient manner” and “enhance[s] certainty and transparency by providing for registration of a notice”).

58. *But cf. supra* note 27 (security interests under English law can only be taken over an incorporated businesses' assets, and company charges do not apply to individuals or partnerships).

basis<sup>59</sup> where registration can be made in advance of creation, or on a transaction filing basis<sup>60</sup> where the security right needs to be created first before registering it. Both Personal Property Security Act (PPSA) and UCC Article 9 type systems treat filing as a priority point whereas the English system treats filing as only perfection requirement.<sup>61</sup>

The UNCITRAL Model Law provides a set of rules with regards to the establishment and the necessary mechanism of the Registry system.<sup>62</sup> This is a useful guide to the legislators together with the other works of the UNCITRAL Model Law.<sup>63</sup> There are two types of general registries: debtor-based and asset-based. General registries are normally debtor-based where security interests created by the debtor are shown registered under the name of the debtor or his or her trading name.<sup>64</sup> There are two types of registration systems: transactions- or documents-based, and notice-based. Transactions-based registration is used in England. An effectively created security transaction needs to be registered in the Companies House within twenty-one days in order to achieve third-party effectiveness. Therefore, advance or notice filing is not possible as the copy of the transaction needs to be uploaded on the registration system.

On the other hand, notice-based registration is widely used in modern secured transactions regimes—including the UCC Article 9 and the PPSAs—and has been supported by the Legislative Guide and the Cape Town Convention on International Interests in Mobile Equipment.<sup>65</sup> It is possible to have an advance registration<sup>66</sup> under a notice registration system, whereby a limited amount of information is registered in advance of creation of the security interest. This information includes the identifier and address of the grantor and the secured creditor, a description of the encumbered assets and the period of effectiveness

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59. The Personal Property Security Acts and U.C.C. Article 9 systems have notice based registration where filing can be done in advance and only single filing is required for all transactions between the same parties involving the same class of collateral.

60. The English perfection system is based on transaction filings, whereby validly created security agreements are filed to achieve third party effectiveness. Advance filing is not possible. Secured creditor needs to file the agreement within twenty-one days after the creation of the security interest. Twenty-one days start from the day after the creation of the security interest. Under the European Bank for Reconstruction and Development (EBRD) Model Law on Secured Transactions (1994), this period is thirty days whereby a registered charge is created by entering into a charging instrument and registration of that instrument at the Registry. EBRD Model Law on Secured Transactions (1994), art 8.

61. *E.g.*, GERARD MCCORMACK, SECURED CREDIT UNDER ENGLISH AND AMERICAN LAW 76 (2004).

62. MODEL LAW, *supra* note 7, at ch. 4, art. 28.

63. U.N. COMM'N ON INT'L TRADE L., UNCITRAL GUIDE ON THE IMPLEMENTATION OF A SECURITY RIGHTS REGISTRY, U.N. Sales No. E.14.V.6 (2014); LEGISLATIVE GUIDE, *supra* note 38.

64. But Cape Town Convention's registries under its protocols (aircraft, MAC, railway rolling stock, space objects) are asset-based registries, which contain all registrable interests but for that it is necessary to have the unique identification/serial number of the asset. Thus, a generic description is not possible. It is also not possible to register after acquired property in asset-based registries as unique identification is necessary.

65. LEGISLATIVE GUIDE, *supra* note 38, at ch. IV, ¶ 14.

66. MODEL LAW, *supra* note 7, at ch. IV, art 4.

of the registration, and the maximum amount for which the security interest may be enforced.<sup>67</sup> The significance of having a notice-based registration system with the advantage of advance registration is that a registration system inherently provides notice to third parties of the existence of a potential secured creditor before the interest's creation as well as an important knowledge and warning source to determine whether some assets of the grantor may be encumbered by an earlier security interest. It is also a priority point under UCC Article 9 and PPSA systems. This simplifies the registration process by reducing the administrative burden, delays, and costs. It also minimizes the risk of error and liability on the part of registrar as well as the secured creditor.<sup>68</sup> Furthermore, for confidentiality reasons and in order to minimize the risk of financiers or lenders searching competitor secured creditors, who may register their representatives,<sup>69</sup> the registry provides that the search can only be done by searching the name or identifier of the grantor or the registration number.<sup>70</sup> Therefore, a publicly-accessible general registry system provides a clear financial picture of the grantor to the secured creditors. This in turn enables the grantor to have access to low-cost credit. The registry system is also part of the robust credit infrastructure promoted by the World Bank.

Obtaining priority is an expectation for the secured creditor. Secured credit is a bargain.<sup>71</sup> In return for a priority position in case of insolvency of the grantor or debtor, it is a fair bargain that the secured creditor extends credit with low interest rates and takes collateral as security. There should be clear and simple rules to ascertain priority. Achieving priority is a key objective of both the Legislative Guide<sup>72</sup> and the UNCITRAL Model Law whereby the law should provide clear rules between competing claimants—secured creditors and asset-based lenders alike—having rights on the same encumbered asset.<sup>73</sup> The UNCITRAL Model Law provides that in a conflict between two security

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67. LEGISLATIVE GUIDE, *supra* note 38, rec. 57; MODEL LAW, *supra* note 7, at ch. IV, art. 9.

68. LEGISLATIVE GUIDE, *supra* note 38, at ch. IV, ¶¶ 10–14. In relation to the possible use of blockchain based registry system see, for example, Charles W. Mooney Jr., *Fintech and Secured Transactions Systems of the Future*, 81 LAW & CONTEMP. PROBS. no. 1, 2018, at 1 (arguing that a blockchain based registry system might be best suited for private registries as opposed to public ones).

69. LEGISLATIVE GUIDE, *supra* note 38, rec. 57(a); *id.* at ch. IV, ¶ 30; MODEL LAW, *supra* note 7, art. 9(2), 10.

70. LEGISLATIVE GUIDE, *supra* note 38, recs. 54(h), 58–60; MODEL LAW, *supra* note 7, art. 22. For the rationale of this approach, see LEGISLATIVE GUIDE, *supra* note 38, at ch. IV, ¶¶ 29–30.

71. See, e.g., Ronald Mann, *Explaining the Pattern of Secured Credit*, 110 HARV. L. REV. 625 (1997); ORKUN AKSELI, INTERNATIONAL SECURED TRANSACTIONS LAW: FACILITATION OF CREDIT AND INTERNATIONAL CONVENTIONS AND INSTRUMENTS (2011); GERARD MCCORMACK, SECURED CREDIT UNDER ENGLISH AND AMERICAN LAW (2004); See also *Symposium: The Priority of Secured Debt*, 82 CORNELL L. REV. 1279 (1997); KATHARINA PISTOR, THE CODE OF CAPITAL: HOW THE LAW CREATES WEALTH AND INEQUALITY 13 (2019) (pointing out that property rights confer title to an owner and allow her to remove an asset she owns from the pool of assets that are in the possession of a bankrupt debtor, no matter how loudly other creditors might protest).

72. LEGISLATIVE GUIDE, *supra* note 38, rec. 1(g).

73. MODEL LAW, *supra* note 7, at ch. I, art. 2(e).

interests in the same asset, the first perfected one by registration or otherwise has priority.<sup>74</sup>

Access to credit is further improved through priority competition between an asset-based financier and an earlier secured creditor who has taken security interests over the present and future assets of the small business. Generally, a small business' main collateral is its receivables. Small businesses borrow on a secured basis; whereas, large firms borrow on an unsecured basis.<sup>75</sup> In some cases, where the small business is not in the form of a company, it may not be able to grant charge over its inventory.

One alternative to bank financing for small business is to utilize asset-based financing. Enabling a small business to choose between a secured creditor and an asset-based lender creates a competition between financiers. This allows the small business to have better financing terms and affordable credit by not providing a collateral from its pool of assets. Purchase money security interest (PMSI) is a crucial financing device, where the debtor is given value by the asset-based financier to acquire rights in or the use of collateral and the value is used for that purpose. The idea behind PMSI is to eliminate the situational monopoly of an earlier secured creditor who has taken security over the present and after acquired assets of the grantor. Therefore, PMSI enables the grantor to have further access to credit from other sources and promotes competition among providers of credit on the basis of price and other terms of the loan transaction.<sup>76</sup> Moreover, PMSI structure does not disadvantage the earlier secured creditor because the asset-based financier is given priority in relation to the specific property acquired.

Recognizing the priority of an asset-based financier against a prior security right with an after-acquired property clause might enable small businesses to have better access to asset-based finance. That is to say, enabling businesses to have access to competing financing options is said to reduce the cost of credit.<sup>77</sup> The issue arises when a small business borrows from a lender who takes a charge over the present and after acquired property of the small business before an asset-based financier lends for the purposes of purchasing a specific property or supplies equipment to the same small business. If the small business is unable to obtain additional financing from the secured creditor, a potential priority conflict may occur. The general rule on priorities between non-possessory security interests under English law is that the security interest created first in time

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74. *Id.* at ch. 5, art. 29.

75. LAW COMM'N, *supra* note 44.

76. The objective is to provide for equal treatment of diverse sources of credit and of diverse forms of secured transaction. Indeed, this is one of the Key Objectives of the UNCITRAL Legislative Guide as well as the Model Law.

77. See, e.g., LEGISLATIVE GUIDE, *supra* note 38, at ch. I, ¶ 52 (“[O]pen competition among all potential credit providers is an effective way of reducing the cost of credit.”).

obtains priority, although there are exceptions.<sup>78</sup> Whereas if the super-priority position of the asset-based financier were recognized, the priority would be based on the type of the security right rather than the time of registration or creation. Unless a subordination agreement is agreed upon between the secured creditor and the asset-based financier, the latter might not be willing to extend credit. This could be a particular problem for small businesses that are new to the market—and thus have no credible credit history and present information asymmetry problems—or too small to be able to provide additional collateral. For this reason, it could assist a small business to have access to competing financiers, if the super-priority position of the asset-based financier were recognized. Previous law reform initiatives on secured transactions law have offered justifications that the asset-based financier should be granted a super-priority status.<sup>79</sup> A super-priority position is offered to the asset-based financier under a number of modern secured transactions laws.<sup>80</sup>

The UNCITRAL Model Law also attempts to increase access to credit by focusing on the efficiency of enforcement mechanisms. Efficient and effective enforcement mechanisms are significant in the credit decision-making. Secured creditors would like to have confidence in the enforcement system that they will be able to satisfy their claims. Delays or excessive costs in the enforcement of security interests will be likely to affect the availability and the cost of credit.<sup>81</sup> Furthermore—as enforcement mechanisms are embedded into national systems and are not international, and judicial enforcement regimes cannot be easily harmonized at the international level—there is a need to establish neutral concepts and mechanisms to enforce debts. The UNCITRAL Model Law's approach in this regard is that enforcement before a court or other authority is left to national laws. It recommends expedited proceedings.<sup>82</sup> These include extra-judicial enforcement mechanisms or out-of-court or self-help remedies mechanisms. They also provide safety mechanisms both for the grantor and secured creditor as well as other parties with interests in the encumbered asset.

As detailed above, the UNCITRAL Model Law increases access to credit in various ways such as: having a functional and comprehensive approach, allowing

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78. See HUGH BEALE, MICHAEL BRIDGE, LOUISE GULLIFER, & EVA LOMNICKA, *THE LAW OF SECURITY AND TITLE-BASED FINANCING* 464–65 (2d ed. 2012).

79. See, e.g., THE LAW COMMISSION, *supra* note 44, ¶ 4.159 (explaining why a purchase-money interest should be protected while someone “who had simply lent money that has been used to reduce a company's indebtedness should not be protected”).

80. See, e.g., U.C.C. § 9-324; NZPPSA, *supra* note 54, §§ 73–77; LEGISLATIVE GUIDE, *supra* note 38, recs. 178–180, ch. IX, ¶ 123; MODEL LAW, *supra* note 7, art. 38–39.

81. LEGISLATIVE GUIDE, *supra* note 7, at ch. VIII, ¶ 6.

82. For the use of ADR in the enforcement of security interests, see, for example, Orkun Akseli, *Mediation in Disputes Arising in the Context of Enforcement of Security Interests*, 22 UNIF. L. REV. 747 (2017); Maya Boureghda Chebeane, *Alternative Dispute Resolution (ADR) and Secured Transactions*, 22 UNIF. L. REV. 773 (2017); Nina. P. Mocheva & Angana R. Shah, *Mediation in the Context of (Approaching) Insolvency: A Review on the Global Upswing*, TRANSNAT'L DISP. MGMT., Nov. 2017, at 1.



parties to create security interests in an efficient manner, encouraging simple and effective registration rules, enabling businesses to have access to competing financing options, and recommending efficient enforcement mechanisms.

#### IV

#### CONCLUSION

Financial inclusion and access to credit are important elements and milestones in achieving financial sustainability. The work of the UNCITRAL in the modernization of secured transactions law has directly and indirectly influenced law reforms around the world.<sup>83</sup> The Secured Transactions Guide, the Model Law on Secured Transactions, and other texts, including the IP Supplement and the Registry Guide, have become the main reference tools for law reform activities. The UNCITRAL Model Law is a useful legislative text for both developing and developed economies. If the law is transparent and provides clear and predictable rules for the grantor and the creditors, it will be easier to achieve a robust credit infrastructure. This will support financial sustainability and inclusive access to finance by including individuals and partnerships in secured lending, in addition to companies, and by extending credit at affordable rates.

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83. *UNCITRAL Model Law on Secured Transactions (2016) – Status*, UNCITRAL, [https://uncitral.un.org/en/texts/securityinterests/modellaw/secured\\_transactions/status](https://uncitral.un.org/en/texts/securityinterests/modellaw/secured_transactions/status) [<https://perma.cc/AA57-8ULQ>].