

UNIFORM COMMERCIAL CODES

Bringing Business to Indian Country

Tribal Secured Transactions Laws

A Working Forum

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Agenda

Morning session

- Comprehensive Overview of Secured Transactions Laws
- Secured Transactions Laws in Indian Country Today

Afternoon Session

- State UCC Filing Office
- The Tribal Perspective
- Interactive Workshop
 - Reviewing Your Tribe's Current Legal Environment for Secured Transactions
 - Developing an Implementation Plan

Barriers to Business in Indian Country

- Many contributing factors
- Differ from Tribe to Tribe, case-by-case
- Some commonly cited key contributors:
 - Shortage of lending institutions in Indian Country
 - Poor credit scores
 - Lack of banking experience
 - Perceived or actual issues with tribal courts
 - Incomplete, outdated or no tribal laws that facilitate financing; or lack of awareness about such existing tribal laws

Why is this a barrier?

- In business, rules are needed so that creditors (such as lenders and sellers of goods on credit) and debtors (businesses and consumers) know what to expect
- No rules or unfamiliar rules = uncertainty
- Uncertainty = risk = increased cost or no deal
- The same is true with doing business in Native communities - the “rules” are necessary
- Laws are the rules; they are necessary for communities to effectively support business activities

Tribes' general right to govern business in their jurisdictions

- Commercial codes govern many aspects of business transactions in state jurisdictions
- For all states and several U.S. territories, many of these laws constitute and are commonly referred to as the Uniform Commercial Code (UCC)
- As a matter of sovereignty, Tribes generally have the same right as states to establish similar laws that govern commerce/business within their jurisdictions – this is also true for Tribes in PL 280 states

What is the Uniform Commercial Code?

- UCC was drafted by the Uniform Law Commission (ULC) and American Law Institute (ALI) during the 1940s and 1950s – a set of model codes to establish a **reasonably consistent** legal environment for commercial transactions among and between businesses and consumers across state lines
- The UCC is a set of template codes developed as a resource for use and enactment by state legislatures
- UCC been enacted by all 50 states and some U.S. territories - not exactly uniform but **substantially uniform**

State of Tribal Commercial Law Today

- Have Tribes enacted these kind of laws?

Some have, but with little consistency from Tribe to Tribe

- What if a Tribe has not adopted these types of laws?

State law typically fills the void, but often without certainty and with a great deal of confusion

Why did the States Adopt the UCC?

- **Economic development:** Non-uniformity among state laws was hindering “cross-border” commerce, thus interfering with economic development
- **Sovereignty:** Concern by states for potential federal legislative intervention/preemption if states did not act to address the non-uniformity issue
- Now, **substantial uniformity** among the states’ commercial laws, including those governing secured lending, permits ease of transactions across state lines, enabling efficient “cross border” commerce

Are there similar concerns about economic development and sovereignty in Indian Country?

12 Articles of the UCC

- Article 1 Definitions and General Rules
- Article 2 Sales
- Article 2A Leases
- Article 2B Licenses
- Article 3 Negotiable Instruments
- Article 4 Bank Collections
- Article 4A Funds Transfers
- Article 5 Letters of Credit
- Article 6 Bulk Sales
- Article 7 Documents of Title
- Article 8 Investment Securities
- Article 9 Secured Transactions

Secured transactions legal developments around the world

- Most, if not all, free market economies around the world have secured transactions laws, or have initiatives to enact or modernize them, in order to facilitate the flow of credit for business development and some consumer purposes
- Because access to credit is necessary for business, developing and emerging nations have made adoption of secured transactions laws an important objective for economic development purposes

Secured transactions legal developments around the world

- See, for example, a 2010 World Bank Study entitled *Secured Transactions Systems and Collateral Registries* at <https://www.wbginvestmentclimate.org/uploads/SecuredTransactionsSystems.pdf>

Secured transactions legal developments around the world

- See also United Nations Commission on International Trade Law (**UNCITRAL**)
 - Has identified secured transactions law as a key foundational need for economic development
 - Has developed a legislative guide to help nations develop such laws and registry (filing) systems
 - The principles in the guide are highly consistent with Article
 - UNCITRAL is in the process of drafting a model ST law
 - The legislative guide may be found at www.uncitral.org/uncitral/search.html?q=secured+transactions

Secured transactions legal developments around the world

- A few examples of the more than thirty countries currently developing or reforming their secured transactions legal regimes
 - **Middle East:** Yemen, Jordan, Afghanistan, Palestine
 - **Asia:** India, China, Sri Lanka, Laos, Philippines, Indonesia
 - **Africa:** Sudan, Ghana, Malawi, Nigeria, Rwanda
 - **Central Asia:** Azerbaijan, Kyrgyzstan
 - **Latin America:** Columbia, Guatemala, Haiti, Peru, El Salvador
- Many other countries have expressed interest
- The development of modern, comprehensive secured transactions regimes has become a global movement **to help facilitate development through improved access to business and consumer credit**

Secured transactions legal developments around the world

- See also an article in **EconSouth**, a publication of the Federal Reserve Bank of Atlanta's *Americas Center*, Third Quarter 2012 issue, entitled **“Secured Transactions Reform: Moving Ahead with Movable Assets”**
- http://www.frbatlanta.org/pubs/econsouth/12q3_summary_secured_transaction_reform.cfm

Two broad categories of secured credit

- Using **real property** (land or things attached to land) as collateral – think of the broad category of “mortgage lending”
- Using **personal property** (everything other than real property) as collateral – secured transactions lending and other credit

NOTE: A secured transactions law does not generally deal with real property (with some exceptions)

Examples of personal property

- **“Movable” property** (equipment, inventory, cut crops, cut timber or under contract to be cut, livestock, minerals/gas/oil removed from the ground, etc.)
- **Payment obligations and financial instruments** (accounts receivable, bank accounts, investment securities, letters of credit, documents of title, etc.)
- **General intangibles** (licenses, copyrights, patents, trademarks, etc.)
- **Fixtures** (property that has attributes of both personal and real property, such as an installed water heater or furnace)

Example: secured transaction (possessory security interest or “pledge”)

- Bill gives Sam a loan of \$100
- Sam gives Bill his leather jacket (approx. value \$100) to hold on to until Sam repays the loan as assurance that Sam will repay (the jacket is the collateral)
- The collateral has been “pledged” to Bill (physically given to him – a **possessory** security interest)
- When Sam fully repays Bill, Bill returns the jacket
- If Sam defaults under the terms of their agreement, Bill may sell the jacket and keep the amount of the sale proceeds needed to pay off the remaining balance of the loan

Example: secured transaction (non-possessory security interest)

- Bill gives Sam a loan of \$100
- Sam signs a **security agreement** (contract) giving Bill a **security interest** (a type of lien) in Sam's leather jacket
- Bill now has a **nonpossessory** security interest in the jacket - he does not have the jacket in his possession
- Sam may continue to use his jacket because he has possession of it
- Upon repayment, Bill no longer has a security interest in the jacket
- If Sam fails to repay under the terms of the agreement, Bill may repossess the jacket, sell it, and keep the sale proceeds to pay off the remaining balance of the loan

Why are non-possessory security interests important?

- The ability of a debtor to give a non-possessory security interest in property to a creditor as collateral to secure a loan or other extension of credit allows the debtor (or other obligor such as a surety) to continue to use the collateral while there is a security interest attached to it
- For example:
 - Inventory for sale
 - Equipment needed to run a business
 - Consumer items such as a car purchased on credit

This is how secured transactions laws enable credit to more readily flow

What is secured transactions law?

- Set of contract and property-based rules governing creditor-debtor transactions (such as collateralized loans and purchases on credit)
- Using personal property as collateral to secure the loan or other extension of credit
- By agreement between the parties as opposed to liens arising as a matter of law (such as a construction lien or mechanics lien) or by order of a court (a judicial lien)

Secured transactions laws determine:

- When and how a debtor gives a security interest (a type of lien) in the debtor's collateral (the mechanics of the transaction)
- A creditor's rights in relation to third parties that also have a legal interest in the same property (e.g., trustee in bankruptcy, other secured creditors or lien holders)
- Remedies available to a creditor if the debtor defaults
- Protections for the debtor to ensure remedies are fair and fairly applied

Example: Consumer Secured Transaction

- Mary buys a washer and dryer on a payment plan from Sears
- She signs a contract with Sears Financial Corporation to make payments for one year
- She takes delivery of the washer and dryer immediately
- Sears Financial Corporation retains a security interest in the washer and dryer until Mary has paid in full
- If Mary defaults, Sears Finance may repossess the washer and dryer

Example: Business Secured Transaction

Native Saddle Corporation (NSC)

- manufacturer located on "x" Reservation
- owned by Dale and Joe, brothers and sole shareholders
- Dale is president and CEO
- saddles are sold retail

Secured loan from Lender

- extends \$10,000 operating line of credit to NSC
- secured by inventory, equipment and accounts receivable of NSC (presently owned and after-acquired)
- security agreement (contract) signed specifying line of credit terms such as
 - payment terms
 - what constitutes a default
 - description of collateral

Personal Guaranty

- Also, Dale and Joe each sign a personal guaranty of repayment up to \$2,500 each to ensure NSC's repayment

Secured Transactions Law

- fills in the details of the contractual arrangements
- provides process for "perfecting" the security interests in the collateral
- specifies what Lender can do if NSC defaults
- identifies whether Lender's security interests in the collateral are valid
- sets forth processes Lender must use if there is a default
- identifies Dale and Joe's obligations
- sets forth protections for NSC and for Dale and Joe

Secured Transactions Laws in Indian Country Today

- Some Tribes have no secured transactions law – state law is the default (often per boilerplate contract language)
- Some have comprehensive but unique secured transactions laws
- Some have adopted the Official Text UCC Article 9
- Some have adopted Article 9 as enacted by the state in which their Tribe's jurisdiction is located

Secured Transactions Laws in Indian Country Today

- Some Tribes have adopted by resolution the version enacted by the states in which their respective jurisdictions are located for single transactions
- Some have only components, such as collection codes governing repossession
- Some have adopted “pre-revision” model tribal versions or state versions (e.g., the Montana Tribal Secured Transactions Code – drafted 1997)

Debunking the Myths

- Are we just adopting laws appropriate only for states?
- Does enactment of such a law impact tribal sovereignty, self-determination, self-governance?
- Does this law favor lenders and other creditors? In other words, are tribal consumers and business borrowers better off if a Tribe does not have a secured transactions law?
- Does a secured transactions law just apply when a tribal consumer, tribal business enterprise, or independent Native-owned business within the Tribe's jurisdiction does business with an outside lender or business?

Benefits of a Secured Transactions Laws for Tribes

Why would my Tribe want to enact a secured transactions law? What are the benefits?

- Creates certainty and predictability regarding the rules for all parties
- May encourage more lenders to do business with Tribe, Tribal members, individual Native-owned businesses
- A Tribe's choice to enact a law that is reasonably uniform with state laws may reduce the cost of transactions
- Exercise of sovereignty

Secured Transactions Law Models

- Tribes may adopt Article 9 as enacted by the state in which the Tribe's jurisdiction is located

CAUTION: If a Tribe opts to adopt state law, it should be done explicitly (by resolution, in full text, or by incorporating it by reference). It should also be carefully adapted to ensure it is appropriate throughout for the Tribe's jurisdiction. For example, are there provisions in the state's law that are not appropriate, are not applicable, or do not work with other tribal law?

Secured Transactions Law Models

- Tribes may adopt the Official Text UCC Article 9

CAUTION: The Official Text UCC Articles are not complete in and of themselves. They are simply template laws, and have many “blanks” that need to be completed and filled in. If a Tribe adopts the Official Text UCC Article 9 by reference or resolution only, the law will be full of “holes” and incomplete

Secured Transactions Law Models

- Tribes may enact their own unique version of a secured transactions law

CAUTION: If a Tribe adopts its own unique version of a secured transactions law, it should ensure that it will be reasonably uniform to state law to avoid the costs and concerns attendant to non-uniformity

Secured Transactions Law Models

- Tribes may utilize a model tribal law, such as the Uniform Law Commission's Model Tribal Secured Transactions Act

CAUTION: The Model Tribal Secured Transactions Act is an excellent model for Tribes. Nevertheless, it must be appropriately and carefully adapted to ensure it addresses important policy and cultural issues.

ULC's Model Tribal Secured Transactions Act (MTSTA)

- ULC Committee on Liaison with American Indian Tribes and Nations
- Drafting committee comprised of more than a dozen commissioners, including several that worked on 1999 revisions to Official Text Article 9 (adopted by all states), representatives from 10 Tribes, other advisors with experience in Indian Country legal/development issues
- Drafting effort took four years; completed in August 2005

MTSTA History

- MTSTA is largely based on revised Article 9, with relevant components of Articles 1, 2 and 8 (where UCC Article 9 incorporates provisions from these Articles by reference)
- **Purpose:** To offer a tribal template “stand-alone” code that, if other UCC Articles are subsequently adopted, will still harmonize (or blend) with those Articles
- MTSTA was drafted to address unique tribal issues while at the same time ensuring familiarity for and ease of use by lenders and other creditors
- Intended to help reduce “cross-border” transaction concerns

MTSTA Special Considerations and Provisions

- No affect on sovereign immunity
- “Fixtures” attached to trust land (outside of this law)
- Possible exemptions from covered property (i.e., sacred items)
- Consumer protections – limitation on choice of law
- Manufactured homes – interim financing
- Coordination with other tribal law
- Tribal customs and traditions (i.e., tribal business day)
- Treatment of self-help remedies (self-help repossession?)
- Choice of law and venue issues
- Implication of tribal liens

NOTE: This list is not exhaustive – just a sampling

MTSTA Benefits for Tribes

- Significant code development cost savings
- Revision benefit – can take advantage of ULC revision efforts
- Reduces “incorporation by reference” of other state law
- Implementation Guide

MTSTA Implementation Guide

- Plain language provision-by-provision commentary and examples
- Enactment guidance for tribal legislative bodies
- Optional provisions with explanations (policy issues)
- UCC filing system options explained
- Educational tool for tribal attorneys and judges, economic and business development staff, lenders and others

What are UCC Lien Filing Systems?

- Public notice system of security interests
- Sometimes called secured transactions registry systems, central indexing systems, clerk's information systems, to name a few
- Provides a way to determine priority between competing creditors
- Enables creditors to search for existing security interests in a debtor's property before agreeing to accept as collateral
- **Note:** a debtor may give security interests in the same collateral to multiple creditors (e.g., senior and junior lien holders)

UCC Filing Systems Establish Creditor Priority

Let's go back to Bill and Sam, and bring in Joe:

- Sam signs a security agreement (contract) giving Bill a security interest in Sam's jacket to secure a loan
- Bill does not file a financing statement in the UCC filing office
- A month later, Sam also gives Joe a security interest in the jacket secure a loan from Joe
- Joe files a financing statement in the appropriate filing office describing the collateral and debtor
- Sam defaults under the terms of both agreements

Who will have priority in the collateral?

Purpose of a UCC lien filing system

- Filing systems are necessary to determine priority between competing creditors and to determine whether collateral is encumbered with prior liens by other creditors
- Filing systems are indispensable components of a secured transactions system – **they are the heart of secured transactions systems**
- **Without a robust, reliable and easily accessible filing system, a secured transactions law is not complete, and therefore will not be effective**
- They should **not** be considered as fee income opportunities. Fees should cover costs of the system (state filing fees typically range from \$5 to \$30)

Options for UCC Filing Systems under Tribal Law

- Tribe develops and manages its own filing system
- Multiple Tribes develop and maintain a filing system as a consortium
- Tribe informally utilizes state system
- Tribe enters into a formal agency arrangement with a state
 - Crow Nation and State of Montana
 - Oglala Sioux Tribe (Pine Ridge Reservation) and State of South Dakota
 - Leech Lake Band of Ojibwe and State of Minnesota
 - Chippewa Cree Tribes (Rocky Boys Reservation) and the State of Montana

Reviewing Your Tribe's Secured Transactions Environment

- Does your Tribe have a secured transactions code?
 - When was it adopted?
 - Is it complete? partial? (e.g., repossession provisions only)
 - Is it another jurisdiction's law incorporated by reference or adopted by resolution of the tribal council or executive branch?
- Is it easily accessible to outside parties - for example, online?

Reviewing Your Tribe's Secured Transactions Environment

- If your Tribe has a ST law, where is the designated location for filing security interests? Conducting UCC searches?
 - Tribal office?
 - County office?
 - State?
- If in a tribal office, how are filings made? Paper or electronic? Are there special forms? Fees? How is it administered? How many filings have been made? How are UCC searches administered?

Important Implementation Considerations

- Ensure law-makers, policy-makers and other key stakeholders are educated about the code's purpose and objectives - *who do you need to engage in the discussion?*
- Involve key stakeholders in addressing policy issues in the code to ensure Tribe's law is culturally appropriate and tailored for your Tribe's business environment – *do you need to engage legal counsel to assist?*

Important Implementation Considerations

- Consider what may be the most appropriate filing system option for your tribe, an implementation plan for the filing system, and a maintenance plan (funding, trained staff, public search capabilities, etc.) – *does your Tribe have the capacity to host its own robust filing system?*
- Avoid adopting another Tribe's law without careful consideration of cultural issues, date of enactment, and source of the law (for example, pre-revision state law)
- Avoid conflicts of interest in drafting

Avoiding Conflicts of Interests

- Sometimes tribal judges are sought out to draft codes for their Tribes because of their legal expertise
- However, there is an inherent conflict of interest when someone participates in both legislative and judicial duties *in the same jurisdiction*
- It is usually not a good practice to have a law drafted by someone who may be called upon to interpret that law in a legal dispute
- This may be considered a violation of tribal constitutional separation of powers *in fact* or *in principle*

Other Important Initiatives and Considerations

- Tribal Judicial /Legal Training Workshops
 - 1 ½ day training sessions for tribal judges and attorneys were hosted by BIA's Office of Tribal Justice Services and the Federal Reserve Banks of Minneapolis, San Francisco and Kansas City. A ULC Commissioner was the principal lecturer. CLE credits available.
 - **Seattle:** January 30-31, 2013
 - **Minneapolis:** May 8-9, 2013
- MTSTA Tribal Training Workshops
 - For tribal leaders, finance officers and economic development staff - have been held in numerous locations around the country by the FRB of Minneapolis, supported by several other FRBs, the SBA, and the Department of the Interior's Office of Indian Energy & Economic Development
- Lender Awareness Training
 - FRB Minneapolis has developed and hosted local post-enactment workshop to support tribes that have adopted the MTSTA and established reliable UCC filing system arrangements/processes
- Tribal Community Awareness Training
 - For tribal consumers and business owners
- Publication of Laws and Court Decisions
 - Necessary to ensure easy access by outside parties

Resources

- For the MTSTA, go to www.uniformlaws.org
 - Click on **Acts**, then **Find an Act** in the drop down box
 - Go to **Model Tribal Secured Transactions Act** for downloadable WORD and pdf versions of:
 - Model Act
 - Implementation Guide (for comprehensive information about secured transactions laws, filing systems, legislative and judicial guidance)
 - Crow-Montana Filing System Compact
 - Other related information
- See also the Minneapolis Federal Reserve Bank's **Indian Country Currents** website at www.minneapolisfed.org/indiancountry/ for related articles and working papers

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