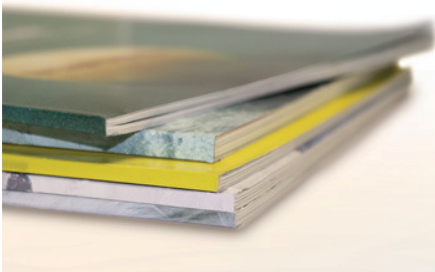


Formal Creation of Jersey Security Interests

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It has been a long time coming but change is going to come. We are on draft 31 of the Security Interests (Jersey) Law 201- (the “Draft Law”) and it is not yet ready to go before Jersey’s legislature, the States of Jersey. Even then, it will take at least another six months before the Draft Law is in force. With grandfathering transitional provisions, lenders still have plenty of time to digest the changes.

Existing Formalities for Valid Security

Let’s start with a brief recap of the existing requirements. All security interest agreements over intangible assets in Jersey currently must comply with certain formalities set out in the **Security Interest (Jersey) Law 1983** (the “Security Interests Law”). Therefore, security interest agreements must now:

- be in writing;
- be dated;
- identify and be signed by the debtor;
- identify the secured party;

- enable the collateral to be sufficiently identified;
- specify the events of default; and,
- enable the secured payment or performance obligations to be sufficiently identified.

Sweeping Aside Existing Formalities?

The Draft Law seems to sweep aside these existing formalities. The definition of “*security agreement*” in Article 1 appears to permit oral and partially written agreements, as does Article 15 which deals with the creation of the security interest. That is not to say there are no requirements for written documentation. For example, under Article 18, which deals with one step of the creation of security interests by the “*attachment*” of security interests to collateral, there is a potential requirement for an agreement “*in writing*” signed by or on behalf of the grantor which contains a description of the collateral sufficient to enable it to be identified. Helpfully, “*in writing*” includes electronic records. However, this potential requirement for an agreement in writing

describing the collateral as above falls away if the lender has possession or control of the collateral. There are other requirements for certain documents to be in writing, for example, an assignment by way of security must be *'by instrument in writing'*.

Events of Default

A key requirement under the current Security Interests Law is to specify the events of default. However, the Draft Law defines events of default as:

- “(a) the failure to pay or otherwise to perform the obligation secured under the security agreement when due; or*
- (b) an event that under the security agreement gives the secured party the right to enforce the security”.*

Thus, theoretically lenders could rely on the first limb of the definition and not bother specifying any other events of default in a written agreement. Also *“obligation”* is not defined in the Draft Law, although references to it are scattered throughout as might be expected. So there is no longer any express requirement to identify the secured payment or performance obligations. So should we expect to see oral or partially written security in future? Should lenders ignore the existing formalities in light of the Draft Law? Absolutely no – they make good contractual sense.

Existing Methods of Creating Security

The Security Interests Law currently lays down particular methods to be used when taking security over different types of collateral. For example, bank

accounts may be secured by the control method when the secured party and the account holding bank are one and the same. Otherwise security is taken over bank accounts by assignment of title to the account and notice given to the third party account holding bank. These particular distinctions are lost in the Draft Law.

To be enforceable against the borrower, the security interest must have an *“attachment”* to the collateral by satisfying all three conditions set out in Article 18 of the Draft Law inter alia: value has been given in respect of the security agreement; the borrower has rights over the collateral or the power to grant rights over the collateral; and either:-

- (i) there is possession or control of the collateral by the lender; or
- (ii) the security agreement is in writing signed by the borrower and containing a description of the collateral that is sufficient to enable the collateral to be identified, as mentioned above.

Thus, *“control”* becomes a central concept in determining *“attachment”* of the security interest to the collateral.

Control

The ways of achieving control over a deposit account or a securities account are set out in Article 3. These include taking control for example:

- by transfer of the account into the name of

the lender with the written agreement of the borrower and the account holding bank; or

- by the borrower and the account holding bank agreeing that the account holding bank will comply with the instructions of the lender; or
- by the lender and account holding bank being one and the same entity (any possible confusion of interests being dealt with in Article 6 of the Draft Law).

In addition control is acquired over a deposit account (but not, it seems, over a securities account) when it is assigned by way of security to the lender.

Security under the current Security Interests Law is taken over shares and other securities, either by possession of certificates of title or by assignment of title with appropriate notice being given to the company issuing the shares or securities. Again under the Draft Law in respect of “*investment securities*” which include shares, units in unit trusts, interests in limited partnerships which are funds and certain related rights, control becomes a central concept for attachment. Control includes having possession of the certificates of title or being registered as the holder with the issuer for investment securities that are certificated. Control is also specified in Article 3 for dematerialised investment securities. (And there are further provisions relevant to control in Article 18 (3).)

Perfection

In addition to attachment, the security has to be “*perfected*” under Article 19 to 28. Perfection helps to achieve priority. For perfection, the lender must: have possession of the collateral for “*documentary intangibles*” (i.e. negotiable instruments and bearer shares); or have control for deposit and securities accounts and investment securities; or to have complied with the new registration requirements for most types of collateral.

Part 8 of the Draft Law establishes the new registration system for security interests, but it should be noted that registration is not compulsory if another method of perfecting the security has been used.

This article has focused on the formal requirements under the Draft Law. However, if enacted in its current form it will make many other radical changes to taking and enforcing security in Jersey which lenders will also need to digest.

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