

FIRST DISCUSSION DRAFT  
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### **Mortgage Note Registry Statute – Discussion Draft**

This is a discussion draft. It is an issue-spotting exercise, not an attempt at resolving open issues or judge-proofing language. It does take positions on issues, but tries to make the alternatives clear, or at least suggests the possibility of an alternative approach.

The drafting style is a rough approximation to ULC drafting style, with comments as well as statutory language. This is necessary for a discussion draft, which must flag alternative approaches, and discuss some subtleties that statutory language cannot easily express. However, it commits many solecisms from a ULC perspective, such as the use of capitals to mark defined terms, and careless cross-references to the UCC. Although the statute is not drafted in federal style, it assumes a single regulator and single registry, which is hard to do on a state level. However, it affects current state law as little as possible.

The approach of this draft is to treat the obligation represented by the deposited notes and transferable records as if they were the original. This is not particularly elegant, and reproduces most of the arcana of UCC Article 3. It also forces the draft to deal with various problems with non-negotiable notes and transferable records. However, this approach has a clean interface with UCC Article 9, creating no new collateral types, with only some relatively easy choice-of-law modifications. It also creates a simple role for the registry: identifying the PETE.

It would be nice to say that this draft merely electronifies current law and practice, but this is not quite true. First, electronification is not a passive process. Information flows and risk allocations are inherently different in a centralized registry, with the registry itself an actor, with potential liability. Second, the existence of a registry, as opposed to physical paper, affects the conflict of laws rules. Finally, this statute makes several policy choices that are not strictly necessary for mere electronification, but may be necessary for a workable system. These are:

- Establishing rights to information.
- Ensuring that a Registrant on the Registry may enforce the associated mortgage if the Obligation deposited with the Registry is enforceable and the person who deposited the Obligation was the person entitled to enforce it.
- Establishing a new set of deposit warranties to protect the integrity of the Registry.

This draft has made two other decisions that should be pointed out here. First, the draft is limited to residential mortgages, although it allows for future expansion to commercial mortgages by regulation. Second, the draft is limited to three kinds of mortgage obligations: those evidenced by a negotiable instrument, a non-negotiable instrument, and a transferable record contained in a Control System. It contemplates paperless obligations (other than transferable records in a control system), but leaves them to regulation. Paperless obligations are far more difficult to address.

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Finally, there were certain issues that we considered, such as escheatment, but did not believe needed to be addressed in this statute. Some of these judgment calls may have been wrong. However, we have flagged any colorable issue that occurred to us, either by drafting as an alternative, or at least raising the issue in comment.

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Subchapter 1: Definitions, Scope, Entities

Part A: Scope, Definitions

Section 101. **Scope** This statute establishes a national Registry for Obligations and governs the operations of the Registry and certain legal consequences of depositing an Obligation in the Registry. The statute applies only to Obligations that are (a) Instruments secured by a Mortgage, (b) Transferable Records maintained in a Control System secured by a Mortgage, or (c) other Obligations [secured by a Mortgage] that the Regulator [and the CFPB jointly] define by Regulation to be Obligations.

**Comment to Section 101**

1. The statute does not require that mortgage obligations be deposited. It seeks to alter the transfer and enforcement of mortgage obligations as little as possible. It seeks to accommodate all aspects of current best practice, except for its reliance on paper documentation. This is not always possible, but it is an aspirational goal of the statute.

2. While the term Obligation is defined in the statute to mean a promise to pay money, section 101 makes clear that the only forms of Obligations that are within the scope of the statute are Obligations that are also Instruments secured by a Mortgage or Transferrable Records in a Control System secured by a Mortgage. The drafters believe that a Person should not be permitted to Deposit a Negotiable Instrument that has been lost, destroyed or stolen but further consideration of this issue is warranted.

3. The section allows for the possibility that the Regulator and the CFPB will expand coverage and include other types of Obligations but the drafters believe that such an expansion requires considerable thought and should not be considered in the first phase of operations of the Registry. As a consequence, this draft of the statute chooses to rely on regulations to decide whether to include paperless notes other than Transferable Records in a Control System. Until such regulations exist, a paperless note that does not satisfy the definition of Transferable Record or that is a Transferable Record but is not in a Control System is not an Obligation that may be Deposited with the Registry.

4. As noted in section 105, this draft does not take a position as to whether the Registry is a federal entity, state entity or private sector entity but it does assume that whatever is created will be national in its reach.

Section 102. **Definitions of Parties**

- ( ) A “Borrower” is an obligor on an Obligation or Deposited Obligation.
- ( ) “CFPB” is the Consumer Financial Protection Bureau.
- ( ) Deposit” means to submit the Obligation, to the Registry for purposes of registration.

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- ( ) “Depositor” with respect to an Obligation, is the Person(s) that Deposits the Obligation into the Registry pursuant to Section 202. Where a Person entitled to make a Deposit uses a Third Party Service Provider to make the Deposit, the Person entitled to make the Deposit, and not the Third Party Servicer, is the Depositor.
- ( ) “Lender” is the initial obligee on an Obligation.
- ( ) “Recording Office” \_\_\_\_\_.
- ( ) “Registrant” with respect to a Deposited Obligation, is the Person identified on the records of the Registry and associated with such Deposited Obligation.
- ( ) “Registry” refers, as the context may demand, to a juridical person or a database maintained by that juridical person.
- ( ) “Regulator” means [Alt 1: an existing agency] [Alt2: a new agency created by this statute].
- ( ) “Servicer” means a Person that is authorized by the Registrant to provide some or all of the following services for the Registrant: maintenance of Borrower payment records, remittance of Borrower payments to the Registrant, maintenance of accounts for payment of taxes and insurance, collection of delinquent payments, modification of loan terms, and approval of transfers of the real property subject to any Mortgage securing an Obligation.
- ( ) A “Successor to a Person” means a Person who has succeeded to substantially all the rights and obligations of the Person by operation of law.
- ( ) A “Third Party Service Provider” is a Person that: (a) performs services for a Depositor or a Registrant under Section 108, or (b) is used by a Depositor in connection with the Deposit of an Obligation in order to satisfy the Registry’s deposit standards as set forth in System Rules or Regulation.

**Comments to Section 102**

5. This draft segregates the definitions by function (like UCC 4, 4A), and does not place them all in one big happy section (like UCC 9). This choice, of course, is only a tentative one. It capitalizes defined terms for clarity, even though this approach is more characteristic of contract drafting than statutory drafting.

6. Future drafts of the statute will need to consider how, if at all, to address obligors, guarantors, and sureties. While these are important issues, the drafters believe that it is important to first get some consensus on the general structure of the statute. Ultimately we will want to consider issues like whether a (pre-deposit) indorser should be treated under the Statute like a Borrower? After all, under the indorser’s obligation of UCC § 3-415, an indorser is liable upon dishonor. Similarly, is an accommodation party a Borrower? An accommodation party can sign as an indorser or [co]maker. Is a

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guarantor, surety, or other secondary obligor whose liability is created off the Instrument (such as with a separate guaranty contract) a Borrower?

7. This draft of the statute does not define the Depositor as the Lender or even a subsequent “person entitled to enforce, person with control, or owner.” The draft introduces a set of Depositor warranties that taken as a whole would mean (if true) that the Depositor is the person entitled to enforce or person with control. The Depositor will warrant to subsequent Registrants [as well as to the Borrower] that the Depositor had the legal rights under state law to enforce the Obligation at the time of Deposit. This warranty sits on top of any rights and defenses under current state law and is important because it is possible that the Depositor was not the PETE when the Obligation was Deposited, in which case the current Registrant will not be PETEs but will have a breach of warranty claim.

8. The statute is meant to accommodate the notion of a joint deposit but more work likely needs to be done in this regard.

9. The choice to use the word “Registrant” was to avoid confusion with ordinary UCC language, such as “Holder.” It is easiest to think of the Registrant as the person entitled to enforce the Deposited Obligation. For deposited Negotiable Instruments and Transferable Records that were in a Control System, the Registrant should be a person entitled to enforce under UCC Article 3 and will make a warranty to that effect. While the statute is written to maximize the likelihood that a Registrant is a PETE, as noted above in comment 2, if the Depositor of the Negotiable Instrument was not a PETE, the statute does not make the Registrant a PETE (but does provide for a new breach of warranty claim against the Depositor). Subsection 203(b) creates an analogous status for deposited Instruments that are not Negotiable Instruments.

10. The definition of Registrant would allow the Registry to recognize more than one Person as the party with the rights set forth in this statute. We believe this approach accommodates current practice but we invite a discussion as to whether this is a place where the statute should deviate from such practice and require in all instances that one and only one Person be entitled to exercise the rights described herein.

11. We have included a definition of “deposit” but are not convinced that it is necessary. We also are not certain that the choice of the word “submit” is accurate – this may depend on whether the statute permits the Depositor to be the entity that destroys the Instrument or whether only the Registry may perform that function.

**Section 103. Definition of Obligations**

( ) A “Control System” is a system (a) employed for evidencing the transfer of interests in a Transferable Record and (b) that is able to reliably establish a person as the person to which the Transferable Record was issued or transferred.

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- ( ) A “Deposited Obligation” is a record of the Registry that identifies an Obligation that has been Deposited with the Registry.
- ( ) A “Mortgage” is a consensual interest in [real][residential] property that secures a debt. The term does not include a lien that secures an obligation owed to a homeowners’ association in a common interest community.
- ( ) “Mortgage Agreement” is a record that creates a Mortgage. [A Mortgage Agreement may or may not be recorded with the appropriate Recording Office.]
- ( ) An “Obligation” is a promissory note or a Transferable Record. The term also includes any other contractual right to payment of money defined as an Obligation by regulations promulgated jointly by the Regulator and CFPB. Subject to Regulations, an Obligation may be in any currency, need not be liquidated, or for recourse, may be secured in part by personal property, and may contain contingencies.
- ( ) [“Residential Property” means real property improved with not more than four dwelling units. The term includes an attached single-family unit, a single-family manufactured-housing unit that is treated as real property under law of the state in which it is located, a time share in residential property if that time share is treated as real property under law of the state in which the property is located, real property on which construction of not more than four dwelling units has commenced, and a single-family unit in a common-interest community. [The term does not include real property that was used or was intended to be used primarily for non-residential purposes such as farming, commercial, or industrial use when a mortgage was created.]]
- ( ) “Transferable Record” has the meaning given in ESIGN § 201 and in UETA § 16 to the extent that such Transferable Record is secured by real property.

**Comments to Section 103**

1. The key term is “Obligation”, which is used here to simply mean a promise by one person to pay money to another. Section 101 makes clear that for purposes of this statute the only forms of Obligations that are covered under the statute in the first instance are Obligations that are also Instruments secured by a Mortgage or Transferrable Records in a Control System secured by a Mortgage. The current draft leaves as undecided whether the law should allow for the possibility that at some future date the Registry will be used to evidence commercial loans secured by real property as well as residential loans secured by real property. While the drafters have some preference for allowing for the possible use of the registry for commercial loans, it would be useful to consider whether such an approach will result in additional enactment concerns.

2. The statute includes the definition of Residential Property that is proposed in the ULC draft Home Foreclosure Procedures Act. It is the belief of the drafters of this proposal that the limitations included in the Home Foreclosure Procedures Act and set forth in the bracketed sentence are not appropriate for this statute. Arguably the limitation on the number of dwelling units is also inappropriate for this statute. The drafters believe that there is also a need to consider whether the

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way in which manufactured-housing unit and time shares are captured in this definition make sense in the context of this statute. More discussion is warranted including consideration as to the degree to which Regulations should be referenced in the definition. If the statute does not limit the use of the Registry to residential mortgage loans, this definition would be removed altogether and left, if at all, to the Regulations or System Rules.

3. The definitions of Mortgage and Mortgage Agreement reflect the work of the ULC in the draft Home Foreclosure Procedures Act. As noted in the comments to that Act the term “mortgage” refers to the lien held by the creditor, which secures payment of the obligation, whereas the term “mortgage agreement” refers to the writing or other record that memorializes the parties’ agreement and creates the mortgage. Depending upon local usage and custom, the mortgage agreement may be denominated as a mortgage, deed of trust, trustee deed, security deed, deed to secure debt, or the like.

4. The bracketed language in the definition of Mortgage Agreement reflects a policy choice not to change current state law with respect to the recording of Mortgage Agreements. It is certainly possible to draft the statute to require that prior to the Deposit of an Obligation the associated Mortgage Agreement must be recorded. While this draft does not take this position, it does require that a document be recorded with the recording office after an Obligation is Deposited that would be a public record that there is a Deposited Obligation with the Registry’s records determining who can enforce the Mortgage. (See Section 202(e)(4)). Is this sufficient or should the statute require recording the Mortgage Agreement before Deposit? If our understanding is correct, and the overwhelming majority of lenders want to record the Mortgage Agreement, it might be helpful for the enactment process to make recording a prerequisite under this statute to depositing with the Registry.

5. One of the most significant drafting decisions reflected in the statute was the decision not to create a new type of property interest that would result from a Deposit. Instead, this law treats the Registry as a record keeper and looks to the records of the Registry to determine the identity of the Person entitled to try to enforce the Deposited Obligation and to determine the type of property rights at issue (e.g., Negotiable Instrument). Essentially the provisions of this statute allow a Person that holds a note issued in paper form to have it converted into an electronic medium and thereafter rely on the records of the Registry for the enforcement of such note.

6. The statute lets personal property secure the Obligation in part. Does it matter how much of the loan is secured by real property? Put differently, should there be some requirement that at least some percentage of the Obligation is secured by real property? What happens when the percentage changes over time with the value of the property? Also, unlike the case of Mortgages, the statute contains no special preemptive rules to assure the integrity of the security interest in personal property as the Obligation is deposited and transferred among Registrants. Do UCC §§ 9-203(g) & 9-308(e) provide adequate protection for these unusual cases?

7. The definition of “Control System” reflects the definition of “control” in both UETA and ESIGN. It is intended to ensure that only those electronic notes that are intended to be treated as the equivalent of a Negotiable Instrument under UETA and ESIGN are treated as Obligations within the scope of this statute (absent action by the Regulator). In fact, once Deposited this statute is drafted to

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treat Transferable Records that were in a Control System identically to Negotiable Instruments Deposited into the Registry. The concept of a Control System is relevant only to determine that the thing Deposited was in fact an Obligation that could be deposited – control and the notion of a Control System is not relevant with respect to post Deposit acts. Of equal importance is the fact that the interests being transferred on the Registry are Transferrable Records (see section 203) and thus the Registry does not need to be a Control System under UETA and ESIGN.

8. The definition of “Transferable Record” comports with the definition of transferable record in ESIGN. The UETA definition of transferable record is broader than that of ESIGN and would capture documents of title under Article 7 of the UCC. For purposes of this statute, the drafters limited the definition consistent with ESIGN. We believe that Revised Article 7 and not this statute should address transferable records under UETA that would have been documents under Article 7 if the electronic record were in writing.

Section 104. **Other Definitions**

(a) **Other definitions include:**

- ( ) “Registry Locator Number” or “RLN” is a number assigned by the Registry to identify each Deposited Obligation.
- ( ) “Regulations” are regulations promulgated by the Regulator and, where indicated, the CFPB.

(b) **Terms defined elsewhere in this statute are:**

- ( ) “Financial Regulator”
- ( ) “Security Procedure”
- ( ) “System Rule”

(c) Terms defined in other law: Any reference in this statute to another statute shall apply to the text of the referenced statute that was in effect as of the effective date of this statute. Any reference to the “UCC” shall be to the 2011 Official Text of the Uniform Commercial Code as promulgated by the Uniform Law Commission and the American Law Institute, unless otherwise stated. Subsequent changes to the referenced statute shall not affect this statute, unless the Regulator recognizes such changes

(d) The following terms are defined in the location indicated:

- ( ) “Good Faith” is defined in Article 1 of the UCC
- ( ) “Instrument” has the meaning given to it in UCC § 9-102(a)(47).

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- ( ) “Knowledge” is defined in Article 1 of the UCC
- ( ) “Negotiable Instrument” has the meaning given in UCC §3-104.
- ( ) “Person” is defined in Article 1 of the UCC. A Successor to a Person shall be treated as the Person for purposes of this statute.
- ( ) “Promissory Note” is defined in Article 1 of the UCC
- ( ) “Record” is defined in Article 1 of the UCC
- ( ) “Writing” is defined in Article 1 of the UCC

**Comments to Section 104**

1. A Person includes any Successor to the Person, such as an estate or merger survivor. The term “Successor to a Person” is defined in section 102 and is intended to be limited to where statutory law would determine succession. The concept is included in this draft to remove any doubt as to whether the Registry is authorized to get instructions from a successor to a Registrant, similar to the approach taken in section 5-113 of the UCC. Ultimately it may be determined that this definition is not required and that the statute should defer to other law on this question.

2. A decision needs to be made as to whether to define certain terms used in this statute by reference to other laws such as the UCC. Subsection (c) deals with some of the problems of cross-references to other statutes. One question to be decided is whether we want the default rule to be that subsequent changes to the law do not automatically apply to this statute (the current proposed drafting of (c)) or whether we want all such subsequent changes to apply unless the Regulator determines otherwise.

3. Before finalizing the statute we will want to ensure that all cross reference to definitions in the UCC are identified in subsection (d).

**Part B: The Registry and the Regulators**

Section 105. **The Registry**

**[Alt 1:** The Registry shall be [insert currently-existing entity here.]]

**[Alt 2:** The Registry shall be a [federally-chartered][state-chartered] instrumentality, with the right to sue and be sued, enter into contracts, and to exercise all powers specifically granted by the provisions of this statute and such incidental powers as shall be necessary to carry on the business of the Registry within the limitations prescribed by this statute.]

**[Alt 3:** The Regulator may recognize a Person as the Registry. Such Person must, to the satisfaction of the Regulator:

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- (a) Be organized as a cooperative or not-for-profit entity[, or operate on a not-for-profit basis];
- (b) Engage in no business other than serving as Registry;
- (c) Contain a governance structure that reflects the interests of all stakeholders in the Registry; and
- (d) Enjoy adequate capitalization, which may contain enforceable [retrospective] assessments on Registrants.]

**Comment to Section 105**

There is no point in drafting a detailed enabling provision, while the basic nature of the entity (*e.g.* government, private, etc.) is undecided. The draft does reflect two policy choices that may be ripe for discussion. The first is that there is only one Registry regardless of whether it is private or public, state or federal. It is the drafters' belief that while multiple registries are possible in theory, such an approach will be far more expensive and inefficient than establishing a single registry. The second is that if a private sector entity is established to serve as the Registry, it should not be a for profit entity. This reflects a judgment of the drafters that a for profit structure might have some perverse incentives with respect to investment in infrastructure for example.

The third alternative sets forth some elementary restrictions on a private entity that have been identified as critical to the success of a private sector financial market utility.

**Section 106. Registry's Powers and Duties**

The Registry shall serve the functions of Registry as set forth in this statute. The Registry is not an agent of any Person and shall not hold any interest in a Deposited Obligation by virtue of its operation as Registry.

**Comments to Section 106**

This provision establishes the authority of the Registry to act. It also makes clear that the statute does not adopt some of the legal structures described above such as the Article 8 structure where the Registry might have been viewed as the top tier holder or a bailment structure where the Registry might be viewed as an agent.

**Section 107. System Rules**

- (a) The Registry is authorized to adopt rules concerning its operations, fees, Security Procedures and the rights and obligations of Depositors, Registrants, and others with access to, or use of, the Registry in connection with such access or use. Such rules are referred to herein as "System Rules."
- (b) No System Rule may go into effect without approval by the Regulator and, if the System Rule affects Borrowers or the general public, without the approval of the CFPB.

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- (c) Approval of System Rules is subject to the [Administrative Procedures Act][state law equivalent].
- (d) A System Rule adopted by the Registry governing rights and obligations among the Registry and the Registrants (including Depositors) is effective even if the rule affects another party who has not consented to the rule.

**Comment to Section 107**

1. This Section reflects two basic regulatory principles of this statute. First, all System Rules require regulatory approval. Second is the principle of divided regulation. Any System Rules that only affect the full-time system professionals only need the approval of the Regulator. System Rules that affect other parties require the dual approval of the CFPB and the Regulator. It is possible to write this statute so that some System Rules only require CFPB approval.

2. This is pretty much the same policy as in UCC §§ 4-103(b), 4A-501(b), and 8-111. However, this statute differs from the UCC provisions in one respect. Regulatory approval of the System Rules is mandatory. Regulatory approval of System Rules helps to ensure that the interests of Borrowers and others who might be affected by a System Rule are taken into account.

We would expect to see System Rules that address, among other things, (a) requirements and procedures for initial registration of Obligations; (b) procedures for changing the identity of the Registrant; (c) procedures for registering changes in Obligations that have been registered and changes to the parties to such Obligations (e.g., loan modifications, substitutions, and assumptions); (d) procedures for instructing the Registry, including instructions about the discharge or a Deposited Obligation or a change in Servicer status; (e) standards, if any, for Obligations to be acceptable to the Registry; (f) any eligibility requirements that must be met before a Person may deposit an Obligation; (g) procedures for making information available on the internet and by other means, as appropriate; (h) procedures for reporting errors made by the Registry; and (i) procedures for obtaining certifications from the Registry as a means of verifying information about a Deposited Obligation.

**Section 108. Communications with the Registry**

- (a) The only Person that may instruct the Registry with respect to a Deposit is a Depositor.
- (b) The only Person that may instruct the Registry with respect to a Deposited Obligation is the Registrant associated with that Deposited Obligation.
- (c) The Registry may establish System Rules that permit a Depositor or Registrant to designate a Third Party Service Provider to send instructions on its behalf. The Registry shall establish System Rules that require a Depositor or Registrant to use a Third Party Service Provider to send instructions on its behalf where direct communications between the Depositor or Registrant and the Registry would expose the Registry to [heightened][unacceptable] information security and other [operational] risks.

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- (d) The Registry shall establish by System Rules, one or more Security Procedures for use by Depositors and Registrants (or their Third Party Service Providers) when sending instructions to, or receiving notices from, the Registry. A “Security Procedure” means a procedure established by agreement of a Registrant, including a Depositor, and the Registry for the purpose of verifying that an instruction to the Registry is that of the Registrant. A Security Procedure may require the use of algorithms or other codes, identifying words or numbers, encryption, callback procedures, or similar security devices. Comparison of a signature on an instruction with an authorized specimen signature is not by itself a Security Procedure. Any Security Procedure established by the Registry and approved by the Regulator (and the CFPB) is commercially reasonable as a matter of law.
- (e) The Registry is not required to accept an instruction from a Registrant, including a Depositor, unless and until such party has entered into an agreement with the Registry setting forth the Security Procedure that will be used to authenticate any communications between the Registry and the Registrant.
- (f) An instruction to the Registry is the authorized instruction of the Registrant, including the Depositor, identified as sending the instruction, if that Registrant authorized the instruction or is otherwise bound by it under the law of agency.
- (g) An instruction sent to the Registry in the name of a Registrant, including a Depositor, is effective as an instruction of that Registrant if it was verified by the Registry pursuant to a commercially reasonable Security Procedure and the Registry proves that it acted on the instruction in good faith and in compliance with the Security Procedure. The Registry is not required to follow an instruction that violates a written agreement with the Registrant or that is not received at a time and in a manner affording the Registry a reasonable opportunity to act on it.

**Comments to Section 108**

1. This section identifies the parties that may instruct the Registry. The draft provision contemplates System Rules that would enable a Depositor or a Registrant to designate its Servicer or an agent for the purpose of instructing the Registry. The System Rules would limit the Depositor’s or Registrant’s right to designate a Servicer (or other agent) to situations where such a designation would not threaten the security or integrity of the Registry.

2. Similarly, this section would require the Registry to require a Depositor or Registrant to communicate instructions through another party if the Registry has concerns that the information security infrastructure of the Depositor or Registrant could put the integrity of the Registry at risk. For discussion is whether the types of risks that are relevant for this Section 108 need to be further defined and discussed. Arguably this same authority is not needed with respect to a Depositor as it is envisioned that the deposit standards established by the Registry would include minimum information security requirements.

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3. Regardless of whether the designation of a third party is done at the request of the Depositor/Registrant or based on requirements of the Registry, all such communications are treated as instructions of the Depositor/Registrant in accordance to subsection (e). Each instruction will identify a Person as the sender of the instruction. Subsection (d) addresses the situation where the Person identified in the instruction as the sender, claims that the instruction was unauthorized. Subsection (d) provides that if in fact the Person identified as having sent the instruction is proven to have sent the instruction, or if that Person's agent sent the instruction, the instruction is authorized. The Registry is protected in this situation even if the instructions were sent using a method other than the agreed upon Security Procedure or the Registry otherwise failed to meet the requirements in subsection (f). The drafters included this provision because we were following the approach taken in Article 4A of the UCC. Query whether such a provision is needed.

4. Unlike subsection (f) which focuses on when an instruction is in fact authorized, subsection (g) follows the approach taken in Article 4A of the UCC and defines situations where the instruction is "verified" and as a result the Registry is entitled to rely on the instruction as the instruction of the Depositor/Registrant regardless of whether in fact the instruction was authorized.

5. This draft generally follows the rules established in UCC Article 4A except with respect to what is meant by commercially reasonable and the ability of a Depositor/Registrant to shift liability back to the Registry for interloper fraud. The draft statute looks to the Registry to design appropriate Security Procedures and then looks to the Regulator and the CFPB to determine that the Security Procedures are commercially reasonable.

6. Subsection (c) also makes explicit an assumption hidden in UCC Article 8: that the Registry must heed appropriate instructions. Both UCC Articles 4A ("payment order") and 8 ("entitlement order") define the scope of communication that give rise to obligations on the part of the party receiving such communications. Do we need a special definition of "instruction" for purposes of the Statute or is the ordinary meaning sufficient in the context of the Registry.

7. For further discussion is whether there is a need for statutory rules for communications by the Registry? Given the types of communications/notices provided by the Registry (i.e., they will not result in a change in legal rights), the drafters assume that such rules would be contained in System Rules and would look to rely on contact information provided by various parties to the Registry (as well as the agreed upon communication channel).

**Section 109. Regulator's Powers With Regard to Registry, its Operations and Members**

- (a) The Regulator shall prescribe regulations to carry out the purposes of this statute except that, on matters of interest to Borrowers[ and the general public], the Regulator shall [consult with the CFPB prior to the issuance of any such regulations][issue such regulations jointly with the CFPB].
- (b) The Regulator may issue Regulations that establish different classes of Depositors but any such distinction must be based on prudential concerns for the financial and operational responsibility

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of the Depositor and must provide some means by which each class of Depositor may deposit Obligations with the Registry.

- (c) The Regulator has visitorial powers over the Registry[ and over any Third Party Service Provider used by a Depositor to satisfy the deposit standards that does not have a prudential supervisor].

**Comments to Section 109**

1. This provision is similar to that found in TILA section 6104(a) – The Regulator shall prescribe regulations to carry out the purposes of this title. Except in the case of a mortgage referred to in section 103(aa), these regulations may contain such classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for any class of transactions, as in the judgment of the Regulator are necessary or proper to effectuate the purposes of this title, to prevent circumvention or evasion thereof, or to facilitate compliance therewith. Does this provision place too much authority with the Regulator?

2. The type of operational details necessary for the establishment of a registry are too detailed in nature to include in a statute and therefore it is necessary to grant rule writing authority to some entity. Admittedly, the authority to issue System Rules subject to approval by the Regulator may be sufficient in most instances. But there are certain matters that rise to the level of public policy decisions that we would expect to be addressed in implementing regulations in the first instance. These include the:

- (a) Types of Obligations that may be registered with the Registry;
- (b) Standards to be met by the Registry (e.g., capital, data quality);
- (c) Content and form of the information that must be retained by the Registry and the security and privacy protections to be offered by the Registry;
- (d) Minimum access requirements; and
- (e) Record keeping requirements.

3. In order to ensure the integrity of the Registry, the Regulator may issue substantive regulations that create different classes of Depositors. Such authority should be exercised carefully as any such distinction will likely increase the cost of using the Registry for certain types of Depositors. It is important that there be a clear justification for such differentiation and that all similarly situated Persons be treated the same way.

4. The statute provides that the Regulator may examine the Registry. Still to be determined is whether the Regulator should also be authorized to examine Third Party Service Providers that are not already subject to supervision.

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Section 110. **Information Sharing with Financial Regulators**

- (a) For purposes of this section, “Financial Regulators” are:
  - (1) The Board of Governors of the Federal Reserve, the CFPB, the CFTC, the FDIC, the FTC, the OCC, the SEC, the OFR, the Treasury Department and [the Housing Regulator]
  - (2) State banking, mortgage broker and insurance regulators; and
  - (3) Federal Home Loan Banks and Federal Reserve Banks.
- (b) The Regulator is authorized to share information about Registrants with the Financial Regulators.
- (c) The Financial Regulators are authorized to share information about Registrants with the Regulator.

**Comments to Section 110**

The definition of “Financial Regulators” only exists for information-sharing purposes. Given sensitivities to the sharing of information among Government entities, do we need to do more to define the scope of the sharing in this section? Should information about the operations of the Repository also be captured here? Should sharing of Borrower information be further regulated? For example, should the statute require that information shared be on an aggregate or statistical basis and not sufficiently detailed to permit identification of individual borrowers? Does it matter whether the Financial Regulator has supervisory authority over the Registrant (and therefore would be entitled to see the information at an individual loan level)? Are there situations in which the FDIC, for example, would legitimately want to identify individual borrowers in order to build a case of (say) racial discrimination against an originator?

More work on this provision may be necessary if this is a state law.

Subchapter 2: Deposit and Registration

Part A: The Deposit

Section 201. **Use of Registry**

- (a) The Registry shall establish Deposit standards that must be met before a Person may Deposit an Obligation with the Registry. Such standards may include, among other things, data quality requirements, information security requirements and capital requirements. If a Person is unable to satisfy the Registry’s one or more deposit standards, it may rely on a Third Party Service Provider to satisfy such standard so long as such Third Party Service Provider is qualified by the Registry and meets its Deposit standards. If a Depositor relies on a Third Party Service Provider to meet a Deposit standard of the Registry, the Third Party Service Provider as well as

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the Depositor has the obligations and makes the warranties associated with the Deposit as set forth in this statute. Any obligations between a Depositor and such a Third Party Service Provider are not governed by this statute other than to the extent that they are affected by System Rules.

- (b) The Registry is responsible for determining [to its satisfaction], at the time of a Deposit, that its standards have been satisfied by the Depositor and/or its Third Party Service Provider. [No Person may sue the Registry based][The Registry shall not be liable for ] on its determination that a Depositor or its selected Third Party Service Provider did not satisfy the Registry standards except where such determination was made in bad faith or in contravention of statutory law, regulations or its System Rules.

**Comments to Section 201**

1. Use of the Registry is voluntary, although universality is a goal. The universality goal requires that the Registry cannot be any more exclusive than is needed to ensure its integrity.

2. At the same time, the integrity of the Registry will turn in large part on whether legitimate Obligations are Deposited and whether the information submitted is accurate, legible and complete. Therefore, this statute, which permits anyone with an Obligation within the scope of the statute to use the Registry, needs to contemplate how best to protect users of the Registry from shoddy practices of Depositors. The proposed statute does this by [requiring] the Registry to set Deposit standards and through a series of Depositor and Registry warranties. The standards should consider, at a minimum, whether the Depositor is reputable, has a balance sheet that can stand behind the Deposit warranties, employs a mature information security/cyber security regime, and has the necessary technology.

3. In circumstances where a Person cannot satisfy the Deposit standards, it may still use the Registry but will have to find a third party that meets the requirements and will stand behind the Depositor. This will make the cost of entry for such a Depositor higher but such differentiation among Depositors is necessary to protect all users of the Registry. Of course, like all System Rules, the Deposit standards will be approved by the Regulator and the Regulator should consider whether the standards are appropriately designed to balance the somewhat competing goals of the Registry to be open to all Depositors but in a manner that does not place unacceptable risk on the other users of the Registry.

4. Note that the Depositor-Third Party Service Provider relationship is purely a creature of private ordering outside this statute. In contrast, this statute regulates the Third Party Service Provider-Registry relationship. This is a drafting choice; not a matter of necessity.

Section 202. **Act of Deposit and Registration**

(a) A request to Deposit an Obligation into the Registry is a request to the Registry to:

- (1) Register the Obligation as a Deposited Obligation; and

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- (2) Identify the Depositor as the initial Registrant of the Deposited Obligation.
- (b) A Depositor making a request to Deposit an Obligation must comply with any relevant System Rules including rules concerning required information. At a minimum such System Rules must require the Depositor to:
- (1) Identify the Depositor and, if applicable, any Third Party Service Provider used by the Depositor to satisfy one or more Deposit standards;
  - (2) Identify the Borrower(s) and provide [valid][current][last known] contact information for the Borrower(s);
  - (3) Identify any Servicer with respect to such Obligation, if any;
  - (4) If the Depositor is the Servicer with respect to such Obligation, identify the party for whom the Servicer is servicing such Obligation;
  - (5) Identify whether the Servicer has full, limited or no authority to modify such Obligation (and if limited authority, the scope of the authority); and
  - (6) Submit a legible copy of the complete Mortgage Agreement related to such Obligation [in a format that satisfies applicable System Rules and Regulations], and indicate whether such Mortgage Agreement has been (or is in the process of being) recorded with the applicable Recording Office and if recorded, the book and page number (or equivalent record locator information) and the Recording Office.
- (c) In addition the Depositor making the request to Deposit an Obligation must:
- (1) If the Obligation is an Instrument;
    - (A) Submit the Instrument to the Registry; [or
    - (B) [Submit a [high resolution][legible] copy of the complete Instrument in a manner that complies with all applicable System Rules and Regulations and, upon acceptance of the deposit by the Registry, destroy the Instrument];
  - (2) If the Obligation is a Transferable Record in a Control System, [move the Transferable Record into the Registry in accordance with System Rules][tender control to the Registry consistent with the rules of the Control System and System Rules][direct the Control System to restrict further transfers and indicate that the Transferrable Record was Deposited];
  - (3) If the Obligation is not an Instrument or a Transferable Record in a Control System, take such other actions as required by System Rules or regulations.

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- (d) Upon receiving a Deposit request, the Registry shall validate the [quality][ legibility] and completeness of the data submitted according to its System Rules.
- (1) The Registry shall accept any request to Deposit an Obligation that the Registry determines meets the Registry's Deposit standards and data requirements.
  - (2) The Registry shall reject any request to Deposit an Obligation that the Registry determines fails to meet the Registry's Deposit standards and data requirements. If the Registry rejects a Deposit, the Depositor may resubmit the request to Deposit the Obligation.
  - (3) Any Depositor warranty contained in this statute pertains only to an accepted Deposit.
- (e) The Registry accepts a request to Deposit an Obligation by:
- (1) Registering the Obligation as a Deposited Obligation by assigning a unique Registry Locator Number to the Obligation and associating such RLN with the Depositor, as the initial Registrant, in the Registry's records. If one or more Persons are jointly the Depositor, the Registry, based on instructions from the Depositor, shall indicate whether such Persons may exercise the rights of the Registrant individually or only jointly.
  - (2) **Alt 1:** Creating a [high resolution][legible] copy of any Instrument submitted to it in a manner that complies with all applicable System Rules and Regulations and destroying such Instrument[; and]  
  
**Alt2:** Creating a [high resolution][legible] copy of any Instrument submitted to it in a manner that complies with all applicable System Rules and Regulations and marking][Identifying] any such Instrument as [deposited][invalid]];
  - (3) Notifying the Depositor [and the related Borrower(s)] that the Deposit has been accepted and providing the RLN; and
  - (4) If the Mortgage Agreement submitted to the Registry in connection with the Deposit has not been recorded in the relevant Recording Office with the RLN, sending [or directing the Registrant to send] to such Recording Office for recording a record, associated with the Mortgage Agreement if it has already been filed, indicating that the Obligation has been Deposited and identifying the assigned RLN. [The record required under this subsection must be sent to the Recording Office within a reasonable period of time after the Registry accepts the Deposit]

**Comments to Section 202**

1. The act of depositing an Instrument into the Registry does not involve the "delivery" of the Instrument to the Registry as that term is understood in UCC Article 3 or 9 and does not involve any indorsement of the Instrument to the Registry or any other party. (see Section 210 – indorsements are

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made under the statute when a Person who is already the Registrant of a Deposited Obligation instructs the Registry to change its records to identify another Person as the Registrant of the Deposited Obligation).

2. Section 202(c)(2) is a place holder. The statute will need to address how one Deposits a Transferable Record that is in a Control System in a manner that results in the Registry maintaining the legally operative record while avoiding having the Registry be viewed as the party with control under UETA and E-SIGN. Whether it is feasible or desirable to have the Transferable Record moved into the Registry will need to be considered. If it is not moved into the Registry, we will need to address what information is required to make the Deposit and the law will need to mandate that the Control System take steps to invalidate the Transferable Record on its system (without loss of data).

3. A decision will need to be made as to whether a Depositor will be permitted to submit an image of an Instrument with a requirement that the Depositor subsequently destroy the Instrument and warrant that the copy is accurate and that the Instrument was destroyed. Or will the statute require that the Instrument be submitted to the Registry and that the Registry create the image and destroy the Instrument.

4. Section 202 in several places includes the notion that the copy/image of an Instrument Deposited with the Registry must be of a high resolution. This notion is in several other places in the draft statute. Clearly there is a need for high quality images that permit a Person to read the Instrument but it may not be a good idea to address these types of technology issues in the statute in any great detail as technology will change over time.

5. The section requires identification of the Servicer. Given the broad definition of Servicer, might there be more than one and do we want to require disclosure of all such parties? The section requires disclosure as to the authority of the Servicer to enter into modifications. Is it possible to provide more information than just full, limited or no authority?

6. The section proposes a new recording obligation in e(4). The purpose of this new recording obligation is to ensure that anyone that relies on the recording office records will have knowledge that an Obligation relating to a recorded Mortgage Agreement is deposited and will help to enable the holder of a first lien and a second lien to identify each other since the Registry Locator Number will be a part of the document being recorded. With the RLN, anyone will be able to identify the current Registrant of a Deposited Obligation. If the Mortgage Agreement has already been filed, the provision calls for the recording of the RTN to be associated with the recorded Mortgage Agreement. If the Mortgage Agreement has not been filed, how should this new document get recorded?

7. This Section does not require that the Registry make information public after Deposit. This requirement occurs later in the statute.

**Section 203. Legal Effect of Deposit and Registration**

(a) Upon completion by the Registry of the acts set forth in section 202(e)(1) :

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- (1) The Deposited Obligation documents the agreement between the Borrower(s) and Registrant with the same effect and validity as the Obligation prior to the Deposit. The tangible Instrument or Transferrable Record that was Deposited ceases to have any effect or validity [as opposed to the Obligation reflected by the tangible Instrument or Transferrable Record while in the Control System];
- (2) The Person identified by the Registry as the Registrant of the Deposited Obligation becomes the Registrant.
- (3) Subject to subsection (c) of this Section:
  - (A) A Deposited Obligation that was created based on the Deposit of an Instrument that at the time of Deposit was a Negotiable Instrument or a Transferable Record that at the time of Deposit was in a Control System shall be [treated as] a Negotiable Instrument for all purposes of the UCC. The destruction of a Deposited Instrument shall not affect the application of this subsection (3).
  - (B) A Deposited Obligation that was created based on the Deposit of an Instrument that, at the time of Deposit, was not a Negotiable Instrument shall be [treated as] a Negotiable Instrument for all purposes [of Articles 3 and 9] of the UCC as enacted in [state where action is brought][the District of Columbia]; except there can be no holder in due course of such a Deposited Obligation.
- (4) The Person(s) identified by the Registry as the Registrant of the Deposited Obligation:
  - (A) If the Obligation Deposited with the Registry was at the time of Deposit an Instrument, shall be treated as having continuous possession of the Instrument that was Deposited for all purposes of the [UCC][other state or federal law].
  - (B) If the Obligation Deposited with the Registry was at the time of Deposit a Transferable Record in a Control System, subsequent to the deposit, shall be treated as having continuous possession of the Negotiable Instrument referenced in 203(a)(3)(A) for all purposes of [the Uniform Commercial Code][other state and federal law].
- (5) For purposes of any law that depends on the location of a Deposited Obligation (or the location of the Instrument that was Deposited), the location of such Deposited Obligation or Obligation shall be deemed to be [ALT 1 the place of incorporation of the Registry][ALT 2: Washington D.C.][ALT 3: ???]
- (6) Any law that requires that notice be given to a Borrower on an Obligation shall be read to require that, after Deposit of the Obligation in the Registry, such notice be given to the Borrower(s) associated with the Deposited Obligation.

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- (b) The Deposit of an Obligation into the Registry shall have no effect on any acts taken before the Deposit and registration [and shall have no effect on the status of any Person with respect to the Obligation before the Deposit and registration].
- (c) Notwithstanding Article 3 of the UCC:
  - (1) An Instrument Deposited into the Registry pursuant to this statute shall not be treated as destroyed for purposes of UCC § 3-309 or as discharged for purposes of UCC § 3-604 notwithstanding the requirement to destroy the Instrument in section 202.
  - (2) Part 5 of UCC Article 3 does not apply to Deposited Obligations except for [to be determined].
  - (3) The records of the Registry may be used to satisfy any post-Deposit Writing requirement with regard to the Instrument.
  - (4) [Other Article 3 trivia involving paper: *e.g.*, 3-201-03, 3-310-11, 3-420]

**Comments to Section 203**

1. As noted in section 202, the Registry accepts a Deposit by creating the Deposited Obligation. Section 203 makes clear that at the moment that the Deposited Obligation is created, while the Borrower's promise to pay continues to exist and is reflected in the records of the Registry as the Deposited Obligation, the Instrument or Transferrable Record in a Control System that was the subject of the Deposit itself no longer has any effect or validity. The Deposited form of the Obligation becomes extinct upon Deposit, replaced by an electronic substitute, a Deposited Obligation.

2. This section creates a bridge between the new Deposited Obligation and the body of law, the UCC, that previously governed transfers and security interests in the deposited Instrument. Treating the deposited obligation as a negotiable instrument under the UCC, possessed by the Registrant, means, for example, that the transfer warranties of 3-416 apply, the rules for perfection by possession and superpriority of UCC 9-313 and superpriority of UCC 9-330, 331 apply; and the third party provisions applicable to promissory notes found in 9-406 apply.

3. Subsection (a)(6) is intended to make sure that current state and Federal laws that require notice to a borrower, for example when a loan is sold, continue to apply when there is a Deposited Obligation in substitution for a loan.

4. Paragraph (a)(3)(B) is adapted from pre-Revision UCC § 3-805. The common law of non-negotiable instruments is very poorly specified, and the only statutory basis of such instruments is now in UCC Article 9. Paragraph (a)(3)(B) conveniently resolves most ambiguities in this law.

5. A decision will need to be made as to what version of the UCC to reference throughout this section. To avoid conflicts, it may be best to identify a specific state enactment or to the official version enacted by the ULC and the ALI. See section 104(c). More discussion of this issue is required.

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6. Nothing in this section or elsewhere in the statute conveys upon a Registrant the status of PETE. PETE status is still determined under the UCC. The statute establishes certain facts that are necessary for the PETE analysis perhaps most importantly the fact that the Registrant has “possession.”

7. If Obligations other than Instruments and Transferrable Records in a Control System are permitted to be deposited with the Registry, the Regulations will need to address the legal effect of the deposit.

8. Subsection (c) is a placeholder. More work will need to be done to make sure that the statute is not in tension with the UCC.

**Section 205. Security Interests in a Deposited Obligation**

- (a) The act of depositing an Obligation with the Registry does not affect the attachment, perfection, or priority of a security interest granted in the Obligation that attached prior to the deposit.
- (b) A description or indication of a Deposited Obligation in a security agreement or financing statement for purposes of the UCC as a deposited obligation or an obligation, reasonably identifies the Deposited Obligation [for purposes of UCC 9-108]. Any description or indication of the Obligation that was sufficient before Deposit remains sufficient upon and following Deposit. This subsection (b) supplements the rules of section UCC 9-108 and does not prevent satisfaction of UCC 9-108 under the provisions of that section.
- (c) Nothing in this statute precludes the creation of a security interest in a Deposited Obligation under UCC Article 9.
- (d) [For deposits that do not take the form of Instruments or Transferable Records, the Regulator is authorized to promulgate rules concerning the attachment, perfection, priority, and enforcement of security interests.]

**Comment to Section 205**

1. This statute authorizes the Regulator to promulgate all commercial-law rules for deposits that do not take the form of Instruments or Transferable Records that were in a Control System, including the law of secured transactions. Of course the Regulator could defer to state law if it determines that state law is sufficient to address the issues that arise with such deposits.

2. The proposed statutory rules for secured transactions only operate on deposits that take the form of Instruments or Transferable Records. All such corresponding Deposited Obligations take the form of Instruments, be they negotiable or otherwise. The ordinary Article 9 rules for instruments apply, especially those related to perfection. Possession may occur on the Registry; filing works the ordinary way. Nothing in the statute, however, precludes the possibility of a Person perfecting a security interest in a Deposited Obligation by means of a UCC filing. Such a secured party is not, however, going to be recognized by the Registry.

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3. This leaves two classes of unresolved Article 9 problems: choice-of-law rules, and the transitions between Obligations and Deposited Obligations. The transition problem is the more interesting and difficult one. Two transition rules seem necessary: one for collateral description (subsection (b)) and one for the deposit itself (subsection (a)).

4. Section 203(b) is intended to ensure that the deposit of an Obligation with the Registry does not result in an erroneous description in a UCC filing statement.

5. Attachment, perfection and priority of security interests in Deposited Obligations will generally be governed by the UCC. Example 1: Lender, a Delaware corporation, lends money to Borrower evidenced by a negotiable instrument and secured by a residential mortgage. Original Lender grants a security interest to Depositor in the resulting negotiable instrument and mortgage. Depositor deposits the note with the Registry. Depositor's security interest in original Lender's rights remains attached. The Deposited Obligation is treated like a negotiable instrument for UCC purposes. Depositor is deemed to be in possession of the original note in the State of X. Depositor's security interest in the obligation is perfected because it is deemed to be in possession. If the Depositor (or another Person) had perfected by filing a financing statement, the financing statement is still sufficient, with any potential number of indications of the collateral as stated in subsection (b).

**Part B: Rights and Obligations of Registrants**

Section 206. **Who may be a Registrant.** Any individual with legal capacity or other Person with legal power may become a Registrant. [If one or more Persons are jointly the Registrant, the Registry, based on instructions from the Registrant, shall indicate whether such Persons may exercise the rights of a Registrant individually or only jointly.]

**Comments to Section 206**

1. Query as to whether this Section is needed.

2. If joint property rights are allowed in the statute, should the statute accommodate rules regarding creditor process and other adverse claims against the property of joint rights holders, the rights *inter sese* of the Registrants, the rights of the Registrants to instruct the Registry, etc. These rights in other contexts (e.g., bank deposits) often differ among states. If these rights are not specified, what (if anything) should the choice of law rule be?

**Section 207. Obtaining the Status of Registrant.**

- (a) In all instances, the Depositor is the initial Registrant. After Deposit and initial registration, the only means by which a Person may become the Registrant of a Deposited Obligation is if the Registry identifies the Person on the Registry's records as the Registrant.
- (b) An instruction to the Registry to change the identity of the Registrant must contain all of the information required by the Registry in accordance with System Rules and Regulations. Regardless of the intent of the Registrant providing the instruction, the effect of the instruction

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is to deliver possession of the Deposited Obligation to the new Registrant for the purpose of transferring the right to enforce the Deposited Obligation.

- (c) Nothing in this statute shall affect the validity or the interpretation of contracts to transfer property rights to a Deposited Obligation from a Registrant to another Person.

**Comment to Section 207**

1. Only the Registrant identified on the Registry (or its authorized Third Party Service Provider or a Successor to the Registrant) may exercise the rights of a Registrant established by this statute including the right to direct the Registry to change the identity of the Registrant of a Deposited Obligation and to enforce the Deposited Obligation. Any purported transfer of such rights off the Registry shall have no effect on the Registry or other third parties not the transferor or transferee.

2. The Registry will need to establish System Rules governing requests to change the identity of the Registrant of a Deposited Obligation. Such rules will set forth the information required to be submitted with such a request. At a minimum, the request will need to include the name of the Person being registered and contact information for that Person. If the new Registrant is a Servicer, the System Rules will require that the request identify the party for whom the Servicer is servicing so that such information can be made available to the Borrower. The System Rules may provide for an instruction to change the identity of the Registrant at a specified future date.

3. Section 207(a) and (b) are needed to ensure that the Person identified as the Registrant will always be the person entitled to enforce under UCC Article 3 (assuming that the Depositor was the PETE)..

4. A Registrant may grant beneficial rights in Deposited Obligations to others by means of a contract. Such beneficial rights shall not grant the beneficial owner any right to enforce, modify, transfer, or discharge in a Deposited Obligation.

**Section 208. Adverse Claims**

- (a) The Registry shall follow the instructions of a Depositor (prior to acceptance of the Deposit) even when the Registry has notice of a property, possessory or other claim to the Obligation that is the subject of the Deposit request. The Registry shall follow the instructions of a Registrant even when the Registry has notice of a property, possessory or other claim to the Deposited Obligation. The Registry is under no obligation to act or to refrain from acting based on notice of such claims.
- (b) Any action based on a claim to a Deposited Obligation asserted against a Person other than the Registry, whether framed in conversion, replevin, constructive trust, equitable lien, or other theory, shall be resolved as though such claim was a claim to the Obligation that gave rise to the Deposited Obligation. [Need choice of law.]

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**Comments to Section 208**

1. An adverse claim is a claim to a Deposited Obligation, or the underlying Obligation, asserted by a Person not recognized as the Registrant by the Registry. Adverse claims may include, but are not limited to (a) pre-Deposit claims of the nature that the Registrant did not have the power to make the Deposit; or (b) post-Deposit claims that the re-registration of a Deposited Obligation was unauthorized or voidable.
2. Duplicate Obligations each of which is Deposited do not give rise to a claim. The claims discussed in this section are claims of a Person without the status of Registrant. The claims resulting from a multiple deposit are, in effect, claims by one Registrant that the other Registrant should not be able to enforce a Deposited Obligation. Such claims are more appropriately left for Subchapter 4.
3. Subsection (a) provides that the Registry does not have to recognize the claims of a Person not recognized as the Registrant by the Registry with respect to a Deposited Obligation. The Registry acts only on instructions from the Registrant (see section 108) or, of course, as directed by a court order. This provision deviates from similar provisions in the UCC in that it permits the Registry to ignore adverse claims even when it has notice of the adverse claim. Is this appropriate for this statute? Should the statute consider some sort of adjudication by the Registry itself when it has notice of such disputes?
4. Subsection (a) currently applies the same rule to instructions from the Depositor prior to the Registry accepting a Deposit as it does to an instruction from a Registrant. Should the rule be the same or should the Registry be required to refrain from accepting a Deposit when it has knowledge of an adverse claim to the Obligation until such claim is resolved? Accepting such an Obligation for Deposit seems to be in tension with the proposed warranty from the Depositor as to knowledge of adverse claims.
5. Subsection (b) is meant to provide clarity to a court as well as the affected parties as to how to treat a claim asserted against a Deposited Obligation. The proposed text would look to the law that would have determined the rights relative to the underlying Obligation. Thus, if the adverse claim involves a Deposited Obligation that was created as a result of the Deposit of a Negotiable Instrument, whether the claim is successful will be determined by the rules in [Article 3] [Article 8?] of the UCC. Note that a successful adverse claim asserted against a Registrant will not quite restore the *status quo ante* where such claim is based on pre-deposit facts. The claimant loses its right to an assignment or replevin of the Instrument or the like, and gains the right of a Registrant. The System Rules will have to be drafted to accommodate this kind of involuntary Registrant, especially if it is unwilling or unable to comply with ordinary System Rules. The statute could be drafted to restore the original rights of the claimant. This would be more complex, and contrary to the policy of the Registry—once an Obligation is in, it never goes out.
6. The text in (b) results from the policy choice to treat Deposited Obligations as much like the original entitlements as possible. It is possible, however, to envision a provision that is more akin to UCC Article 8:

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*An action based on an adverse claim to a Deposited Obligation, whether framed in conversion, replevin, constructive trust, equitable lien, or other theory, may not be asserted against a Person who becomes a Registrant under [ ] for value and without notice of the adverse claim. For purposes of this provision,*

*(1) a Person has notice of an adverse claim if:*

*(aa) the Person knows of the adverse claim;*

*(bb) the Person is aware of facts sufficient to indicate that there is a significant probability that the adverse claim exists and deliberately avoids information that would establish the existence of the adverse claim; or*

*(cc) the Person has a duty, imposed by statute or regulation, to investigate whether an adverse claim exists, and the investigation so required would establish the existence of the adverse claim.*

*(2) Having knowledge that a Deposited Obligation has been re-registered by a representative imposes no duty of inquiry into the rightfulness of a transaction and is not notice of an adverse claim. However, a person who knows that a representative has re-registered a Deposited Obligation in a transaction that is, or whose proceeds are being used, for the individual benefit of the representative or otherwise in breach of duty has notice of an adverse claim.*

*(3) Filing of a financing statement under Article 9 is not notice of an adverse claim to a Deposited Obligation.*

7. Adverse Claims are claims to the Deposited Obligation, not the mortgaged property. Subchapter 4 deals, in part, with claims to the mortgaged property.

**Section 209. Creditor Process**

- (a) The interest of a debtor as Registrant in a Deposited Obligation may be reached by a creditor only by legal process upon the Registry.
- (b) The interest of a debtor other than the Registrant in a Deposited Obligation that has been registered in the Registry in the name of a secured party may be reached by a creditor only by legal process upon the secured party where the creditor has knowledge that the Registrant is a secured party.

**Comments to Section 209**

1. Unlike UCC Article 4A where it was important to limit injunctions once a funds transfer was initiated until it was completed, there is really no need to develop special rules in this statute to govern when a court may or may not issue an injunction against a Registrant or other interested party outside the Registry.

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2. Although perhaps not necessary, it may be useful for the statute to address creditor process. Section 209(b) adopts the approach in UCC Article 8 for securities entitlements. The wording in Article 8 does not take into account that a secured party for purposes of Article 9 also includes the purchaser of a securities entitlement. To help provide clarity, the drafters broke this into two scenarios; the first where the debtor is also the Registrant and the second where the debtor is not the Registrant. Does a provision like this make sense in the context of the Registry?

3. Is there a need to articulate other types of actions that a court could stop the Registry from taking?

**Section 210. Indorsement Accompanying Registration**

- (a) An instruction to the Registry to change the identity of the Registrant of a Deposited Obligation shall be deemed to be accompanied by an indorsement of the Obligation that gave rise to the Deposited Obligation by the Registrant issuing the instruction.
- (b) The Registrant instructing the Registry to change the identity of the Registrant of the Deposited Obligation may include in the instruction whether the indorsement is [in blank or special,] with or without recourse, and with or without warranty. The Registry shall ensure that any such instruction is entered in the Registry records in a manner that permits all future registrants to see the information.
- (c) If the Registrant instructing the Registry to change the identity of the Registrant of the Deposited Obligation fails to include the information in (b) above, the indorsement shall be treated as an indorsement [in blank, and] without recourse or warranty.
- (d) The warranties referred to in this Section are the transfer warranties set forth in UCC Section 3-416.

**Comments to Section 210**

1. This section is necessary to ensure that the Person identified as Registrant on the Registry will be the person entitled to enforce the Deposited Obligation (if the Depositor was a PETE). Allowing the indorsement to be with or without recourse and warranty permits parties to continue to structure their transaction consistent with current practices.

2. The drafters of the statute have as a policy matter looked to Article 3 of the UCC to provide most of the legal framework for Obligations on the Registry after the Deposit. Section 210(d) is an example of how this policy is effected in the statute. Read together sections 207(b) and this section 210 provide that re-registration is a transfer of an instrument with an indorsement. The default rule in this statute is that the current Registrant warrants these matters to all future Registrants.

3. Although this draft leaves the option of special indorsements as an open issue, no good reason for permitting them occurs to us.

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**Section 211. Modifications and Other Changes Affecting the Obligation or Mortgage Agreement**

- (a) The Registrant of a Deposited Obligation shall Deposit with the Registry a Record evidencing any modification made to the Deposited Obligation and the Registry shall associate such modification with the Deposited Obligation. Such deposit must comply with Section 202. The Registrant may submit any other documentation that identifies changes to the parties to the Deposited Obligation, title to the property securing the Deposited Obligation, or changes to the Mortgage Agreement. The Registry shall associate any additional documentation submitted with the Deposited Obligation to which it relates.
- (b) [With the exception of a modification of an Obligation which may only be Deposited by the Registrant, any Person may submit documentation identified in (a) above to the Registry. All such submissions must comply with relevant System Rules. Except with respect to a modification, the Registry shall have complete discretion to determine whether the documentation submitted should be made available in the Registry. In no event shall the Registry be liable to any Person for its inclusion of, or failure to include, a document in the Registry submitted in accordance with this subsection (c). ]
- (c) The effect of any modification on the rights and obligations of any Person with respect to the Deposited Obligation and the associated Mortgage shall be determined under other law.

**Comment to Section 211**

1. The statute is silent as to who is authorized to modify a mortgage loan although it is the drafters' expectations that the Registrant is the Person that is authorized to modify the mortgage loan (where the Registrant is the Servicer, the statute requires that the scope of the authority of the Servicer to modify the Deposited Obligation be noted and that the Person on whose behalf the servicing is conducted to be also identified.)

2. Regardless of who is authorized to modify a mortgage note, because the Registry will only interact with the Registrant with respect to the Deposited Obligation, only the Registrant may Deposit the modification in the Registry. A Registrant that fails to comply with this requirement would be liable under section 605 to a Person who suffers a loss as a result of such failure to comply. For discussion is whether the liability rule in section 605(a) should apply to this situation or if a special liability rule should be included here..

3. There are other types of documents that may be useful to include in the Registry such as a loan assumption agreement, a deed of sale, notice of a successor to the Borrower (perhaps due to death), or a guaranty. Section 206 does not require a Registrant to submit these documents to the Registry but does make clear that such an option exists. No liability attaches to the Registrant for its failure to submit such information. Should the statute treat certain of these documents similarly to a loan modification and require that they be submitted to the Registry?

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4. Query whether the statute should permit others not the Registrant to submit information. If such an option is permitted, it will be important to make sure that the Registry is not exposed to risks that it cannot control. So, for example, the Registry should be able to determine in its System Rules the means by which it will accept such submissions. The Registry should not be in a position where it needs to determine whether the documentation is fraudulent.

**Section 212. Satisfaction and Discharge of Deposited Obligation**

- (a) A Registrant is required to instruct the Registry when a Deposited Obligation has been fully satisfied or discharged. Upon receiving such an instruction from the Registrant, the Registry shall indicate in its records that the Deposited Obligation has been fully satisfied or discharged and shall not act on any subsequent instruction to register the Deposited Obligation in the name of another Person.
- (b) If [30] days after a Borrower has fully satisfied or discharged the Deposited Obligation the Registry records do not indicate that the Deposited Obligation was satisfied, the Borrower may notify the Registry that it has paid the Deposited Obligation in full.
  - (1) Upon receiving such notice, the Registry shall promptly notify the Registrant thereof.
  - (2) If 30 days after the Registry has received such instruction from a Borrower the Registry records do not indicate that the Deposited Obligation has been fully satisfied or discharged, the Borrower may seek an order from a court of competent jurisdiction directing that the Registry indicate in its records that the Deposited Obligation has been fully satisfied or discharged. The Registry may interplead the Registrant into such proceeding. If the Borrower succeeds in its action, the Registry shall pay the Borrower's reasonable legal fees.
  - (3) The limitation period for such a suit is [six] years after the final payment on the Deposited Obligation is due, according to the documentation on file with the Registry, including any modification of the Deposited Obligation submitted to the Registry.
- (c) [Ten] years after a Deposited Obligation is satisfied, the Registry will destroy all records relating to such Deposited Obligation except to the extent that the Regulator and CFPB, in a joint regulation, mandate a different retention period.

**Comments to Section 212**

1. The Registry's records can serve a function similar to a canceled mortgage note: evidencing payoff. This means that the Registry's records must be marked accordingly. This is the responsibility of the Registrant. The Borrower has a right to sue the Registry (after providing notice of the payoff), if the Registry does not update its records. The Registry's System Rules will almost certainly shift risk onto the Registrant.

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2. Subsection (b) is as consumer-friendly as possible. Since the Registry will likely demand an indemnity from the Registrant in its System Rules, the main effect of making the Registry a defendant is to encourage it to act as the Borrower's advocate in payoff disputes. Alternatively, the statute could require the Registrant to pay the reasonable legal expenses of both the Borrower and the Registry; collecting from the Registrant, however, may give rise to additional litigation and further burden the Borrower.

Subchapter 3: Information and Access Rights

Section 301. **Information Maintenance Requirements.**

- (a) The Registry shall establish System Rules that set forth all of the information that a Depositor must provide to the Registry in connection with a request to Deposit an Obligation, including all of the information required under Section 202, and that a Registrant other than the Depositor must provide upon registration under Section 207. The System Rules shall establish the means by which the information shall be submitted including setting forth technology and security requirements aimed at ensuring the integrity of such a submission.
- (b) The Registrant of a Deposited Obligation shall maintain the accuracy of all of the information in the Registry concerning the Deposited Obligation including information concerning the Servicer and, if the Registrant is the Servicer of such Deposited Obligation, concerning the identity of the party for whom the Servicer is servicing. Any updates to the information in the Registry must be submitted to the Registry, in accordance with relevant System Rules, within [ ] [business days] of the event giving rise to the need for the update.
- (c) The Registry shall be responsible for maintaining all of the information required under (a) and (b), and, with respect to each Deposited Obligation:
  - (1) The identity of each Registrant of that Deposited Obligation and the time when such Person was the Registrant;
  - (2) If the Obligation giving rise to the Deposit was an Instrument, a record as to whether the Registry created the electronic image of the Instrument or whether the Depositor (or its Third Party Service Provider) created the image;
  - (3) A record of each indorsement made under Section 210;
  - (4) An indication as to whether the Registry has been notified that a foreclosure proceeding or other enforcement action is being pursued by a Registrant in connection with a Deposited Obligation in accordance with Section 401; and
  - (5) An indication as to whether the Registry has been notified that the Deposited Obligation was fully satisfied or discharged in accordance with Section 212.

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(d) The Registry shall collect and, except as otherwise noted in Section 202, maintain all such information and make such information available for the timeframe specified in Section 303 and consistent with this Subchapter and any applicable System Rules and Regulations.

**Comments to Section 301**

1. This section requires that the Registry establish System Rules addressing the information requirements of the Registry. It also places a requirement on the Registry to retain information and make it available to various parties consistent with this subchapter. This section is not meant to suggest a specific technology solution and will need to be re-examined in that context as the drafting evolves. It is envisioned that certain of this information will be submitted to the Registry in a structured format.

2. Is there a need to modify the term “information” in subsection (a) so that it refers to correct and/or complete?

3. If a Registrant fails to update information in the Registry that has changed, the liability provision of section 605(a) would be triggered as the Registrant has failed to comply with this statute (and System Rules). Is there any reason to have a special rule here on liability?

4. Section 301 employs System Rules. Should Regulation be used instead? See Section 302.

Section 302. **Regulations.** The Regulator, acting jointly with the CFPB, may issue Regulations that modify the rights set forth in this Subchapter.

**Comment to Section 302**

This Subchapter tries to be reasonably complete, but will doubtless have to be modified with time. Also, it cannot possibly prescribe those System Rules that are necessary for adequate data integrity and security.

Section 303. **Responsibility of Registry for Information**

- (a) The Registry shall be responsible for:
- (1) Accurately recording and maintaining records of Deposits, registrations and other instructions provided to the Registry in accordance with any requirements of this statute, Regulations and System Rules;
  - (2) Accurately capturing all of the information, [in a high resolution, electronic format][in accordance with technical standards set forth in System Rules or Regulation], contained in any paper document that is submitted to it;
  - (3) Preserving all information required by Section 311; and

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- (4) Providing information pursuant to a request made in a manner and format required by System Rules for information required by this statute, its regulations, or any System Rules.
- (b) The Registry shall maintain an information security program designed to protect the security and confidentiality of information in the Registry, to protect against any anticipated threats or hazards to the security or integrity of such information, and to protect against unauthorized access to such information.

**Comment to Section 303**

1. The Registry is only responsible for veracity of the identity of the Depositor because this is the one area that the Registry controls. The obligation contained in subsection (a)(1) is of informational integrity and completeness, not truthfulness. The System Rules, if properly written, should ensure that the Registry should be able to check for informational completeness by automated means.
2. This Section also sets forth the general requirement for an information security program that protects the integrity of the Registry's records.
3. If the Registry is operated by an agency or instrumentality of the government (state or Federal), the statute will need to address how laws such as the Freedom to Information Act are meant to apply. This applies for Section 303 as well.
4. If the Registry breaches its obligations it may be liable under Section 605(b).

**Section 304. Access Rights**

- (a) A Borrower is entitled to access to all information identified in Section 301 with respect to a Deposited Obligation as to which it is a Borrower.
- (b) A Registrant is entitled to access to all of the information identified in Section 301 with respect to any Deposited Obligation as to which it is the Registrant.
- (c) At the request of a Registrant, and consistent with System Rules, any Person may be provided access to all of the information to which the Registrant is entitled under this Section. It is the sole responsibility of the Registrant to ensure that its request to the Registry to grant access is consistent with any confidentiality obligations of the Registrant.
- (d) Any Person shall be entitled to know of the existence of a Deposited Obligation by means of disclosure of the RLN, the identity of the Registrant, [the Servicer], and, at the option of the Registry, an image of the Mortgage Agreement or information sufficient to identify the real property securing the Deposited Obligation.

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- (e) The Registry shall grant a court access to any information that the court requests [by court order]. Upon an order from a court with jurisdiction over the Registry, the Registry shall grant access to records at the direction of the court to a third party.
- (f) [special government rule? Academic researcher?]
- (g) The Registry shall issue System Rules setting forth requirements concerning the time and manner in which information requests may be made, the method(s) that the Registry may use to respond to such requests, procedures for obtaining certified records from the Registry, and any fees associated with information requests consistent with the terms of any Regulations. With regard to the access rules specified by subsection (a), the Registry must provide at least one method of providing such information free of charge and within a reasonable period of time.

**Comment to Section 304**

1. Subsection (c) is intended primarily for Servicers. Servicers have little formal role in this statute, but the statute must be written to accommodate their role. The draft does not establish any obligation on the part of the Registry to determine if the request from the Registrant to grant access to a third party is consistent with the Registrant's confidentiality obligations. Because the Registrant currently has access to all of this information and has the ability to provide access to third parties, the drafters do not believe that the Registry should have any obligations – the Registrant would be subject to a claim for breach of a confidentiality obligation to the same extent it faces such a claim today. However, the statute could require that the Registry take some action prior to granting such access. If this is desired, is obtaining a certification from the Registrant sufficient?

2. The drafters expect that the decision of how to draft subsection (d) will turn in part on the technology design of the Registry.

3. It is probable that the Regulator, in consultation with the CFPB, will issue Regulations that address information requests. If so, the System Rules described in subsection (e) will need to be consistent with those Regulations. It is also expected that the System Rules will need to be reviewed and approved by the CFPB as well as the Regulator.

Subchapter 4: Enforcement

Section 401. **Commencement of Enforcement.** Prior to or at the time of filing any judicial foreclosure action or other litigation intended to enforce a Deposited Obligation, or [ ] any non-judicial foreclosure proceeding, the Registrant shall provide notice to the Registry. Upon receipt of such notice, the Registry shall:

- (a) Indicate on the Registry that the Deposited Obligation is subject to enforcement and identify the court or other forum in which enforcement is pending.

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- (b) Provide access to records of the Registry concerning the Deposited Obligation to the court where the foreclosure action or other litigation is pending .

**Comments to Section 401**

1. The limited access to the courts under ordinary circumstances is intended to protect the privacy of the Borrower. Unless the Deposited Obligation is being enforced, the courts generally will have no reason to access Registry data that are not available to the general public. Of course, if the Registry data become relevant in the context of some other litigation, the courts should have access and section 304 provides a means by which such a court may obtain access. This provision is triggered by notice from the Registrant and not the court itself.

2. The requirement to provide notice to the Registry with respect to judicial foreclosure or other litigation is triggered with the filing of the action. It is less clear when the notice needs to be provided in the context of a non-judicial foreclosure proceeding. The drafters need more guidance with respect to the timing of such notice.

Section 402. **Termination of Enforcement.** If a Registrant dismisses or otherwise ceases to pursue its enforcement proceeding, the Registrant may, but is not required to, provide notice thereof to the Registry. Upon receipt of such notice, the Registry shall:

- (a) Remove any indication in the Registry that the Deposited Obligation is subject to enforcement; and
- (b) Retain a record that the Deposited Obligation has been the subject of enforcement proceeding, including a record of when the Registry had been notified of such enforcement proceeding.

**Comment to Section 402**

This undoes the previous section, but creates a record, for the benefit of any subsequent Registrants who may want to know the history of this.

Should this be drafted as an affirmative obligation on the Registrant? Is there a need for such an affirmative duty? The drafters have assumed that while this may be information that is nice to have, it is not strictly speaking necessary and therefore made this section optional.

Section 403. **Contract Rights.**

- (a) Unless otherwise provided in this statute, in any proceeding to enforce a Deposited Obligation the [contractual] rights of the parties to the litigation shall be determined by applying the provisions of Section 203 except that if Regulations authorize the Deposit of Obligations with the Registry other than Instruments and Transferrable Records in a Control System, such

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Regulation shall establish how such an Obligation is to be treated for purposes of applying this Section 403.

- (b) [In any proceeding in a court to enforce a Deposited Obligation, the [form][nature] of the Obligation prior to Deposit is admitted unless specifically denied in the pleadings. If the [form][nature] of the Obligation prior to Deposit is specifically denied in the pleadings, the burden of establishing the [form][nature] of the Obligation is on the Registrant but an Instrument is presumed to have been a Writing unless the Instrument was destroyed other than by the Registry. ]

**Comment to Section 403**

In order to know what rules to apply when enforcing a Deposited Obligation it will be necessary to determine the nature of the Obligation giving rise to the Deposited Obligation at the time of Deposit – was the Obligation a Negotiable Instrument, a Non-Negotiable Instrument, a Transferable Record in a Control System or something else. Subsection (b) addresses the burdens on the parties with respect to proving the form of the Obligation at the time of Deposit.

Section 404. **Foreclosure.** Notwithstanding any state rule of law to the contrary:

- (a) Once an Obligation is Deposited with the Registry, only the Registrant of the Deposited Obligation created by such Deposit shall have the power to initiate a judicial or non-judicial foreclosure proceeding under state law with respect to the Mortgage associated with the Deposited Obligation.
- (b) Any assignment of a Mortgage made after the Deposit of the related Obligation with the Registry is not required to be recorded in a Recording Office as a prerequisite to initiation of a foreclosure proceeding, and any change in the records of the Registry of the identity of the Registrant of a Deposited Obligation shall have the same effect and serve the same notice function as the recordation of an assignment of a Mortgage under state law.
- (c) A Registrant may not initiate a judicial or non-judicial foreclosure proceeding with respect to any Mortgage Agreement relating to a Deposited Obligation unless the recording obligation set forth in Section 202(e)(4) has been satisfied.

**Comments to Section 404**

1. If this is enacted as state law, this provision will need to be revised to be more in the nature of a repealer clause and consideration of the need to amend any constitutional rule.

2. There are at least three consequences to the rule established in sections (a) and (b). First, it would alter the law in states where law has developed that suggests that an Obligation and the associated Mortgage may be separated. Next, laws that require a lender to be identified in the land records as a precondition to foreclosure would be replaced by this rule which generally looks to the Registry. Finally, this rule would make clear that even if under current law the Registrant was not

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entitled to enforce the Mortgage, once the Obligation is Deposited, the Registrant is exclusively the Person entitled to enforce the Mortgage and any other Person claiming a right to enforce would be an adverse claimant. It is important to stress with respect to this last point that if the Person claiming the right to enforce the Mortgage turns out to be the PETE (but not the Registrant), the Registrant would still be the party with the right to foreclose under this statute absent action by a court that results in a change to the Registry's records.

3. Subsection (a) as currently drafted would not permit a Registrant to have its Servicer foreclose on its behalf unless (a) the Servicer is in fact an agent under relevant state law (in which case Section 604 would apply) or (b) the Servicer becomes the Registrant. When the Servicer is or becomes the Registrant in order to initiate the foreclosure proceeding, it is the party with all of the rights and obligations under this statute. While there may be an agreement between the Servicer and the Lender limiting what the Servicer has the right to do, such contracts have no effect on parties other than the Servicer and the Lender. The Borrower, the Registry and others may rely on the Servicer's status as Registrant. To aid Borrowers in settlement discussions, in accordance with Sections 202(b)(3) and 301(b), whenever a Servicer is the Registrant, the identity of the Person for whom the Servicer is servicing must be submitted to the Registry and will be disclosed to the Borrower.

4. Of course if the Servicer is initiating the foreclosure as agent of the Registrant, any foreclosure proceeding initiated by the Servicer will need to clearly note the agency capacity of the Servicer and the identity of its principal, the Registrant. Otherwise, the proceeding can be challenged since Section 404 of this statute clearly provides that only the Registrant may foreclose. A Servicer, that is not the Registrant, acting (or appearing to act) in its own capacity would not have authority to foreclose.

5. Subsections (a) and (b) are intended to correct misreadings of existing law by the courts. Subsection (c) creates a new legal rule.

**Section 405. Recorded Mortgages**

- (a) If the Mortgage Agreement is recorded in the applicable Recording Office the Registrant shall be treated [for all purposes] as the mortgagee of record including for purposes of releasing the Mortgage.
- (b) Submission of a Mortgage Agreement to the Registry shall not be treated as recording the Mortgage Agreement in the applicable Recording Office and shall not alter the nature or priority of the Mortgage;
- (c) Any law that requires notice be given to any Person identified in the land records as mortgagee shall also require that notice be given to the Registrant of a Deposited Obligation if the recording requirement of Section 202(e)(4) has been satisfied with respect to such Deposited Obligation.

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- (d) The Registrant may act to satisfy the recording obligation in Section 202(e)(4) at any time with respect to any Deposited Obligation of such Registrant.

**Comments to Section 405**

1. Is this drafted correctly with the reference to the Mortgage Agreement or should it be the Mortgage? As these terms are taken from the draft Home Foreclosure Procedures Act, we look to guidance from the ULC drafters. Also, do these provisions work in deed of trust states?

2. The Registrant's power to act as the mortgagee of record is a corollary of the structure of this statute. Given statutes in several states that assess penalties against the mortgagee if it does not timely release the mortgage, this section does not include any discussion as to what acts a Borrower may take if the Registry records reflect that the Deposited Obligation has been fully satisfied or discharged but the Mortgage has not been released. Presumably, regardless of what this statute provides a Borrower could always record a certificate from the Registry that indicates that the Deposited Obligation has been fully satisfied or discharged. Does this statute need to address this issue?

**Subchapter 5: Warranties**

This Subchapter introduces a new set of warranties from the Depositor which serves the role of gatekeeper. This later set of warranties is arguably all that should be needed in an electronic registry scheme, and is our preference. The UCC Article 3 system of transfer warranties makes little operational sense in a centralized Registry system. It also shifts risk associated with the Registrant onto intermediate parties, who are not particularly well-suited to bear the risk. Nevertheless, this draft does not attempt to alter the UCC Article 3 scheme and in fact adopts it for all Obligations deposited with the Registry (see Section 203).

This Subchapter does not draft for a more ambitious policy: assuring the integrity of the mortgage securitization system. It does not do so because we believe that the purpose of this statute is limited to ensuring as best we can the integrity of Registry. However, the broader policy is an important one, and this statute could address it.

Fraud in the residential mortgage market has been a significant problem in recent years and the focus of legislative, prosecutorial and supervisory attention. Borrowers are protected by a growing number of consumer protection laws and CFPB regulation of the market generally (e.g., qualified mortgages)—we shall assume *arguendo* that this protection is adequate. Securities law, however, is not very effective to protect RMBS investors. It is disclosure-based, and assumes good (or at least solvent) actors. We have also seen that the other players in this market have had very little incentive, to date, to refuse to transact with bad actors or otherwise engage in serious diligence of the market players. A warranty of good behavior (essentially the veracity of upstream representations) by a solvent sophisticated party (e.g., the Depositor) would change the incentives of the system. Such a warranty would be easy to work into the structure of this statute.

Such a warranty would also transform the market, in ways both good and bad. We decided to leave such a radical idea for discussion of the concept, without the distractions of draft language.

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Section 501. **Warranties Generally**

- (a) The warranties in Subchapter 5 of this statute may not be [varied][disclaimed] by contract or System Rules. Warranties that supplement those of this statute, if consistent with System Rules and regulations, are enforceable according to the ordinary rules of contract law.
- (b) Unless indicated otherwise in this statute, a Person to whom the warranties under this Subchapter 5 are made [and who took the Deposited Obligation in good faith] may recover from the warrantor as damages for breach of warranty only an amount equal to the loss suffered as a [direct] result of the breach, but not more than the unpaid principal amount of, and interest [due to accrue on], the Deposited Obligation at the time such Person took the Deposited Obligation plus expenses incurred as a result of the breach.
- (c) Unless notice of a claim for breach of warranty is given to the warrantor within 30 days after the claimant has reason to know of the breach and the identity of the warrantor, the liability of the warrantor for breach of warranty is discharged to the extent of any loss caused by the delay in giving notice of the claim.
- (d) A cause of action for breach of warranty under this Subchapter 5 accrues when the claimant has reason to know of the breach.

**Comments to Section 501**

1. Subsection (a) reflects a judgment—based on the events of the past few years—that the warranties are too important to leave to the parties. Many of these warranties can be found in the law of negotiable instruments. UCC § 3-416. The chief difference between these warranties and those of the UCC are that these warranties are non-variable.

2. Subsection (b) requires more thought as to the measure of damages. It is drafted from the perspective of a Registrant of a Deposited Obligation and looks to provide recovery for losses suffered as a result of the breach but capped at what the Registrant would be entitled to get paid by the Borrower over the life of the Obligation that was the subject of the Deposit. Is this the right way to think about the cap or should the cap be limited to the unpaid principle amount plus any accrued but unpaid interest. Does there need to be any cap?

3. In addition to considering whether this is the right way to think about capping the liability to a Registrant, more thought needs to be given to breach of warranty claims made by a Borrower since a Borrower is the one that owes on the Deposited Obligation.

Section 502. **Depositor's Warranties.**

- (a) The Depositor of an Obligation that gives rise to a Deposited Obligation warrants to each Registrant of the Deposited Obligation and to the associated Borrower(s) that, at the time of Deposit of the Obligation:

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- (1) If the Obligation Deposited with the Registry is an Instrument, the Depositor:
    - (A) Was rightfully in possession of the Instrument when it Deposited the Instrument; and
    - (B) The Instrument was payable to bearer or to the Depositor;
  - (2) If the Obligation Deposited with the Registry is a Transferable Record, the Depositor had control of the Transferrable Record as defined under either UETA or ESIGN at the time of the Deposit;
  - (3) [To its knowledge, the Obligation had not been altered before the Deposit;]
  - (4) [It has no knowledge that the signature of the Borrower(s) on the Obligation is unauthorized];
  - (5) [It has no knowledge of an adverse claim to the Obligation];
  - (6) It has not previously deposited the Obligation in the Registry and has no [knowledge] [notice] that the Borrower(s) has signed identical Obligations; and
  - (7) If the Depositor retained the Instrument and submitted only an electronic image of such Instrument to the Registry:
    - (A) The electronic image of the Instrument accurately represents all of the symbolic information on the front and back of the Instrument as of the time of Deposit and the image conforms to the technical standards contained in any Regulation or System Rules; and
    - (B) After Deposit, the Instrument was promptly destroyed.
- (b) For purposes of this Section 502, if a Depositor uses a Third Party Service Provider to satisfy the Deposit standards set forth in System Rules or Regulations, such Third Party Service Provider also warrants to each of the warranties set forth herein in addition to the Depositor.
- (c) A Registrant that submits a modification related to a Deposited Obligation makes the warranties in this Section 502 with respect to the amendment only.

**Comments to Section 502**

1. The Depositor is the gatekeeper to the Registry. These warranties provide protections not just on Instruments but on any Obligation that is Deposited. Given the significant role played by the Depositor and the potential liability associated with these warranties, Section 201 directs the Registry to

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establish Deposit standards that take into account data quality, information security and capital. If a Depositor cannot satisfy one or more Deposit standards it may rely on a third party but under Section 201, such third party becomes responsible under the statute to the same degree as the Depositor. Thus, each of the warranties set forth in Section 502 would be made by both the Depositor and the Third Party Service Provider. We recognize that the Deposit standards could, therefore, make it more expensive for some Depositors to be able to use the Registry and, in some instances a Depositor simply may not be able to find a third party willing to act on its behalf. Because of this reality, it will be important that the Regulators carefully consider the Deposit standards proposed by the Registry and balance the need for open access to the Registry against the gatekeeper functions of the Depositors. It may also be appropriate to limit the set of warranties made by the third party depending on which Deposit standard is being satisfied by the third party service provider. So, for example, if the only function of the service provider is to meet the technology requirements for creating and submitting an image, perhaps the service provider warranty should be limited to subsections (a)(6) and (7)?

2. Subsection (a)(6) is not easy to draft. It refers to the practice of some mortgage loan originators to have the Borrower sign multiple “original” mortgage notes. Sometimes more than one of the notes gets sold in the secondary mortgage note market. This can happen due to negligence or outright fraud. The Depositor has a better chance of averting such fraud than the Registry, so the Depositor is the warrantor here. The Borrower receives no warranty for any alleged obligees who claim outside the Registry because the Depositors cannot serve as gatekeepers for those who do not deal with it. The Borrower’s relief, if any, is left to its common-law or UCC remedies.

3. Subsection (a)(7) is based on the substitute check warranties in the Check Clearing for the 21<sup>st</sup> Century Act. Because it captures all Instruments and not just Negotiable Instruments, the warranty focuses on destruction of the Instrument and not on double presentment. Depending on whether some other act is permitted, such as marking the Instrument as “deposited with the Registry,” this warranty may need to be revised.

4. The term “symbolic information” in subsection (a)(7) makes clear that the destruction of the original document unavoidably loses information, no matter how good the imaging. The highest quality image cannot reconstruct, for example, the chemical composition of the ink used to sign the Instrument. The Registry is not responsible for the loss of any information except the symbolic information conveyed by the image.

5. As drafted, these warranties cannot be disclaimed and run to each Registrant and the Borrower. Should the Depositor be able to disclaim any of these warranties? Should the warranty run only to a Registrant in privity with the Depositor? Should all of these warranties run to the Borrower or only certain warranties?

6. Certain of the warranties are drafted to require knowledge. Should these be written to include where the Depositor knows or should have known?

7. Subsection (c) reflects the view that submitting a modification of a Deposited Obligation to the Registry is the equivalent of making a deposit. Would it be better to have a separate section to

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address these Registrant warranties or is it sufficient to capture this notion within the Depositor warranties?

Section 503. **Registry Warranty.** If an Instrument is submitted to the Registry in connection with a Deposit, the Registry warrants to each Registrant identified as a Registrant of the related Deposited Obligation and to the associated Borrower(s) that:

- (a) The electronic image of the Instrument accurately represents all of the symbolic information on the front and back of the Instrument as of the time of Deposit and the image conforms to the technical standards contained in any Regulation or System Rules; and
- (b) After deposit, the Instrument was destroyed..

**Comment to Section 503**

1. In Chapter 6 there is a provision that makes the Registry liable for its failure to follow its System Rules, Regulations and this statute. Here we provide separate warranty protections with respect to the conversion of an Instrument to electronics both in terms of data integrity and in terms of potential double liability.

2. The term “symbolic information” makes clear that the destruction of the original document unavoidably loses information, no matter how good the imaging. The highest quality image cannot reconstruct, for example, the chemical composition of the ink used to sign the Instrument. The Registry is not responsible for the loss of any information except the symbolic information conveyed by the image.

- 3. Should the Registry warrant any other aspects of its operation of the system?

Subchapter 6: Miscellaneous

**Section 601. Jurisdiction and Venue of Registry**

- (a) Personal jurisdiction of the Registry is in [Alt1: the state of its organization] [Alt2: Washington, D.C.][Alt3: its principal place of business].
- (b) The System Rules shall contain a consent for jurisdiction in actions brought by a Borrower to the jurisdiction in which the [the property securing the Mortgage is located] [Borrower is domiciled.]
- (c) [Alt: Notwithstanding any other provision of law, all suits of a civil nature at common law or in equity to which the Registry shall be a party shall be deemed to arise under the laws of the United States, and the district courts of the United States shall have original jurisdiction of all such suits; and the Registry which is a defendant in any such suit may, at any time before the trial thereof, remove such suit from a state court into the district court of the United States for the proper district by following the procedure for the removal of causes otherwise provided by law.]

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**Comment to Section 601**

1. The notion in subsection (a) and (b) is that almost all claims among Registrants are claims among professionals. To avoid forum-shopping and inexperienced courts, Registrants may only sue in the Registry in its own jurisdiction. When a claim is brought by a Person other than a Registrant against a Registrant personal jurisdiction of these claims do not involve the Registry.

2. If the Registry is an instrumentality or a utility, the state of organization is appropriate. If it is a Federal agency, Washington, D.C. is appropriate. The removal language, cribbed from 12 USC § 632, is appropriate for instrumentalities or utilities, but superfluous for agencies.

Section 602. **Notice**

- (a) **[Alt1:** Notice to the Registry by a Person shall not be effective unless made in accordance with System Rules.][**Alt2:** use UCC 1 definition of notice]
- (b) Notice to the Registry from a court or court orders are effective if:
  - (1) The court has personal jurisdiction over the Registry; and
  - (2) Either:
    - (A) The court providing notice complies with System Rules; or
    - (B) The Registry has had reasonable time to act on the notice or order.

**Comment to Section 602**

1. The “reasonable time to act” language in subparagraph (b)(2)(B) is pervasive in the UCC. It protects intermediaries—who are responsible for real-time execution of instructions—from court orders that coincide with the instructions. The Registry does not need such protection if a court complies with System Rules (*e.g.*, uses the Registry’s website rather than paper).

2. Borrowers, like any other Person, are expected to comply with System Rules. However, the need for CFPB approval and public comment of System Rules should protect Borrowers from unreasonable technological expectations.

- 3. Note that subsection (a) is not subject to subsection (b), because a court is not a Person.
- 4. As noted in alternative 2, another option is to use the definition in UCC Article 1.

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Section 603. **Evidence.** The Registry's records satisfy the best evidence rule.

**Comments to Section 603**

1. This section may be useful in proving the terms of the Obligation and the Mortgage Agreement. These records are not conclusive, and the parties to any litigation are free to object that the records do not reflect the true agreements or Instruments executed by the parties. Note that the statute does not require that the original Mortgage Agreement be tendered to the Registry, although it does expect submission of the Instrument (query whether more needs to be done in the statute to address what is meant by submitting the Instrument where the Instrument is a non-Negotiable Instrument. The Registry's records will presumably all be electronic.

2. The final draft of the statute may permit or require the Registry to retain the original Instrument for a period of time. If such a requirement exists, should the Registry be required to produce the original Instrument? The drafters note that such a requirement would in essence turn the Registry into a custodian and require an investment in paper custody that may not be warranted as the industry transitions to an all-electronic market.

Section 604. **Supplemental Principles of Law.** Unless displaced by the particular provisions of this statute [and the Regulations and System Rules adopted pursuant to it], other law and the principles of law and equity, including the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, and other validating or invalidating cause, supplement its provisions.

Section 605. **Liability.**

(a) Unless stated otherwise in this statute, a Person (other than the Registry) is liable for damages in the amount of any loss caused [directly] by the failure of such Person to comply with this statute, Regulations or System Rules[ and reasonable attorney fees]. Unless expressly provided for in this statute or in Regulations, incidental, consequential, and punitive damages shall not be recoverable.

(b) Unless stated otherwise in this statute or in Regulations,

(1)The Registry shall be liable to a Depositor, a Registrant, or a Borrower only for damages in the amount of any loss caused [directly] by the failure of the Registry to comply with this statute, Regulations or System Rules.

(2) The Registry shall not be liable to any other Person for its actions or inaction except where such Person establishes that the Registry, in error or without authority, caused such Person to lose or fail to attain the status of Registrant.

(3) Incidental, consequential, and punitive damages shall not be recoverable from the Registry.

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(4) The Registry shall not be entitled to assess or otherwise seek indemnification or contribution from Depositors, Registrants or Borrowers for any losses for which it is responsible under this subsection (b), where the Registry's liability was the result of its bad faith, wilful misconduct or gross negligence.

**Comment to Section 605**

1. This section is a bit of a placeholder. We need to make sure that this provision is sufficient for addressing the different scenarios that might give rise to losses as a consequence of the actions or inactions of the Registry. Strict liability of the Registry for violation of its own System Rules, regulations or this statute fits the ordinary intuition that an intermediary should be responsible for its own operational delicts and nothing else. But will this provision sufficiently address operational errors such as an error or mistake in carrying out an instruction of a Registrant?

2. Because of the role played by the Registry, the drafters thought it important to limit the types of Persons that can seek to recover from the Registry.

3. The statute is drafted so that only money damages are available to a Person who asserts a claim that an error or other wrongful act of the Registry deprived that Person of the status of Registrant. The statute could be drafted to provide that such a Person could seek the right to become the Registrant but such an approach is complicated where innocent third parties have obtained the status of Registrant in the interim. The drafters believe that money damages from the Registry should be sufficient in such instances. An aggrieved party might also have a claim against the wrongfully named Registrant.