

## UCC DIGITAL ASSET AMENDMENTS: IMPLICATIONS FOR CRYPTO MARKETS

- Sponsors of the Uniform Commercial Code (“UCC”) recently finalized amendments to the UCC to address emerging technologies (the “2022 Amendments”).<sup>1</sup> If adopted at the state level, the 2022 Amendments should clarify the application of UCC rules to secured transactions, creditor rights, custody and transactions involving the purchase and sale of certain digital assets.
- The 2022 Amendments include a new Article 12 and related updates to Article 9 for transactions involving “controllable electronic records” such as Bitcoin and Ether as well as such records that may develop in the future. These updates generally enable a party to perfect a security interest in such records by obtaining “control”. Article 12 also includes negotiability provisions that generally provide for the priority of a “qualifying purchaser” with control of such records over competing property claims, including an earlier security interest that has been perfected under the UCC.

This briefing provides a high-level summary of certain key aspects of the 2022 Amendments related to digital assets. We encourage readers to reach out to the contacts listed below with any questions or requests for additional detail, including in relation to other aspects of the 2022 Amendments not addressed in this briefing.

### Control of Digital Assets under the UCC

Prior to the 2022 Amendments, the UCC did not include digital asset-specific provisions addressing (i) when a secured party has “control” of digital assets such that its security interest prevails over competing creditor claims, or (ii) when a purchaser of such assets has “control” for purposes of acquiring its interest free of competing claims, such as an earlier perfected security interest.

### Key issues

- Control of Digital Assets Under the UCC
- New Article 12: Controllable Electronic Records
- Definitions of “Money” and “Electronic Money”
- Indirect Holding of Digital Assets
- Effective Date

## New Article 12: Controllable Electronic Records

The 2022 Amendments create a new Article 12 (*Controllable Electronic Records*), which includes specific provisions addressing the acquisition and disposition of security and other property interests in a “controllable electronic record”, which is a record stored in an electronic medium that can be subjected to “control” under UCC §12-105. Such records include Bitcoin and Ether as well as certain other digital assets that may be developed in the future.

“Control” of such records generally means the person has a private cryptographic key or other technology that gives the person: (i) the power to avail itself of substantially all of the benefits of the record, the exclusive power to prevent others from availing themselves of such benefits, and the exclusive power to transfer control of the record to another person; and (ii) the ability to readily identify itself as having the powers specified in (i).

To the extent Article 12 and related amendments to Article 9 apply, a party that obtains control of such records benefits from added protections corresponding to the capacity in which it is transacting:

- **Secured Party:** Although it is also possible to perfect a security interest in such records by filing a financing statement, a secured party that perfects by control has priority over a secured party that does not have control, including one that has otherwise perfected its security interest.
- **Qualifying Purchaser:** A good faith purchaser for value of such records benefits from new negotiability provisions. If such a purchaser obtains control without notice of a property claim in such records, it is a “qualifying purchaser” that takes its interest in such records free of an earlier security interest, even if perfected.

These control, perfection and negotiability provisions only apply to a subset of digital assets that fall within the definition of “controllable electronic record” and certain accounts and payment intangibles evidenced by such a record. Other digital assets are subject to separate UCC provisions.

## Definitions of “Money” and “Electronic Money”

The 2022 Amendments update the UCC definition of “money” to exclude electronic records of a system that existed and operated as a medium of exchange prior to being authorized or adopted by a domestic or foreign government, such as Bitcoin, which was adopted by El Salvador and the Central African Republic. The 2022 Amendments also add the new “electronic money” property category for money in an electronic form, which is subject to specific control, perfection and negotiability provisions.

## Indirect holding of Digital Assets

The 2022 Amendments include helpful clarifications to Article 8 indicating a securities intermediary and its customer can agree to treat certain digital assets as “financial assets” subject to the UCC provisions applicable to “investment property”, aligning with existing market practice in relation to digital asset custody and the perfection of security interests in digital asset collateral under an “Article 8 opt-in” indirect holding structure. For additional detail, please refer to our previous client briefing discussion on **Creating and Perfecting Security Interests in Cryptoassets**.

## Effective date

Although the 2022 Amendments contemplate that each state will select its own effective date, they include an “adjustment date” concept that is meant to provide a phase in period of at least one year from effectiveness before new rules would apply to pre-existing interests (among other things). Some states have taken steps to adopt versions of Article 12 and related amendments. We encourage readers to contact our team members with any questions about the current status of the amendment process and the application of the rules to specific digital asset lending and trading arrangements.

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## Endnotes

1 UNIF. COM. CODE & EMERGING TECHS. Art. 12, §12-105 (Unif. L. Comm'n & Am. L. Inst. 2022), available at <https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=67fe571b-e8ad-caf8-4530-d8b59bdca805&forceDialog=1>.