

U. S. Department of the Interior
Assistant Secretary—Indian Affairs
Office of Indian Energy and Economic Development
Division of Economic Development

Tribal Economic Development Principles at a Glance Series

Why Tribes Should Adopt a Secured Transactions Code



This is the third in a series of economic development primers prepared by the Indian Affairs Office of Indian Energy and Economic Development (IEED), Division of Economic Development (DED), U.S. Department of the Interior, to offer answers to fundamental questions about creating jobs and expanding economies in federally recognized tribal communities.

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If you would like to discuss tribal secured transactions codes in more detail, please contact the Division of Economic Development at (202) 208-0740.

What is a secured transaction?

A secured transaction is an agreement between two parties in which one of the parties gives property (other than real estate) as collateral – or security – for a loan. There are two types: one that involves a “possessory security interest” (Example A) and another that involves a “non-possessory security interest” or “lien” (Example B):

Example A:

Tom seeks to borrow \$2,000 from Mary. Mary agrees to loan Tom the money but wishes to have some means of being paid back should Tom default. Mary knows that Tom has a hand-crafted roping saddle worth \$2,000 and that this can become collateral for the loan. So she asks Tom to give her possession of the saddle until the loan is repaid. Mary takes possession of the saddle (still owned by Tom) and thereby obtains a possessory security interest in it. If Tom pays back the loan, Mary must return the saddle to him. But if Tom fails to pay back the loan, Mary may sell the saddle and retain the portion of the sale proceeds that she needs to pay off the balance of the loan.

Example B:

The facts are the same except that Tom and Mary sign a “security agreement” giving Mary a non-possessory security interest or “lien” on the saddle. In this case, Tom retains possession of his saddle. Should Tom fail to pay off the loan, Mary will be able to take possession of the saddle, sell it, and retain the portion of the sale proceeds that she needs to pay off the balance of the loan.

Why are non-possessory security interests important?

Liens like the one described in Example B enable businesses to obtain the credit they need to buy office or farm equipment, machinery, vehicles used for business, and other tangible personal property used in commerce. Likewise, they enable consumers to buy on credit the tangible items that businesses produce or sell, including vehicles and appliances.

Why are secured transactions codes needed?

Laws are needed to enforce the liens or security interests of creditors. If such laws did not exist or were not enforced, sellers of goods would be reluctant to accept anything but cash for the full sales price of any tangible items they might otherwise sell on a credit basis. Likewise, lenders would be reluctant to loan unless they knew with certainty that a borrower would repay. This would prevent businesses from starting up or expanding because they could not obtain key equipment, machines, or vehicles, or may not have access to operating lines of credit.

These laws are important, too, because they provide a means of reconciling competing claims in collateral by establishing who has priority when there are several claimants.

Why does Indian Country in particular need secured transactions codes?

Without such codes and an accurate, reliable and publicly accessible system for filing claims, tribal firms are often unable to finance the purchase of business-related equipment from sellers located outside tribal jurisdictions because a dealer cannot enforce its lien (or security interest) in the purchased item once it has been transported to a reservation. Or, if tribal firms are able to access financing, it may be at higher interest rates and for shorter terms, thereby making the credit unaffordable. This is because most tribes have not adopted a secured transactions code together with a reliable and modern lien filing system to specify how security interests may be created, perfected, and enforced. Absent these rules, creditors may increase borrowing costs to offset risks or refuse to lend altogether.

Affordable credit is a daunting problem in Indian Country. Eighty-six percent of tribal lands do not have a bank and 15 percent of American Indian and Alaska Natives live 100 miles or more from one.¹ Of financial institutions on or near tribal communities, only 33 percent offer start-up loans, only 29 percent offer small business loans, and just 26 percent offer micro business loans.²

Entrepreneurs and investors depend on a strong legal infrastructure to protect their interests. Commerce is inhibited when financial transactions lack certainty and protection. Lenders are willing to lend when they can rely on a secured transactions code to assure that they will be repaid in the event of a default. Access to affordable credit is a fundamental component of sustainable economic development in all modern market economies.

Here's an example of how the lack of a secured transactions code can block economic development in a tribal community:

Bob is a young tribal member living on the reservation. He is a capable auto mechanic who wants to purchase auto repair equipment in a border town so that he can start an auto repair business. Because there are no auto repair shops on the reservation, tribal members are anxious for Bob to open one.

Since Bob just graduated from high school and is living with his family, he does not have enough savings to afford the \$5,000 price of the equipment he needs. There are no banks on the reservation, and the bank in the border town will not lend to him because he has no permanent job and has not established a credit record.

Bob's only alternative is to buy the equipment on credit from a border town store. The proprietor of this store is impressed by Bob and is willing to sell him the equipment on credit until he learns that Bob lives on the reservation.

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¹ Drew Tulchin and Jessica Shortall, "Small Business Incubation and Its Prospects in Indian Country," Social Enterprise Associates, December 2008, p. 1

² *Ibid.*

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“I’m willing to sign a contract to make monthly loan payments with interest, just like most of your other customers who don’t pay with cash,” Bob protests. “What’s the problem?”

The proprietor shakes his head saying, “The other customers you refer to all live in town. If any of them stop making their monthly payments, I have a lien on the items they’ve purchased and can repossess those items. But, I cannot enforce a lien on anything I sell to you because there is no way to protect my interest under tribal law. If I sell you the equipment on credit and you stop paying me, I have no way to recover the equipment and I’ll be out \$5,000.”

The result is that Bob is unable to start his business and the tribal community will not have a local auto repair shop.

Are tribes required to write their own secured transactions codes?

They can. But this is unnecessary because the National Conference of Commissioners on Uniform State Laws (NCCUSL) and a working group of tribal officials have already drafted the Model Tribal Secured Transactions Act (MTSTA) as a template for legislation by tribes to facilitate transactions between lenders and businesses. The model, created in 2004, was drafted with the objective of creating a uniform tribal secured transactions law consistent with Article 9 of the Uniform Commercial Code (UCC) in tribal business, legal, and cultural environments. NCCUSL and the American Law Institute drafted the UCC in the 1940s to establish a consistent legal framework for commercial dealings between parties from different states. Every state plus the District of Columbia, Puerto Rico, and the U.S. Virgin Islands has adopted the UCC. Article 9 of the UCC covers secured transactions.

While the MTSTA differs from UCC Article 9 in a number of ways, its major principles, terminology, and processes are similar enough to the UCC to ensure that tribal and non-tribal practitioners can work effectively within both tribal and state jurisdictions.

What does the MTSTA do?

The MTSTA provides a set of rules that specify how security interests may be created, perfected, and enforced, and who has first rights when two or more competing creditors have legally enforceable interests in the same collateral. Under this system, a creditor files a financing statement at a public filing office that constitutes notice to other interested parties about security interests in the personal property of the debtor. This financing statement perfects (or makes good against third parties) a creditor’s security interest in most kinds of personal property.

What is the core purpose of the MTSTA?

Its main purpose is “*to promote economic development by encouraging and supporting business dealings between tribal entities, tribal member-owned businesses and tribal consumers, and financial institutions and other businesses outside of a Tribe’s jurisdiction*” (Comment on MTSTA §9-103).

Is there something more a tribe must do in addition to adopting the MTSTA?

Yes, adopting a secured transactions code is just the first step. The next, indispensable step is for a tribe to provide a means of recording financing statements. A financing statement notifies the public that the creditor/secured party may have a lien on the personal property of a particular debtor. Public filing offices determine when filings will be accepted, how records must be maintained, what kind of fees will be charged, and how information is made available to the public. In most states, it is the Secretary of State who administers the UCC filing office. For most tribes, setting up a reservation-based financing statement filing system would be prohibitively expensive. Generally, tribes also lack the capacity and training to administer these systems. A more practical approach for a tribe that has adopted the MTSTA is to enter into a joint powers agreement, memorandum of understanding, or compact with the state to administer the financing statements that arise from the tribe’s secured transactions code. Another advantage to state systems is that they are electronic and accessible online. The MTSTA specifically authorizes tribes to use state filing systems (MTSTA §9-501(g)).

IEED has made itself available to help tribes negotiate joint powers agreements, memoranda of understanding, or compacts with states in order to include in state commercial lien recording systems financing statements and liens incident to tribal commercial codes. Some tribes have adopted codes but failed to designate a filing system, while others have adopted codes and designated a state filing system but neglected to enter into a formal agency arrangement with the state filing office.³

³ “Implementation Guide and Commentary to the Model Tribal Secured Transactions Act,” National Conference of Commissioners on Uniform State Laws, 2005, p. 94.

When a Tribe adopts a secured transactions code, is it waiving sovereign immunity?

No. Adopting a secured transactions code has no effect on sovereign immunity and, in itself, is an act of self-governance and sovereignty. The MTSTA contains a section not contained in UCC Article 9 that protects the sovereign immunity of a tribal nation, plus its agencies and instrumentalities, and any waiver of sovereign immunity “must be approved by an authorized representative or governing body of the Tribe and appropriately recorded” (Comment on MTSTA §9-102). The MTSTA also contains a provision on choice of law that preserves tribal sovereignty even if another state or federal law applies to the transaction or a part of it (MTSTA §9-117).

What if a tribe were to adopt the official text of UCC Article 9 rather than adopting the MTSTA?

This would be ineffective as this version is just a template and contains many blank spaces. Nor was it designed, as MTSTA was, specifically for tribal nations.

Why can't a tribe just adopt Article 9 as it was enacted by the state in which the tribe is located?

Nothing prevents a tribe from doing so. However, unlike the MTSTA, state codes were not devised with tribal nations in mind, so state codes may contain provisions that do not comport with tribal law and custom.

What if a tribe adopts its own unique version of Article 9?

Again, it is within the power of a tribe to do this. But, the danger in doing this is that some provisions of the tribe's code may not synchronize with the state's code. Tribal secured transactions are supposed to make credit transactions between persons on and off the reservation more seamless and fluid, less troublesome, less likely to lead to misunderstandings, and more apt to encourage commerce. Those with provisions that are not materially similar to those of the state code may have the opposite result.

But, isn't adoption of a secured transactions code just an invitation to non-tribal members to come on the reservation and repossess personal property held by tribal members? Won't this lead to trouble?

No. The MTSTA allows a creditor/secured party to repossess collateral after the debtor's default only by consent of the debtor after the default occurs or through a judicial process, and all repossessions must be done without "breaching the peace" (MTSTA §9-609).

Repossession occurs as a last resort by a secured party dealing with loan or other credit agreement payments that are overdue or nonexistent who has obtained from the borrower a financing statement filed in accordance with the code, thereby perfecting his or her rights in the property. A security agreement usually defines what constitutes a debtor's default. Default occurs when the debtor either fails to make a payment when due or violates his or her security agreement.

After a debtor defaults, the secured party may obtain possession or control of the collateral by written consent of the debtor or by obtaining an order from the tribal court. The secured party can then sell the property and pay off the debt (or a portion of it) with the proceeds, or, in some cases, keep the collateral to satisfy the debt. The debtor can reacquire (redeem) the collateral by paying off the debt before the collateral is sold.

Wouldn't it be a better idea then for a tribe to adopt the MTSTA, but delete provisions authorizing repossession?

No. This would be self-defeating as it would essentially neuter the code. It is unlikely that a creditor will allow anyone to purchase on credit where the creditor cannot repossess the personal property that has been financed. Without a provision authorizing repossession, someone buying personal property on credit could stop their payments and remove it to the tribal community where it could not be lawfully repossessed.

Are there any kinds of personal property that a tribe should consider removing from the scope of a secured transactions code?

Yes, a tribe can insert a provision into its code that prohibits, for example, the pledging of sacred objects as collateral for credit transactions or loans. The MTSTA includes as a "usage of trade" a local custom or tradition of the tribe. The MTSTA's implementation guide points out that if a provision of the MTSTA conflicts with a tribal custom or tradition, the tribe should consider which should take precedence and specify that result in its enactment of the law. Transfer of sacred objects out of tribal possession is an example of this kind of conflict (MTSTA §9-114).

Has IEED had a role in tribes adopting the MTSTA?

Yes. Tribal adoption of the MTSTA has long been a priority for IEED and the Division of Economic Development has funded several tribes to explore adoption of commercial law codes modeled on the MTSTA: the Chippewa Cree Indians of the Rocky Boy Reservation (2005); the Crow Tribe (2005); the Arapaho Tribe of the Wind River Reservation and the Shoshone Tribe of the Wind River Reservation (2005); the Confederated Tribes of the Warm Springs Reservation (2006); the Seminole Nation of Oklahoma (2006); the Sac & Fox Nation (2006); the Oglala Sioux Tribe (2006); the Blackfeet Tribe (2006); the Confederated Tribes of the Umatilla Indian Reservation (2006); and the Tulalip Tribes (2006). However, this funding is no longer available.

In 2007, DED organized with the National Congress of American Indians the National Native American Economic Policy Summit in Phoenix, Arizona, which was attended by over 500 tribal and federal representatives. Among the 100 recommendations adopted by tribal leaders at the Summit was to “Develop commercial codes that can be adopted or customized by each tribe. . .”.⁴

In FY 2012 and FY 2013, DED joined with the U.S. Small Business Administration (SBA) and the Federal Reserve System to sponsor at six key Indian Country locations training workshops for tribal government and business representatives on how adoption of the MTSTA can boost creditor and investor confidence in tribal economies and ensure the steady growth of business and consumer credit on reservations.

⁴ Native American Economic Policy Report, NCAI and IEED, 2007, p. 6.



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