

A R T I C L E

# Enabling Investment in Environmental Sustainability

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This Article proposes an “environmental practices money security interest” (EPMSI) that lawmakers could add to Uniform Commercial Code (UCC) Article 9.<sup>1</sup> The EPMSI would grant priority over earlier investors to financiers whose extensions of credit enable debtors to invest in improving environmental impact.

An extensive conversation about creating incentives for commercial actors to take more responsibility for environmental harm is underway. Very few participants, however, identify commercial finance law as a potential site for developing these types of incentives.

Imagine a company that wants to renovate its manufacturing processes to reduce waste and utilize alternative fuels. Such renovation could require contracting with various experts, service providers, and engineers, as well as acquiring both tangible and intangible property. A company may want to undertake this type of improvement but be unable to do so because it lacks either internal funds or the capacity to issue low-risk debt to pay for the process. The company may lack the capacity to issue low-risk debt because an existing secured creditor has a floating lien on the company’s assets and this creditor is unable or unwilling to fund the renovation process. The proposed EPMSI rules would create a collateral-security device that private parties could elect to use in this type of situation.

The EPMSI concept invokes difficult questions. Why rely exclusively on government subsidies such as tax credits and subsidized loans to induce investments in improved environmental impact when we could also enact commercial law devices that do so? At the same time, why disrupt secured creditors’ priorities and risk a negative response in the credit market to address environmental concerns that should be left to regulation? The complete version of this

Article delves more directly into these difficult tensions.<sup>2</sup> This version presents the EPMSI as concisely as possible.

The proposed EPMSI would put secured lenders in the position of either funding costs of improvements in environmental impact, or risking subordination to a financier who will. In some instances, engaging in environmental practices may yield very tangible returns for debtors; in others, the value of services may be harder to calculate or may be externalized. The EPMSI rules could allocate to secured parties the costs of creating environmental benefits that could accrue to society at large. An exception to first-in-time priority for EPMSI creditors would require a legislative determination that, when companies seek financing for environmental practices, they should have the capacity to issue high-priority debt.

The issue of creating costs that yield externalized benefits pervades thinking about responsibility for the environment. If costs are always imposed on the public because the public benefits, then private actors have no incentive to reduce the harm they inflict—short of civil or criminal liability. At the same time, if certain private actors bear costs the benefits of which are externalized, and they cannot do so and stay profitable, then this creates other costs to the public that we must consider.

Government subsidies for “green” investment allocate the costs of inducing such investment to the public. One could argue that a device like the EPMSI that allocates costs to private parties is not as desirable as public subsidies because secured lenders, if an EPMSI were enacted, would charge more for credit and lend less, passing costs on to companies in ways that hinder growth.

But even if we assume that creditors, to some extent, would lend less if states enacted EPMSI rules, this alone does not justify rejecting the EPMSI. It just complicates fundamental questions surrounding the EPMSI concept. What is better, maximum access to credit or the capacity to issue high-priority debt to fund improvements in environmental impact? Responding to imminent environmen-

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*This Article is excerpted from the Indiana Law Journal, 85 IND. L.J. 597 (2010), and is reprinted with permission.*

1. U.C.C. §9 (2005). Unless otherwise indicated, citations herein to the UCC are to the official text and comments of the American Law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL).

2. See Heather Hughes, *Enabling Investment in Environmental Sustainability*, 85 IND. L.J. 597 (2010).

tal problems will be costly; failing to adequately respond would be much more costly.

Some may consider any proposal that would result in credit constriction to be bad or unjustified unless its benefits were proven to outweigh the costs associated with credit constriction. This type of proof is extremely difficult, if not impossible, to make. Questions about how best to induce desirable modes and levels of investment are precisely what this work hopes to invoke.

UCC Article 9 currently contains rules creating the purchase-money security interest (PMSI) for acquisition of goods, and the production-money security interest (PrMSI) for agricultural finance. The PMSI is included in UCC Article 9 in all states. The current PrMSI rules appear in appendix II to Article 9. Six jurisdictions have enacted these rules.<sup>3</sup> The PMSI and the PrMSI are “super-priority” security interests: so long as PMSI and PrMSI creditors comply with the relevant notice provisions of Article 9, they enjoy priority in advance of earlier secured claims.

States could draw on the PMSI and PrMSI rules to create an EPMSI. Generally speaking, interests that enjoy later-in-time priority present risk of dilution of earlier creditors’ claims. Numerous scholars have observed that the tracing and identifiable collateral requirements that limit the scope of PMSIs temper this threat of dilution. In the case of the EPMSI, service providers and providers of assets other than goods may be EPMSI creditors. While environmental practices money collateral may include assets to which earlier creditors are looking for security, notice requirements and limitations on the scope of EPMSI collateral can contain the threat of dilution of earlier creditors’ claims.

UCC Article 9 sets forth the order of priority in which various creditors take from an insolvent debtor’s assets. Generally, these rules grant priority to secured over unsecured creditors. Secured creditors’ priorities rank in the order in which each creditor came along—first in time, first in right.<sup>4</sup> However, some security interests enjoy later-in-time priority. These “super-priority” security interests enjoy an exception to the general rule to enable or facilitate the type of credit they involve. In essence, by permitting certain secured creditors to prevail over earlier secured creditors, the code, as Hideki Kanda and Saul Levmore put it, “compromises between the advantages and the disadvantages of ‘new money.’”<sup>5</sup>

As we consider these advantages and disadvantages, two points about UCC Article 9 become important. First, legal scholars overstate the extent to which the purchase-money rules avoid dilution risk by limiting PMSI collateral to new goods. Second, scholars tend to overlook the existence of the production-money interest in agricultural

finance in analyses of Article 9 and interests with later-in-time priority.

In a nutshell, conventional wisdom holds that the limitation of interests with later-in-time priority to new assets acquired with new value is key to the coexistence of floating liens and super-priority security interests. But this conventional wisdom about interests with later-in-time priority plays down both: (1) the reality that the purchase-money rules do present risk to earlier creditors, and (2) the existence of the production-money interest in agricultural finance (in which the later-in-time creditor’s interest is not limited to new goods and their identifiable proceeds).

Much of the scholarly analysis of PMSI rules seems to assume an idealized form of purchase-money interest, rather than a reality in which purchase-money interests are risk altering. As with any type of credit, a debtor can use PMSI credit to acquire new equipment or inventory that takes the company’s business in a new direction that ultimately hurts its creditors.

With respect to the PrMSI, perhaps scholars regard this device as an anomaly limited to agricultural finance. But the current PrMSI, along with its predecessor 9-312(2), disrupts the notion that we can explain the coexistence of first-in-time and later-in-time interests under Article 9 completely in reference to the PMSI’s strict, asset-based nature. The existence of the PrMSI complicates the notion that Article 9’s approach to priority is a coherent scheme in which interests with later-in-time priority are neatly contained to purchase-money situations in which debtors acquire new goods that are the later creditors’ collateral.

My complete article discusses at greater length (i) theoretical understandings of later-in-time priority, the PMSI and PrMSI, (ii) the issue of costs of credit and imposing costs on secured creditors, and (iii) other basic questions that the EPMSI concept raises. These include the effects of negative pledge clauses, the possibility of debtor abuse of the EPMSI, and concerns about proposals to enact rules creating special priority for loans to enable whatever other objectives lawmakers may deem worthy of incentivizing. Again, the purpose here is just to present the EPMSI.

The structure of and policies behind the PMSI offer a framework for thinking about the proposed EPMSI. Similarly, the evolution under Article 9 of production-money interests in farm products provides insight into super-priority security interests that is useful to consider when contemplating an environmental-practices-money interest. The EPMSI concept, in important ways, both draws upon and departs from the models provided by these interests.

A PMSI arises when a secured party’s extension of credit enables the debtor to acquire new goods such as inventory or equipment.<sup>6</sup> These rules enable a debtor to have some latitude in seeking new assets and new credit despite the presence of an existing secured creditor with substantial control over the debtor. Also, purchase-money credit can benefit the prior secured creditor because the debtor is get-

3. See ME REV. STAT. ANN. tit. 9, §1324-A (Supp. 2008); MISS. CODE ANN. §75-9-324A (2004); N.C. GEN. STAT. §25-9-324.1 (2003); W. VA. CODE §46-9-324a (LexisNexis 2007); WISC. STAT. ANN. §409.3245 (West 2003); WYO. STAT. ANN. §34.1-9-324A (2009).

4. See U.C.C. §9-322 (2005).

5. Hideki Kanda & Saul Levmore, *Explaining Creditor Priorities*, 80 VA. L. REV. 2103, 2105 (1994).

6. See U.C.C. §9-103.

ting assets on better terms than it otherwise could—assets that are not part of the collateral pool to which prior creditors were looking for security.

But debtors can apply PMSI credit in ways that (1) sink a debtor deeper into debt when it cannot pay all of its obligations, or (2) enable the debtor to acquire assets to move in a new direction that hurts the debtor's financial performance. Some scholars point out that because the PMSI creditor comes later in time, it has better, more current information with which to determine whether its loan is too risky. While this observation may be true, it does not change the fact that the PMSI rules present risk to earlier creditors.

On the environmental front, innovative processes and equipment that improve environmental impacts of doing business are proliferating. Many of these innovations are expensive and many are speculative in the sense that they are new and in the sense that it is unclear whether or not companies can internalize the benefits of investment in them. The range of investments that companies are seeking to improve environmental efficiency is broader than investments in new equipment or other goods.

As the PrMSI rules show, the notion that special priority rules should apply in certain contexts to service providers is not new. Currently only six states offer enhanced priority for holders of production-money interests, but before 2001, forty-five states and the District of Columbia enacted an earlier form of the PrMSI in old section 9-312(2).

There are several, major differences between PMSIs and PrMSIs. Some of these differences fuel the lack of consensus over model section 9-324A. In important ways, the proposed EPMSI has more in common with the production-money interest than with the more widely accepted purchase-money interest.

One significant difference is that the PMSI collateral constitutes new goods, while the collateral securing the PrMSI may be the same farm products to which a prior creditor is looking for its security. This can be the case, for example, when the PrMSI creditor provides services, seed, or fertilizer that is promptly used up in crop production. The proposed EPMSI would also differ from the PMSI in that EPMSI creditors may provide services (for example, to make facilities more energy efficient). The environmental-practices-money collateral, then, may include assets to which earlier creditors are looking for security.

Both the PrMSI rules and the proposed EPMSI rules limit the super-priority security interest to the extent of new value that the creditor provides. In the PrMSI context, this new value is supplies or services to yield new farm products. Though the PrMSI is not limited—like the PMSI—to new goods and their identifiable proceeds, there is a relationship between production-money credit provided and the farm products that the debtor then produces.

In the EPMSI context, a creditor that enables environmental practices may not, in many cases, assist the debtor in developing or acquiring discrete, new property. The new value an EPMSI creditor provides may create savings

in energy or waste management costs, reduced liabilities under environmental regulations, new intellectual property, or enhanced good will, for example. In some instances the benefits of investment in environmental practices may be externalized entirely. Depending on tolerance for risk of dilution of earlier creditors' claims, EPMSI collateral could be as broad as all the debtor's personal property, or as narrow as, for example, specific intellectual property acquired with environmental practices money credit.

The purpose of presenting draft provisions 9-324B and 9-103B here is to make the EPMSI concept as concrete as possible. Notice and priority provisions could be drafted as follows:

9-324B. PRIORITY OF ENVIRONMENTAL PRACTICES MONEY SECURITY INTERESTS.

(a) Except as otherwise provided in subsections (c), (d) and (e), if the requirements of subsection (b) are satisfied, a perfected environmental-practices-money security interest in environmental-practices-money collateral has priority over a conflicting security interest in the same collateral and, except as otherwise provided in Section 9-327, also has priority in their identifiable proceeds.

(b) An environmental-practices-money security interest has priority under subsection (a) if:

(1) the environmental-practices-money security interest is perfected by filing when the environmental-practices-money secured party first gives new value to enable the debtor to engage in environmental practices;

(2) the environmental-practices-money secured party sends an authenticated notification to the holder of the conflicting security interest not less than 10 or more than 30 days before the environmental-practices-money secured party first gives new value to enable the debtor to engage in environmental practices if the holder had filed a financing statement before the date of the filing made by the environmental-practices-money secured party; and

(3) the notification states that the environmental-practices-money secured party has or expects to acquire an environmental-practices-money security interest in the debtor's property and provides a description of the environmental-practices-money collateral.

(c) Except as otherwise provided in subsection (d) or (e), if more than one security interest qualifies for priority in the same collateral under subsection (a), the security interests rank according to priority in time of filing under Section 9-322(a).

(d) To the extent that a person holding a perfected security interest in environmental-practices-money collateral that is the subject of an environmental-practices-money security interest gives new value to enable the debtor to engage in environmental practices and the value is in fact so used, the security interests rank according to priority in time of filing under Section 9-322(a).

(e) To the extent that environmental-practices-money collateral is also purchase-money collateral [or production-money collateral], the notice and priority rules applicable to purchase-money security interests under Section 9-324 [or production-money security interests under Section 9-324A] shall govern.

There are two main challenges to defining the scope of an EPMSI. The first challenge is defining the range of credit extensions that would give rise to this type of interest. The second challenge is determining to what assets an EPMSI should attach, given that environmental-practices-money creditors may be providing services or other value and looking to the same assets as earlier creditors for security.

The most difficult provisions to craft are subsections defining “environmental practices” and “environmental-practices-money collateral.” For purposes of an EPMSI, “environmental practices” should refer, speaking generally, to practices, processes, or projects that businesses undertake to improve the impacts that their activities have on natural resources. This is a broad and potentially amorphous category of undertakings. People commonly invoke the concept of “environmental sustainability” to refer to the goals of these kinds of practices. But defining environmental sustainability is complicated such that defining environmental practices as practices that improve environmental sustainability compounds the challenge.

Nonetheless legislatures, industry groups, international organizations, and others have engaged in defining the concepts of “environmental sustainability,” “sustainable development,” “renewable energy” and other similar concepts for purposes of lawmaking and for defining best practices.

One approach to defining “environmental practices” for EPMSI purposes is to draw from these efforts. A second approach is to cross reference existing statutory provisions that concern environmental impact. In any event, the task is to create a working definition that is concrete enough to define a particular type of extension of credit, yet broad enough to refer to this type of credit as it may arise in diverse contexts.

9-103B. ENVIRONMENTAL-PRACTICES-MONEY SECURITY INTEREST; APPLICATION OF PAYMENTS; BURDEN OF ESTABLISHING

(a) Definitions. In this section:

(1) “environmental-practices-money collateral” means [ALTERNATIVE 1: personal property that secures an environmental-practices-money obligation] [ALTERNATIVE 2: intellectual property acquired or developed with environmental-practices-money credit] [ALTERNATIVE 3: deposit accounts of the debtor containing cash derived from savings in energy costs];

(2) “environmental-practices-money obligation” means an obligation of an obligor incurred as all or part of the price of goods or services or for value given to enable a nonconsumer debtor to engage in environmental practices if the value is in fact so used; and

(3) “environmental practices” means [ALTERNATIVE 1: practices, processes, or projects undertaken to improve environmental impact or sustainability] [ALTERNATIVE 2: engagement of services or acquisition of personal property for the purpose of improving energy efficiency, reducing carbon emissions, increasing use of renewable energy, retaining ecosystem services, or minimizing loss of plant or animal habitat] [ALTERNATIVE 3: An investment is one in environmental practices if it improves the environmental impact of the debtor’s activities. An investment does this if it reduces carbon emissions made by the debtor or caused by the debtor’s products. An investment does not improve the environmental impact of the debtor’s activities if it is not used to make a material change in the debtor’s processes, practices, or property intended to improve the environmental impact of debtor’s business.] [ALTERNATIVE 4: engagement of services or acquisition of property [that entitles the debtor to a tax benefit authorized pursuant to Colo. Rev. Stat. 31-20-101.3] or [to effectuate a “direct emissions reduction,” “emissions reduction measure,” or “market-based compliance mechanism” as defined in California Health and Safety Code §§ 38505(e), (f) and (k), respectively]].

[Subsections (b)–(d) track the language found in uniform section 9-324 and model section 9-324A.]

The first three alternatives in draft 9-103B(a)(3) above attempt substantive definitions. The safe-harbor provisions in Alternative 3 could be enacted along with the definitions in Alternatives One or Two.

Alternative One is obviously very broad, and it may be the least desirable of the proposed rules in terms of clarity. General definitions of sustainability tend to be stated very abstractly. They articulate general standards that, if breached, may result in liability. They are not necessarily designed to define a set of practices that result in sustainability. Conversely, the concrete definitions of environmental sustainability tend to be industry specific. These definitions are so detailed that they tend to be useful only for companies involved in the particular industry for which the standards are articulated.

Under these draft rules, an EPMSI creditor is required to give notice to earlier creditors before the EPMSI arises. Debtors and creditors need to be able to know whether they are creating an EPMSI in advance of the extension of credit that finances the qualifying practice.

Lawmakers could allow private actors to work out among themselves, to a large extent, what would constitute “environmental practices.” If disputes arise, then courts would participate in the process of delineating what constitutes “environmental practices” for purposes of section 9-103B(a)(3). While clarity at the outset could be an issue (and lack of clarity itself has costs) this approach would create an expansive range of contexts in which private actors could utilize the EPMSI.

Alternative Two presents the same general considerations as Alternative One, except that it refers to a set of

concepts that is more specific than “environmental impact or sustainability.” By reigning in the definition of “environmental practices,” Alternative 2 clarifies the kinds of activities that could give rise to an interest with later-in-time priority, if they are undertaken with EPMSI credit. If a legislature finds clarity to be more important than creating a security device with broad applicability, more specific formulations that also contain substantive definitions of concepts like “renewable energy” or “reducing carbon emissions,” could be appropriate.

Earlier creditors could contest EPMSI status upon receiving the notice required by proposed section 9-324B, leaving the debtor and the later-in-time creditor to work out whether they believe that the later-in-time credit will finance activities that are clearly within the contemplation of section 9-103B(a)(3). This approach raises the questions of (1) whether the rules should require an objection notice within a certain time after receipt of section 9-324B notice from the debtor, and (2) whether failure to object should constitute a waiver of rights in a priority dispute.

State legislatures could create a regulatory board that comments on, or certifies in response to inquiries, what constitutes “environmental practices.” This approach has drawbacks, too, of course. If commercial actors needed to look to the state for a continually evolving definition of “environmental practices” for EPMSI purposes, that would create a lot of state involvement in commercial affairs. However, defining “environmental practices” entirely within the four corners of 9-103B could institutionalize the status quo. This institutionalization could codify a conception of environmental practices based on dominant practices today, when approaches to improving environmental impact are rapidly evolving.

One response here could be to use safe-harbor provisions that offer clear instructions to parties engaging in activities that currently fall squarely under “environmental practices,” and yet leave open the possibility of new practices. Alternative Three in proposed section 9-103B(a)(3) presents an example of such a provision. A safe harbor could enable debtors and creditors to transact with certainty about the security interest’s EPMSI status. At the same time, it would not prohibit debtors and investors with a greater appetite for risk from entering into transactions that they believe are EPMSI transactions, even though the investment at issue does not fall into previously contemplated categories of “green” investment.

Legislators could formulate 9-103B in an altogether different way as well—by cross-reference to existing statutory provisions. A majority of states in the United States have enacted legislation addressing the issue of climate change. These statutes include definitions of terms such as “renewable resource,” “renewable energy,” or “alternative fuel” that 9-103B(a)(3) could reference.

This approach may make EPMSI definitional provisions easier to draft, but the definitions cross-referenced may be broad, imprecise, or not drafted from a secured transactions perspective. These other statutory definitions

may have been promulgated in a context in which a state agency exists to elucidate the meanings of terms, and definitions enacted in state climate change statutes may evolve over time or be elucidated by case law or regulation. In addition, this approach also may raise delegation of lawmaking issues.

In any event, the proposed Alternative Four in draft 9-103B(a)(3) contains two examples of how cross-referencing for purposes of defining “environmental practices” might be done. The Colorado code section referenced here authorizes governing bodies in the state to offer, notwithstanding any law to the contrary, incentives “in the form of a municipal property tax or sales tax credit or rebate, to a residential or commercial property owner who installs a renewable energy fixture on his or her residential or commercial property.”<sup>7</sup> A “renewable energy fixture” means “any fixture, product, system, device, or interacting group of devices that produces energy . . . from renewable resources, including, but not limited to, photovoltaic systems, solar thermal systems, small wind systems, biomass systems, or geothermal systems.”<sup>8</sup>

“Environmental practices” for purposes of an EPMSI could be defined as engagement of services or acquisition of property that entitles the debtor to a tax deduction authorized by these provisions. (A cross-reference to these Colorado provisions would require revisiting section 9-334 of the UCC regarding priority of interests in fixtures. Section 9-334(d) could be amended to include EPMSIs along with PMSIs as interests that, in accordance with section 9-334, can have priority in advance of an encumbrancer or owner of real property.)

Acquisition of goods—the actual solar panels or wind turbines, et cetera—in conjunction with an investment that would give rise to a tax benefit could be financed with purchase-money credit. The environmental-practices-money creditor, in this context, would be important to the extent that a debtor must invest in services or assets other than goods to make an investment in a “renewable-energy fixture.” A creditor that both provides services and finances the acquisition of a renewable-energy fixture would have a purchase money interest in the fixture itself and an environmental-practices-money interest in the fixture and any other related environmental-practices-money collateral.

The California Global Warming Solutions Act of 2006<sup>9</sup> offers another example of state climate change legislation that EPMSI provisions could cross-reference. This Act authorizes the State Air Resources Board to promulgate regulations and programs to reduce greenhouse gas emissions. The State Air Resources board is “a state agency charged with monitoring and regulating sources of emissions of greenhouse gases that cause global warming in order to reduce emissions of greenhouse gases.”<sup>10</sup>

7. COLO. REV. STAT. §31-20-101.3(1).

8. *Id.* §31-20-101.3(2).

9. CAL. HEALTH & SAFETY CODE §§38500–01, 38505, 38510, 38530, 38550–51, 38560–62, 38564–65, 3870–71, 38580, 38590–99.

10. *Id.* §38510.

This board is authorized, among other things, to issue regulations creating “market-based compliance mechanisms” to reduce greenhouse gas emissions.<sup>11</sup> Under the statute, “market-based compliance mechanism” means either of the following:

- (1) A system of market-based declining annual aggregate emissions limitations for sources or categories of sources that emit greenhouse gases.
- (2) Greenhouse gas emissions exchanges, banking, credits, and other transactions, governed by rules and protocols established by the state board, that result in the same greenhouse gas emission reduction, over the same period, as direct compliance with a greenhouse gas emission limit or emission reduction measure adopted by the state board pursuant to this division.<sup>12</sup>

These provisions contemplate an emissions credit or trading system. For purposes of an EPMSI, “environmental practices” could be defined as engagement of services or acquisition of property to effectuate an emissions reduction or a market-based compliance mechanism within the meaning of the climate-change statute.

If California, for example, were to consider EPMSI rules that cross-reference this Global Warming Solutions Act, the result could be, essentially, a type of purchase-money interest in emissions credits or “carbon credits.” This possibility raises the question of whether EPMSI rules should be geared towards funding compliance with existing requirements, or, on the other hand, facilitating funding for investments that companies might not otherwise make. Speaking hypothetically, if compliance with emissions caps were required by law, and the relevant emissions credit system in place permitted purchase of credits as a means of compliance, then EPMSI credit to facilitate such purchasing would allocate to secured parties costs that companies must incur anyway. At the same time, debtors, perhaps, could benefit from the capacity to issue low-risk debt to finance costs of compliance in situations where existing secured lenders will not do so. EPMSI credit could give companies access to a wider range of financiers and a wider range of options for effectuating compliance. The appropriate scope and applicability of the EPMSI concept, in this regard, requires further contemplation and debate.

The scope of “environmental practices” and “environmental-practices-money collateral” affects the EPMSI provisions’ potential to enable transactions that dilute earlier creditors’ claims. At the broad end of the spectrum in terms of EPMSI collateral, EPMSI rules could create a later-in-time interest with priority in all personal property assets of the debtor.

But we can imagine broader and narrower versions of EPMSI. It is conceivable that EPMSI rules could limit EPMSI collateral to a segregated asset to which earlier creditors are not looking for security (hence, minimizing dilution risk).

Another device for limiting the threat of dilution of earlier creditors’ claims is to provide notice to these creditors of an impending super-priority security interest. If an earlier creditor has notice that the debtor plans to grant an EPMSI, it can re-negotiate with the debtor, extend credit for environmental practices itself, or otherwise protect against the dilution threat.

Secured parties could respond to EPMSI rules with contract provisions prohibiting debtors from assigning new security interests. Promises by debtors not to grant to any other person a security interest in the assets assigned—negative pledge clauses—are common. Negative pledge clauses do not block creation of later security interests, but they are a strong deterrent. Many debtors would be unlikely to avail themselves of EPMSI credit if doing so constituted a default under their existing credit agreements.

States that want to enact EPMSI rules and also preserve debtors’ capacity to utilize these rules despite negative pledge clauses could do so with statutory provisions that render ineffective contract provisions making assignment of an EPMSI an event of default. For example, North Carolina responds to this issue in the PrMSI context by enacting a nonuniform subsection (f) in its version of section 9-324A that makes ineffective contract provisions (1) prohibiting the creation of PrMSIs, or (2) making the creation of a PrMSI an event of default.<sup>13</sup>

Negative pledge clauses may pose a greater threat to the use of EPMSIs than they do to PMSIs and PrMSIs because EPMSIs would present, potentially, greater dilution risk. Whether secured creditors use these clauses, and debtors agree to them, would depend upon the particularities of new transactions.

As ideas emerge for financing investment in improved environmental sustainability, we should not overlook the UCC as a potential site for innovation. Ultimately, levels of commitment to mechanisms for private funding of improved environmental impact, and of tolerance for risk of dilution to secured creditors’ positions, are for collective determination.

11. *Id.* §38570(a).

12. *Id.* §38505(k).

13. N.C. GEN. STAT. ANN. §25-9-324.1 (West 2003).