

Overview of NZ PPSA & Some Practical Implications for Trans-Tasman Financing

Presented by: **Mark O'Regan and Matt Yarnell**
Chapman Tripp, Wellington
New Zealand

→ Cheaper, Faster, Simpler and Safer

Overview of NZ PPSA & Some Practical Implications for Trans-Tasman Financing

Objectives

- Provide a brief overview of key aspects of NZ PPSA
- Raise issues regarding possible application of NZ PPSA
- Focus on some practical implications for Trans-Tasman financing

Overview

- A. What does the PPSA do?
- B. When will it become effective?
- C. How are PPSA security interests created?
- D. Key terms
- E. Priority
- F. Effect of non-perfection
- G. Enforcement
- H. Conflict of laws
- I. Trans-Tasman financing transaction – sample transaction and practical issues

A. What does the PPSA do?

- regulates the registration, priority and enforcement of security interests over personal property (not land) – wide scope
- imposes “good faith” obligation on secured parties (s.25) (can parties to a security agreement agree in advance what will constitute good faith?)
- replaces various statutes that had different documentation and registration requirements and priority regimes (e.g. Chattels transfer Act 1924)
- same rules apply whether the debtor is company, individual, trust etc. – regardless of form or who has “title” to the personal property – but, how PPSA applies is influenced by “type” of collateral (e.g. consumer goods)

B. When will it become effective?

- regulations and on-line register still required (further amendments to PPSA may be made)
- best guess: end Q1 2001
- six month transitional period
 - ↳ register/reregister (identify transactions affected)
 - ↳ debtor will need to sign “romalpa” terms of trade (s.36)
 - ↳ adequacy of description of collateral and proceeds (ss.36/46)

C. How are PPSA security interests created?

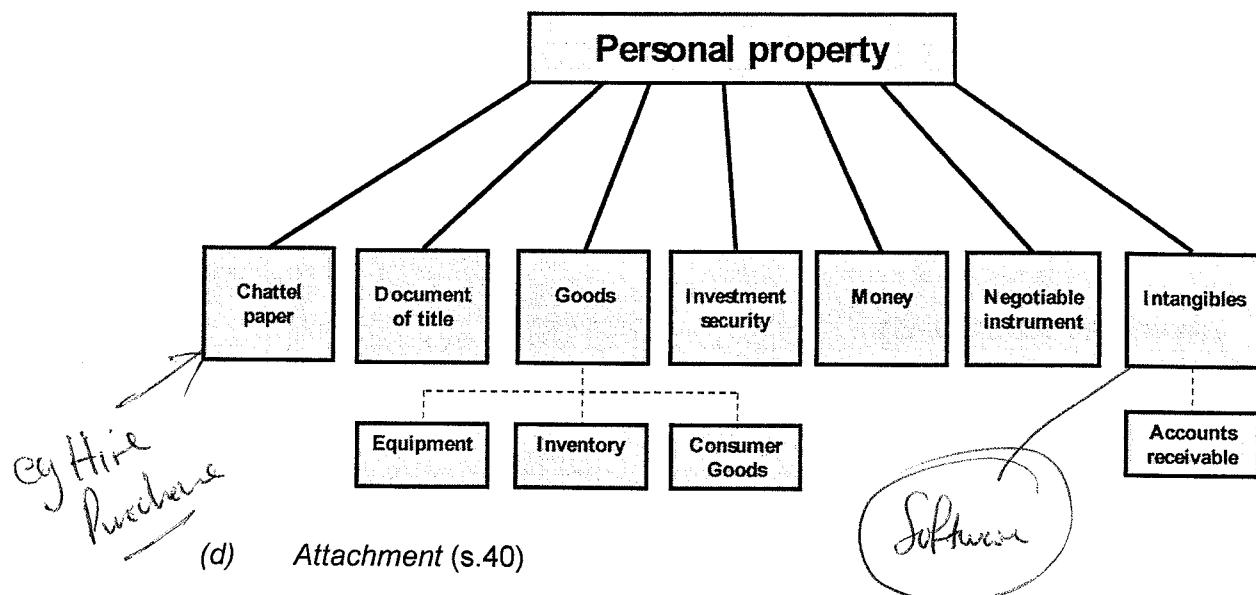
- no need for special documents or language to create security interests
- no need for different type of security interest depending on type of collateral
- certain distinctions are no longer relevant under PPSA:
 - ↳ legal/equitable
 - ↳ fixed/floating
 - ↳ mortgage, charge, assignment, pledge etc.

D. Key terms

- security interest
- purchase money security interest (PMSI)
- personal property
- attachment
- perfection
- (a) *Security interest (SI) (s.17)*
 - any transaction that:
 - ↳ creates an interest in personal property
 - ↳ to secure payment or the performance of an obligation
 - focus is on the *substance* of the transaction
 - *deemed* security interests (whether or not it “secures” performance or payment)(s.17(1)(b)):
 - ↳ lease having a term of more than 1 year
 - ↳ transfer of accounts receivable
 - ↳ commercial consignments (e.g. floor plan financing/other inventory financing so long as both parties deal in the goods in the ordinary course of business)
- (b) *Purchase money security interest (PMSI)*
 - security interest in collateral taken by secured party providing credit to purchase that collateral (e.g. seller)
 - includes “romalpa” terms of sale and the interest of a lessor of goods under a lease for a term of more than 1 year
 - no need for holder of PMSI to give notice to prior chargeholder

- financiers may want to regulate/restrict creation of PMSI's in documentation (e.g. approval of PMSI terms)

(c) *Personal Property*



- occurs when:
 - ↳ secured party has given value; and
 - ↳ debtor has rights in collateral (whether or not debtor has title; and
 - ↳ in respect of third parties, the security interest is enforceable (s.36)
- s.36 compliance:
 - ↳ collateral is in secured party's possession OR debtor has *signed* security agreement *adequately describing* the collateral
 - ↳ description of collateral can be all present and after acquired property
 - ↳ requirements for "serial numbers"
- (e) *Perfection (s.41)*
 - security interest has attached
 - secured party has *registered* a financing statement OR has *possession* of collateral ("possession" excludes seizure/repossession; special rules for investment securities/negotiable instruments – ss.18/48)

- order of attachment and perfection not relevant
- perfection extends to proceeds (s.45)

E. Priority

- general rules (s.66) – subject to special rules under PPSA
 - between security interests**
 - perfected security interest has priority over unperfected one
 - priority of 2 perfected security interests determined by order of registration
– “first to file” rule
 - perfected PMSI has super-priority
 - priority of 2 unperfected security interests determined by order of attachment
- other interests in the collateral**
- buyer/lessee of collateral for value takes free from unperfected security interest (s.52) (no general “without notice” requirement)
- execution creditors have priority over unperfected security interests if collateral seized
- exceptions to general priority rules for:
 - ↳ buyer or lessee in “ordinary course of business” of seller/lessor’s business
 - ↳ buyer or lessee of consumer goods of less than \$2,000 value
 - ↳ consumer buyer or lessee of motor vehicle from licensed motor vehicle dealer
 - ↳ cash
 - ↳ purchaser taking possession of negotiable instruments or investment securities without notice of security interest

F. Effect of non-perfection

- unperfected security interests are not void against a liquidator or official assignee (c.f. s.18 Chattels Transfer Act 1924, s.103 Companies Act 1955)

G. Enforcement

- statutory remedies include sale and application and retention of collateral
- receiver's rights and powers are not limited by the enforcement provisions of the PPSA (practical issue - reconciliation with Receiverships Act)
- purchaser from a secured party takes free from subordinate security interests

H. Conflict of Laws (by reference to Australia/NZ)

- NZ law applies if (s.26):
 - ↳ collateral (goods/non-possessory security interest in chattel paper, investment security, negotiable document of title, money or a negotiable instrument) in NZ at date of attachment
 - ↳ collateral (goods) in Australia at date of attachment but secured party knew it would be moved to NZ
 - ↳ security agreement governed by NZ law
 - ↳ NZ law otherwise applies

NB – uncertificated investment security situated where records of clearing house or depository kept

- if collateral (goods) are exported from Australia to NZ, PPSA provides for "continued perfection" or "temporary perfection" upon their arrival in NZ
- "continued perfection" – if security interest perfected in Australia, it will continue to be perfected in NZ if perfected in NZ by the earliest of:
 - ↳ 60 days after goods are brought to NZ
 - ↳ 15 days after secured party knows the goods have been brought to NZ

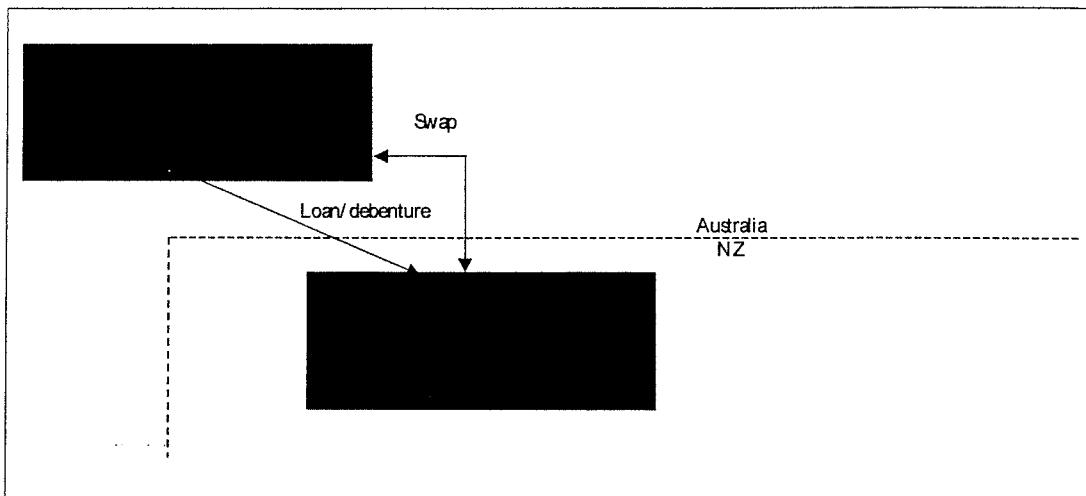
- ↳ when perfection ceases in Australia

Still permitted to perfect under PPSA outside these time frames – but could lose priority

- “temporary perfection” – if security interest *not* perfected in Australia, temporary perfection in NZ for 30 working days after collateral moved to NZ
- Australian law (including conflict rules) applies if debtor “located” in Australia when security interest is in:
 - ↳ an intangible (e.g. account receivable or contractual rights)
 - ↳ equipment or inventory leased to others and which is normally used in more than 1 jurisdiction (e.g. aircraft)
 - ↳ non-possessory security interest in chattel paper, investment security, negotiable document of title, money or a negotiable instrument (e.g. assignment of hire purchase agreements, without possession)
- if a NZ debtor moves from NZ to Australia (or transfers collateral to a party located in Australia), perfected security interest remains perfected in NZ if perfected in Australia by the earliest of:
 - ↳ 60 days after relocation of debtor to Australia or transfer of collateral
 - ↳ 15 days after secured party knew of relocation/transfer



H. Trans-Tasman Financing Transaction – Sample Transaction

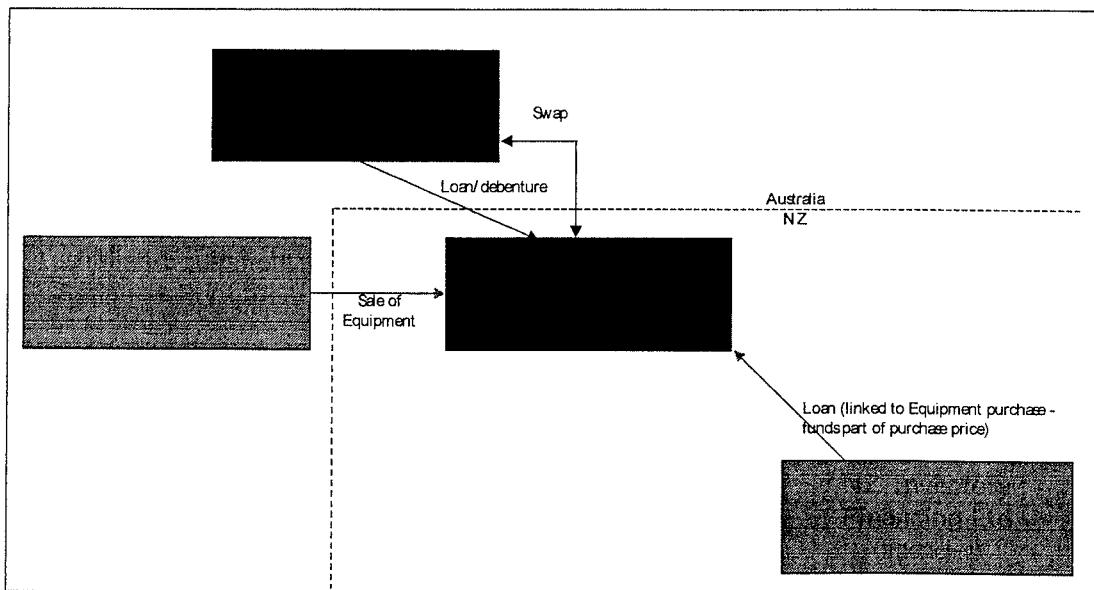


(a) NZM – financing by AGF:

- ↳ all “present and after-acquired property” (s.36)
- ↳ register financing statement (FS) - old law/priorities apply during transitional period if pre-PPSA debenture
- ↳ description of “proceeds” - impact of current “floating charge” language (i.e. scope of authorised disposal of collateral – ordinary course of business prior to default) on AGF’s ability to trace collateral (s. 45) and preferential creditor priorities
- ↳ “all obligations” - if NZM guarantees obligations owed to AGF by another person, AGF will owe disclosure obligations to NZM as a “debtor” (for PPSA purposes) (e.g. notice of enforcement against guaranteed party)
- ↳ Possible new PPSA-specific obligations:
 - ↳ prohibit creation of other security interests – what about “deemed” SIs (e.g. romalpa terms of trade with NZM’s suppliers)?
 - ↳ Put third parties on notice of the terms of the debenture (s.53 – lessee/buyer without notice of breach)
 - ↳ Notify AGF if:

- ↳ PMSIs created
- ↳ goods move outside NZ (e.g. need to register FS under Australian PPSA)
- ↳ goods acquired which need to be identified by serial number in FS (unnecessary if SI includes all “after-acquired property”?)
- ↳ change in nature of business – classification of goods changes from equipment to inventory (priority determined at time of attachment, but application of other PPSA provisions may be affected)
- ↳ debenture (i.e. security agreement) needs to provide for future advances (s.71)
 - ↳ “secured indebtedness” from time to time enough? cross reference back to loan agreement? (Saskatchewan PPSA includes “related agreements”) – risk for AGF if construed strictly
 - ↳ Status of advances made before security agreement entered into or before SI perfected (s.72 – all advances have same priority)
 - ↳ no need for priority amount – but s.80A(2), Property Law Act 1952 still relevant to land (review s.80A references in pre-PPSA debenture – unilateral subordination agreement in favour of other secured parties?)
 - ↳ subsequent amendments to debenture – when is a new SI created (e.g. expand class of obligations secured or class of beneficiaries)? Risk of intervening interests (other than other secured parties) in collateral
- ↳ register FS in advance of providing financial accommodation
- ↳ can have charge over NZM’s deposit account with NZIF (s.17(2) – *Re: Chargecard*)
- ↳ contracting out – debtor rights on enforcement (right to “reinstate” security agreement)

- ↳ NZM liquidation – preferential creditors have priority over SIs over inventory/accounts receivable
- ↳ swap (A\$/NZ\$; fixed/floating interest) – netting/set off agreement – not registrable (s.23(c))



(b) Sale of Equipment by AES

- ↳ secured sales transaction – PMSI
- ↳ must register FS within 10 working days of debtor taking possession of "equipment" to get super-priority
- ↳ if "inventory" must register FS before debtor takes possession
- ↳ retention of title by AES not sufficient protection ("romalpa" previously effective without registration)
- ↳ debtor (NZM) must sign security agreement
- ↳ adequate description of collateral
 - ↳ includes "proceeds" and the collateral itself – tracing issues, AES's rights in respect of non-cash proceeds (e.g. interest in hire purchase agreements)
 - ↳ serial number required? (regulations yet to come)(if AES gets it wrong on FS, subsequent buyer without knowledge)

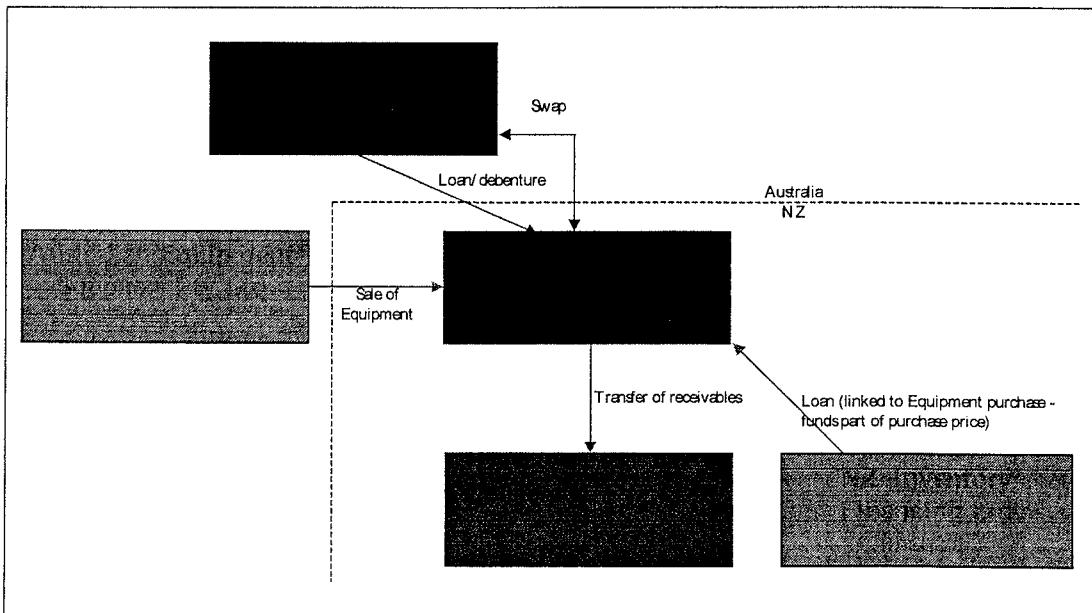
could take free from AES's SI - s.55, search of register by subsequent buyer not enough to give it knowledge)

- ↳ commingling – special rules
- ↳ if FS registered in time, priority ahead of debenture (even if FS for debenture registered first and AES knows about AGF debenture or that it is a breach of the terms of the debenture)
- ↳ AES not obliged to notify AGF of creation of PMSI (any restriction in debenture?)
- ↳ registration invalid if FS "seriously misleading (s.150)
- ↳ even if unregistered, still has priority over unsecured creditors (not void against liquidator of NZM)
- ↳ won't secure amounts owing other than purchase price for those goods
- ↳ "software" component of equipment - status of software licence as collateral (intangible personal property)? (s. 30 – conflict of laws, likely to be governed by Australian law)
- ↳ Financier to AES – ensure NZ PPSA registration of all SIs over personal property which will be moved to NZ (e.g. exporters of manufactured goods to NZ)

(c) NZM – Financing by NZIF

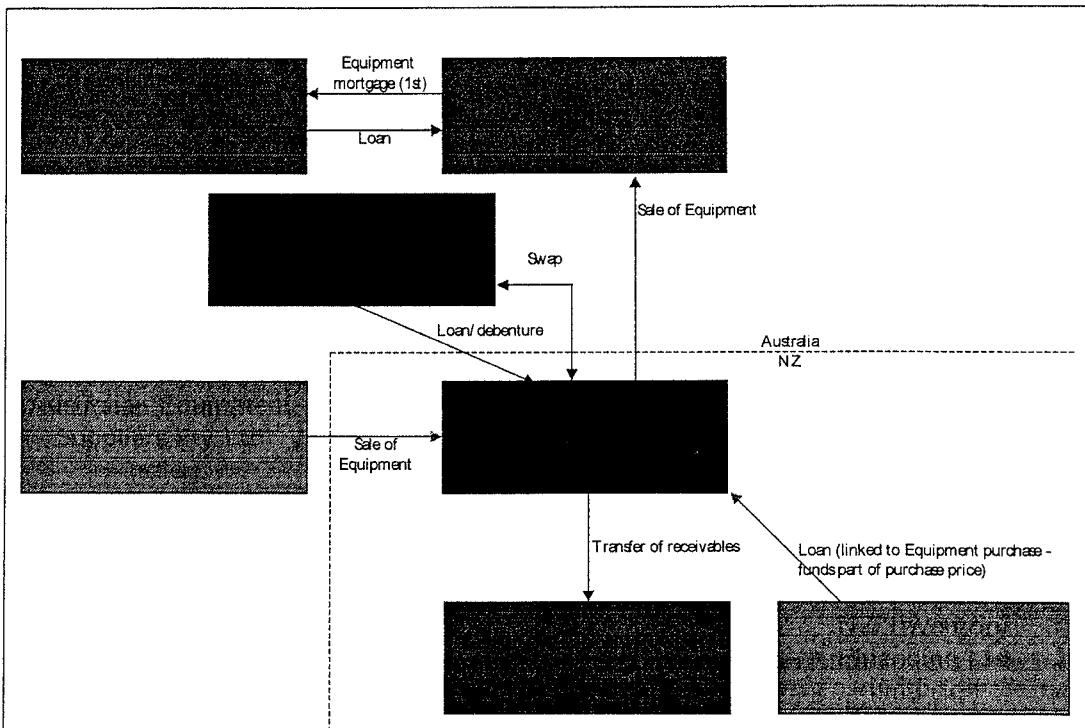
- ↳ PMSI – if loan applied to acquire Equipment
 - ↳ degree of linkage – evidentiary issue
 - ↳ advanced after purchase/refinancing
- ↳ priority – if perfected by registration
 - ↳ ahead of AGF debenture
 - ↳ behind AES – seller's PMSI (if perfected in time, s.76) (even if NZIF registered FS first)
- ↳ may secure other amounts owing (c.f. AEG PMSI)

- ↳ if AEG and NZIF SIs are not perfected *in time*, an Australian financier of AEG which has a SI in the equipment gets
 - ↳ “temporary perfection” (if unperfected in Australia)
 - ↳ “continuing perfection” (if perfected in Australia)



(d) Transfer of accounts receivable to CollectaCo

- ↳ “deemed” security interest (s.17)
- ↳ exceptions - sale of accounts receivable as part of sale of business and assignment of accounts receivable to facilitate collection (c.f. factoring) (s.23)
- ↳ needs to register FS to perfect SI (not always previously registrable)
- ↳ CollectaCo’s rights subject to prior “equities” (e.g. set-off between NZM and customers) unless NZM’s terms of trade exclude customers right to assert such defences
- ↳ Problem for factor – AES (PMSI supplier) has priority over proceeds of sale of inventory (s.74) (i.e. AES will have a better claim to the proceeds of sale of the Equipment than CollectaCo - previously, factor would have an absolute assignment of the account receivable)



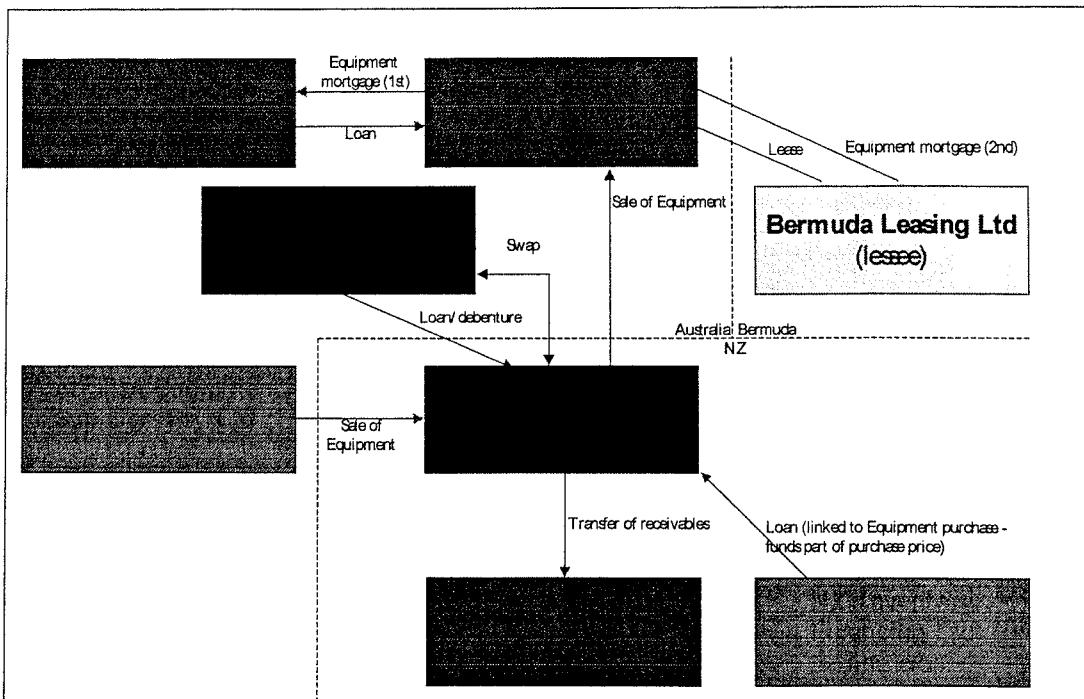
(e) Sale of Equipment to OL

- ↳ equipment free of SIs? - ensure purchase price applied to discharge AES and NZIF security interests and that each releases property from its SI – order/timing (what about CollectaCo's interest in the account receivable due from OL – priority of interest?)
- ↳ Sale in NZM's "ordinary course of business" – rights of buyer in goods (status of software licence?) (s.53)
- ↳ OL not in "possession" of the Equipment – risk that NZM might sell it a second time:
 - ↳ s.27 of Sale of Goods 1908 - second purchaser gets good title if acting in good faith and without notice of the previous sale
 - ↳ currently address risk by registering "bill of sale" under Chattels Transfer Act 1924 (repealed by PPSA)
 - ↳ s.53(2) provides that a second purchaser from MZM, in the ordinary course of NZM's business, takes free of SIs given by MZM, unless second purchaser knows the second sale is in breach of the security agreement (what constitutes requisite knowledge?)

- ↳ s.53(2) of PPSA prevails over s.27 to the extent that NZM retains possession with consent of secured party - but, OL does not have a security interest if it is a true sale

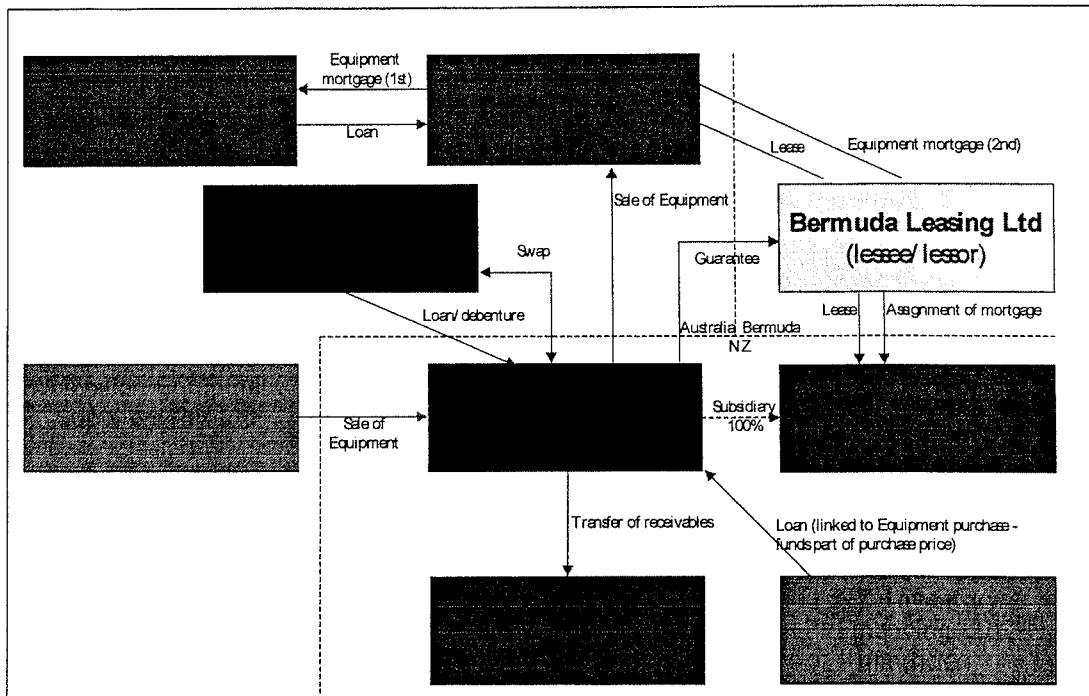
(f) OL – financing by ABC

- ↳ competing SI in goods – check for registration of SIs in NZ/Australia (due diligence regarding identity of previous owners of goods)
- ↳ ABC will have a PMSI if its loan relates to acquisition of Equipment by OL – priority between ABC PMSI and NZIF PMSI
- ↳ loan/security agreement expressed to be governed by Australia law
- ↳ general rule - NZ law applies to Equipment (goods) (re: validity, perfection and effect of perfection or non-perfection of SI in goods) because collateral located in NZ when SI attaches (s.26)
- ↳ BUT:
 - ↳ if Equipment constitutes goods that are normally used in more than 1 jurisdiction and held by OL for lease, or
 - ↳ if Equipment constitutes intangibles (software rights),
Australian law applies (s.30 – location of debtor when SI attaches)
- ↳ if SIs *not* registrable in Australia, ABC's SI could be subordinate to other interests in the goods (s.32) – therefore, register FS in respect of SI created by equipment mortgage (1st)



(g) Lease of equipment by OL to BL

- ↳ deemed SI and PMSI, if term of more than one year (subject to PPSA perfection and enforceability requirements) – register FS in respect of lease
- ↳ PPSA enforcement rights/remedies provisions don't apply (Pt 9) if not a lease which comes within generic "security interest" wording ("finance leases" do secure performance/payment; "operating leases"/"true leases" likely to constitute deemed SIs)
- ↳ register FS in respect of SI created by equipment mortgage (2nd) (purchase option) (see above)



(h) Lease of equipment by BL to NZL (with NZM guarantee)

- ↳ register sublease – deemed SI and PMSI (but, application of “sale and leaseback” exception to PMSI)
- ↳ if Equipment constitutes intangibles (rights to use software), Bermudan law applies (s.30 – location of debtor when SI attaches)
- ↳ if such a SI not registrable in Bermuda, NZL’s SI could be subordinate to other interests in the goods (s.32) – therefore, register FS in respect of SI created by assignment of equipment mortgage (2nd) (purchase option) (NB. not previously registrable under Chattels Transfer Act 1924)
- ↳ order of FS registration where structured transaction?
- ↳ NZM guarantee of NZL’s obligations – NZM a “debtor” (BL will owe disclosure obligations to NZM as “debtor” (for PPSA purposes - e.g. notice of enforcement against guaranteed party))

[Handwritten signature]