Submission to “Inquiry into the Personal Property Securities Bill 2008 [Exposure Draft]” to the Senate Standing Committee on Legal and Constitutional Affairs

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To: Committee Secretary
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This Submission is a response to the call for further comments on the Exposure Draft of the Personal Property Securities Bill 2008 issued on 12 November 2008 by the Senate Standing Committee on Legal and Constitutional Affairs, a branch within the Commonwealth Attorney-General.

I have been a law academic for over the past ten years, researching and teaching mainly in the field of corporate/commercial law. I am currently at Deakin University School of Law, and prior to that, I was at Monash University Department of Business Law and Taxation for some five years. In addition to my main research and interest in corporate law, I also have some interest in banking and finance law and this has been through my research and teaching of lending law (and company law) while I was at Monash University. Prior to that period, I practised as a corporate lawyer both in Australia and in Singapore.

Most of the comments I intend to provide in this submission will be in relation to fixed and floating charges, particularly when the charges are created over book debts and their proceeds. The submission will be focusing on the interaction between the proposed PPS Act and the currently existing Corporations Act (C’th), which is the Act that regulates priority ranking of charges and distribution of funds, together with other related Acts and with general laws. My comments are provided under the following headings.

Insufficient time for public comments:
I wish to first congratulate the Commonwealth Attorney-General for taking the initiative to put the personal property securities reform project back on the table and for taking a proactive step in moving this project forward. Having said this, I do not
understand why there is a need to rush through the reform process. On its website, the Commonwealth Attorney-General has made a public announcement, on several of the webpages, that the Attorney-General is expecting the PPS Bill to “commence as law by May 2010”, ie as an Act. There is no other information on its website advising on the parliamentary reform process other than the Attorney-General’s Department’s timeline, which appears to be rather constricted in the durations given for public consultations and comments.

The reform agenda for this project started in April 2006. The first draft of the PPS Bill 2008 (called the Consultation Draft of the Personal Property Securities Bill 2008) was released for public comments in May 2008, with a closing date 3 months later on 15 August 2008. At the close of the submission date and soon after and unlike some other law reform bodies, there was no information given on the website regarding the number of submissions received and the range of contributors; the only information publicly available was that the Attorney-General’s Department has noted the six key issues in point form that require special attention, saying that “the industry has highlighted [six key issues]... as warranting closer attention. Specifically, key input that will be reflected in the final Bill will cover... [the paragraph went on to list out the six key issues in point form]”. Subsequent to that, the second draft of that Bill (called, “Personal Property Securities Bill 2008 [Exposure Draft]”) was then released on 12 November 2008, calling for further public comments to be made by 10 December, that is, within 28 days from the date the second draft was released. By the look of things and by the way the reform process has been carried out, I find it hard to understand why there is a need for such urgency in this matter.

I can appreciate the need for consolidating laws on personal property securities and the importance of having a centralised online registration system for all personal property securities and I can also see many of the benefits that come with that system and I fully support that move, but I think a delay of another two to three years in the reform process would not adversely affect Australia’s position in the global market. Currently, there are over 70 pieces of both federal and state and territory legislation operating in this area, and the consolidation in this area requires careful examination of all these legislation. In order to save everybody’s time in the long run and to minimise the number of cases going to court for judicial interpretations, for example, on the ambiguous and conflicting terms and principles, and to minimise the parties’ costly litigation and court expenses, my view - to put it simply - is that we must invest more time, more resources, and more efforts into trying to get this project done properly and to get it right the first time.

**Expected “commencement date”:**
My next comment is in regard to the expected “commencement date” shown on the website. I do not think it is appropriate to announce publicly on its website that the
PPS Bill will “commence as law in May 2010”. By having the Attorney-General’s Department giving this information to the general public about the commencement date, it creates an impression, and wrongly so, that the Attorney-General has the power to set a commencement date for an Act, that the Attorney-General is more superior than the Parliament, and that the PPS Bill prepared by the Attorney-General’s Department will become effective as law by that date regardless of the differing views from the public. Viewers who are most inclined to believe that what is printed on the Attorney-General’s website is true and correct are those whose background is not in law and who have very little or limited knowledge of the law reform process. The further problem to this is that these viewers may feel less inclined to voice their ideas and opinions on the belief that their voices will not be heard or their ideas and opinions will not be taken seriously.

The remaining comments are specifically on the Personal Property Securities Bill 2008 [Exposure Draft] (hereinafter, called the second draft of the PPS Bill 2008).

I have spent many hours reviewing the second draft of the PPS Bill and have also briefly compared it against the first draft. It appears that the second draft is no where a major improvement from the first draft. The six key issues collectively identified by the Australian Attorney-General as being the industry’s concerns and as noted on its website have not all been addressed in the second draft. Further, much of the complexity in the language and in the drafting remains unchanged and also the ambiguity in the terminologies used in certain areas has made it even harder to comprehend the underlying concepts and rationales. The style of drafting in conveying the concepts in both versions are substantially similar. That is, the second draft of the PPS Bill is as equally difficult to read and difficult to follow as the first draft, in that the second draft retains numerous cross-references of sections and retains double negatives and circularities in some of the key phrases. The Bill compels the reader to keep turning the pages back and forth in an attempt to understand how the proposed law applies to a particular situation (such as charges over book debts). Further comments and examples follow.

Numerous cross references:
There are numerous cross-references throughout the entire Bill which makes the reading rather frustrating. For example, in an attempt to understand how the Bill has defined words such as “negotiable instrument” or “account” referred to in s.51(5), one has to first go to s.26 (which is the “Definition” section) which then redirects the reader to another section. There are plenty of those re-directions under s.26, which overall makes s.26 redundant.

Difficulty in understanding the proposed section 51:
Another example is in the use of double negatives and circularities in the expression, which generally makes it hard for the reader to digest and process the relevant information. A clear example of this is in s.51. According to the heading under s.51, the proposed provision is supposed to provide a definition of “circulating asset”. Instead, s.51 begins with an explanation that a “personal property is a circulating asset…” in subsection (1), then subsections (2) and (3) focus on defining what “a current asset” is by saying: “Despite subsection (1), a current asset is not a circulating asset if…”.

Section 51(5) then goes on to define “current asset means any one of the following:

(a) currency;
(b) a negotiable instrument;
(c) an ADI account (other than a term deposit);
(d) inventory;
(e) an account (other than a term deposit) that is the proceeds of inventory; and
(f) an account that arises from granting a right, or providing services, in the ordinary course of a business of granting rights or providing services of that kind (whether or not the account debtor is the person to whom the right is granted or the services are provided).

Example: An account that is credit card receivable is a current asset under paragraph (f).”

One would beg to ask the question, what is the point of having a heading “Meaning of circulating asset” in s.51 when the description under that section appears to be focusing more on “current asset”. Ironically, reference is made to the term “circulating asset” throughout the PPS Bill, and yet the definition is ambiguous.

Further, it is unclear as to precisely what kind of intangible property would fall into the “current asset” category. It is clear that tangible property is a type of current asset, but not all intangible properties are. Section 51(3) reads:

“Despite subsection (1), a current asset is not a circulating asset if:
    (a) the personal property is tangible property; and
    (b) the security interest is perfected by possession.”

From that, it seems that only tangible property can strictly be categorised as current asset while intangible property is not recognised under s.51 unless it is one that falls within the list contained in s.51(5), and as reproduced above, it is only a short and narrow list of items of intangible property. By this, whether shares, bonds, and other similar types of intangible property could be categorised as “current asset” is yet to be seen.
On the side, it is interesting to note here also that under s.38, and particularly under s.38(2), tangible property is described to “include a description of the intellectual property rights” and yet no further information is given to explain how those intellectual property rights can possibly be tangible (one would think that tangible property is something that one can touch and feel). It is interesting point to make because common sense would implicate that intellectual property rights are a clear example of intangible property, not tangible property as stated in the Bill. Overall, the use of terminologies in the various provisions (which is explained further below) needs to be untangled and clarified.

Under s.51(5), the term “inventory” is referred to as part of an example of a “current asset”. However, the term “inventory” is not defined anywhere in the PPS Bill. As an illustration, when a business (including goodwill) is charged for a loan, could one consider goodwill as a type of current asset under s.51(5)? If the answer to that question is yes, then how can goodwill, (being strictly an intangible property) be reconciled with the description under s.51(3) when that provision clearly does not include intangible property? It appears there are contradictions between the proposed s.51(3) and 51(5).

My other difficulty in understanding s.51 is trying to figure out whether the proposed PPS Bill would also cover a situation where future liabilities are the subject of security (such as book debts that come in after a security has been created). Section 51(5) concentrates on the specific list of “current assets” which I presume these are circulating asset (because the heading under s.51 reads “meaning of circulating asset”). One would query as to why “future assets” have not been included in the PPS Bill. Section s.282 of the Corporations Act 2001 (C’th) does in fact refer to “future liabilities” in the ranking of priority of charges.

Uncertainty in section 50:
It may be right to say that s.50 is intended to point out that the common law distinction between fixed and floating charges will no longer be applicable when the proposed PPS Act comes into force. My reading of that comes from the combination of subsections (4) and (5) where both refer to “security interest” as being the new label in place of a charge. If this is what is intended, then would it not be more accurate and to the point by actually stating and making the point the abolition of the common law distinction, rather than explaining it in so many different words to a page and using terms such as “property”, “personal property”, “circulating asset” which could all mean the same thing or entirely different things, depending on how one’s interpretation differs from another. In the current proposal, there appears to be ambiguity in the meaning of the words “property”, “personal property” and “circulating asset” and such, in practice and within any particular context, could lead
to a misinterpretation of s.50. Also, there is a possibility that s.50 could be interpreted as if certain elements of the common law distinction is still retained because of the variations, particularly from subsections (1) through to (3), contained in s.50.

Another possible confusion flowing from the proposed s.50 of the PPS Bill is the overlap with the current priority ranking provisions (ss.279-282) under the Corporations Act 2001 (C’th). The current draft of the PPS Bill makes no mention of how the new proposed law will interact with the current ss.279-282 of the Corporations Act and there is no mention as yet about which provisions of the Corporations Act will undergo amendments or repeal.

Another possible interpretation of s.50 is that the common law distinction will not be abolished entirely, instead the floating charge component may have been modified legislatively through the careful description of the term “circulating asset” under s.51. Conversely, the common law distinction may well be retained to some degree through the careful description of the term “control” under the proposed ss.52 and 53.

Examples of circularities and repetitions in the expressions:
The second draft of the PPS Bill contains just as many of the multiple repetitions of similar words and expressions in the same sentences and paragraphs as in the first draft. Although at times, it may be necessary to have some repetitions, there are however far too many of these in the revised draft of the PPS Bill. One example of the circularity is under s.35. Section 35 attempts to define the word “account”, by saying in s.35(1) that, an “account means a monetary obligation”. Section 35(2) goes on to read: “A monetary obligation is an account whether or not the obligation has been earned by performance.” One would query whether it is necessary to explain “account” with the use of the word “obligation” and then repeat those words immediately in the next subsection.

A further example is found in s.32, which defines the term “purchase money security interest” in a circular motion. To illustrate my point, s.32(3) reads:

“If a security interest in collateral secures purchase money obligations and obligations that are not purchase money obligations, the security interest is a purchase money security interest only to the extent that it secures the purchase money obligations.”

Similarly, s.32(4) reads:

“If a security interest is granted in purchase money collateral and collateral that is not purchase money collateral, the security interest is a purchase money
security interest only to the extent that it is granted in the purchase money collateral.”

Essentially, the underlying ideas contained in s.32 are either lost or clouded with multiple repetitions of similar words and expressions. In short, I have difficulties understanding exactly what “purchase money security interest” means, and it is impossible to give literal interpretation when all 4 nouns are combined in that order and within that context.

Another example is in s.31, in relation to the meaning of “PPS lease”.

There are plenty of those other combined nouns throughout the revised PPS Bill. However, given the limitation of my research time and resources, it is not possible for me to identify and highlight all of the inconsistencies and uncertainties in this submission.

Uncertainties in the use of terminologies:
As explained above in relation to the confusion in the use of “tangible property” and “intellectual property rights” under s.51 and s.38 and how the latter does not make common sense, further example can be found in s.35(4) and s.41(1)(d).

Section 35(4) specifically states that “account” does not include “a negotiable instrument”. Section 41(1)(d) defines “a negotiable instrument” to mean “any other writing that evidences a right to payment of currency and that is of a kind that, in the ordinary course of business, is transferred by delivery with any necessary endorsement or assignment”. It seems strange to me that an account cannot be a negotiable instrument when the description for a negotiable instrument is clearly a form of monetary obligation in the ordinary sense. When an account (or invoice) is issued to a debtor for the work done or for the goods supplied, then it is reasonable for the creditor or the supplier to assume that the invoice issued, which has been delivered in a written form, is in fact a form of a right to payment of currency.

There are other terms that are unclear and ambiguous. For example, the difference between grantor and debtor – are they similar or different? The terms security and security interest have been used in the same paragraphs and sections and in varying contexts – are they similar or different? The terms “collateral”, “collateral description, “personal property” – are they similar or different?

There is a sense from the revised Commentary to the Bill and from the initial Options Paper that there is every intention for the common law distinction between fixed and floating charges to become redundant and inapplicable – if this is the continued
thought in the latest revision, then what is the point of having “circulating asset” and “control” tests explained in convoluted details?

**Relationship with the Corporations Act 2001 (C’th):**
The revised PPS Bill provides only a skeleton of how the proposed PPS Act will deal with the conflict of laws situations and glosses through some of the possible overlaps and interactions with the other laws currently existing without going into much detail as to the mechanisms or the approach in resolving or reconciling the possible inconsistencies in the laws. It mentions briefly the concurrency in the laws and the prevailing laws in the proposed Part 1.2 of the revised PPS Bill (which the second draft, within which Part 1.2, remains substantially unaltered from the earlier draft).

It is all well and true to say that in the event of inconsistency between the state statute law and the Commonwealth statute law over the same subject matter that s.109 of the Commonwealth Constitution would come into effect to give Commonwealth law a supremacy over the state law. It is also true to say that if there is inconsistency between a statute law and a common law, and in the absence of any concurrency rule set out in the statute or in the absence of the statute giving legal effect to the common law rule, the statute law will prevail. My concern is what happens when both Commonwealth statute laws are inconsistent.

I acknowledge that the revised PPS Bill does refer to the Commonwealth Corporations Act 2001, but perhaps not enough to address the core issue of how certain Parts and sections of the currently existing Corporations Act and the proposed PPS Act will operate conjunctively and harmoniously. The following are four examples of how the revised PPS Bill lacks clarity in its relationship with the Corporations Act:

First, the proposed Part 7.3 of the revised PPS Bill refers to priority and attachments on insolvency and bankruptcy in a global sense, and yet it does not acknowledge the fact that sections 279 – 282 of the current Corporations Act also concern with priority ranking of charges. There is no mention that the current sections 279 - 282 of the Corporations Act will be amended or repealed, nor is there any reference to how both systems will interplay.

The second failure in the proposed PPS Bill is the absence of clear rules on the maintenance of employee preferences in insolvency. This was one of the six key issues identified by the Commonwealth Attorney-General as one of the industry’s concerns. However, this issue has not been addressed adequately or at all in the revised PPS Bill. Although, the PPS Bill does refer to Part 5.2 of the Corporations Act (which is about rights and liabilities of receivers and controllers of company property in insolvency and about the priority ranking of the different charges), all that
the PPS Bill has actually stated, in this area of overlap, is in the following words (under the proposed s.155):

“This Chapter (meaning enforcement of security interests) does not apply in relation to property while a person is a receiver, a receiver and manager or a controller of the property, within the meaning of Part 5.2 of the Corporations Act 2001”.

This proposed s.155 appears unclear and uncertain. If the enforcement of security interests chapter under this proposed PPS Bill does not apply within Part 5.2 of the Corporations Act as it says, then does this mean that Part 5.2 will not be operating and will Part 5.2 be amended or repealed. If Part 5.2 of the Corporations Act allows to remain as it is when the proposed PPS Act does become law, then under what circumstances will the current Part 5.2 be continued to apply, because Part 5.2 does in fact refer to fixed and floating charges in the sense that there is that distinction? Further, the phrase “in relation to property” in the proposed s.155 seems rather broad and overly general.

The third problem with the revised PPS Bill is in relation to the proposed s.232 where it refers to in Note 2 that “A security interest might also be void under s.263 and s.264 of the Corporations Act 2001”. Although it seems that the revised PPS Bill is displacing the use of the word “charge” by replacing it with a more general and more loose and flexible expression such as “security”, “security interest”, “collateral”, and “collateral description”, it is uncertain how much of the elements of a “charge”, from the common law perspective, will be retained.

Fourth, the revised PPS Bill provides a brief reference to “financial product” that it has the same meaning as given under the Corporations Act and that all financial products will be regarded as a “personal property” relevant to the PPS Bill. The term “financial product” is defined in Chapter 7 of the Corporations Act and this chapter devotes entirely to financial services laws and the regulation of financial products and financial services. It is unclear how the proposed PPS Act will sit with the current Chapter 7 of the Corporations Act given the numerous ambiguities in the terminologies in the revised PPS Bill. For example, the PPS Bill is focusing more on “current asset” and “tangible property” while the “financial product” under Chapter 7 is about intangible property and includes future assets (such as managed investment funds or superannuation funds). Further, the proposed definition of “intangible property” in the revised PPS Bill is restricted. Further, when a company security is created over the managed investment funds or the superannuation funds, there is a possibility of a serious conflict in the laws between Chapter 5 of the Corporations Act, which deals with charges and priority ranking, and the proposed laws set out in the PPS Bill.
The need to protect all consumers:
In the current agenda, the PPS reform appears to benefit a section of the community only. The proposed provisions in the PPS Bill cater more for the corporate and retail end of the grantors and security holders and very little is said about general consumer protectionism. This is likely to have been driven by certain industry groups (such as the financial institutions and other corporate security providers) and law firms that desire to protect the interest of their corporate clients.

Given that the reform is specifically about personal property securities, and given that personal property can mean anything of value, including household goods and goods of personal value, one should work on the notion that the consumer protection provisions must be included to protect the general household consumers as well. The PPS Bill should include provisions such as the equivalent of s.4B of the TPA and the misleading and deceptive conduct provision – it is the ordinary individual consumers who are more vulnerable when their goods are parted for security and when they are uncertain whether the collateral description is clear and accurate and that the security contract that they have signed up for are not containing unjust and unequal bargaining terms. After all, the proposed PPS Act has the potential to impact on all Australians. There needs to be a focus of a wider spectrum of consultations and gathering broader public comments by advertising in varying kinds of media and providing longer period for submissions and comments.

Concluding remark:
My overall comment is that the revised PPS Bill is poorly drafted. The Bill could be improved by adopting perhaps a more “structured” approach, ie by removing many of the cross-references and repetitions of words and expressions and by arranging the different types of personal property securities under different and varying chapters and parts and with the regulatory provisions of those types under the same chapters rather than having words that are too broadly described and with multiple exclusionary provisions scattered throughout the Bill. Perhaps an excellent example is found in the Corporations Act 2001 (C’th). This way, it minimises the reader having to keep turning pages back and forth just to get a sense of what a particular concept or principle is.

My other concerns are that the revised PPS Bill has not considered thoroughly the issues on how to protect the employees’ statutory interests in insolvency, on how the proposed PPS Act will impact on the insolvency law and on financial services law, and on consumer protection generally. There are also terms in the revised PPS Bill that contradict those in the current Corporations Act.
It is good to see that the second draft of the PPS Bill has removed the expression “flawed asset arrangement” that appeared from the first draft. That expression is found in the New Zealand PPS Act, enforceable since May 2002 and has been severely criticised.

There are some other phrases, expressions and words in the revised PPS Bill that are similar to those found in the New Zealand counterpart. Prior to the New Zealand PPS Act coming into force in May 2002, Michael Geyde argued strongly that “the Act should not be brought into force until it was fixed up” and in his book, he noted at least 100 defects contained in that Act (see Geyde M, Wood, R, and Cuming, R., Personal Property Securities in New Zealand, Brookers, Wellington, 2002). Those defects are now beginning to surface gradually through judicial pronouncements (see, for example, Service Foods Manawatu Ltd (in rec and liq) Re Simpson and Walton v. NZ Associated Refrigerated Food Distributors Ltd (unreported, High Court Wellington, CIV-2005-485-1820, 30 January 2008). In that case, a New Zealand judge has criticised that while the legislative requirement of a “collateral description” in the financing statement might not be “seriously misleading”, the term “collateral” was “possibly overly broad”.

For the purpose of improving on the next draft of the PPS Bill, further insights could be gained from an article by Michael Gedye, “Reflections on some practical issues which have arisen under New Zealand’s Personal Property Securities Act and some lessons for Australia”, (2004) 15 Journal of Banking and Finance Law and Practice 20, and from reading some other New Zealand cases, such as Graham v. Portacom New Zealand Ltd [2004] NZLR 528, and Waller v. New Zealand Bloodstock Ltd [2005] 2 NZLR 549.

It is hope that the next draft of the PPS Bill will be a substantial improvement from the last revision.

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