

22 April 2010

Ms Julie Dennett
Committee Secretary
Senate Standing Committee on Legal & Constitutional Affairs
Department of the Senate
Parliament House
CANBERRA ACT 2600

By email: legcon.sen@aph.gov.au

Dear Ms Dennett,

Inquiry into the Personal Property Securities (Corporations and Other Amendments) Bill 2010

The Westpac Group is pleased to accept the Committee's invitation to make a submission to this inquiry. Westpac supports the Government's reforms in this area and generally consider that the majority of the changes proposed in this bill are appropriate. However, there are some issues that we believe require further consideration and amendment. Our comments with respect to these issues are outlined in this submission

Issues for further review

Issue No. 1 - Schedule 2, Item 51, increasing the number of days to 15 in which a Purchase Money Security Interest (PMSI) security interest holder will have to perfect registration.

We very much support the proposal to increase the number of days from 10 to 15 in respect of personal property which is not inventory (section 62(3)).

However we believe that difficulties may arise with this time period running from the "date of possession" as referred to in section 62(3)(b)(i). In particular:

1. Financiers may encounter problems in establishing what date the grantor obtained possession of the goods and therefore fail to register their PMSI within the 15 day period. This issue particularly arises in respect of serial numbered goods (as opposed to other personal property where it may be possible to capture PMSIs through a description in a financing statement which is lodged in advance of the expected date of possession).
2. Financiers who are refinancing the purchase of collateral, and thus have a PMSI, could never make the deadline (except in the very rare situation where the refinancing occurs within 15 business days of the date of taking possession).

3. Financiers who have PMSIs which are transitional security interests (that is, security interest created before the registration commencement time) will not be able to make the deadline, except where the grantor took possession within the 15 business days before the registration commencement time.
4. Where goods are initially financed and purchased overseas, and then brought into Australia, registration would normally follow the goods being brought into Australia. That may be well after the grantor obtains possession

There has been some suggestion that the first issue in point 1 could, to some extent, be solved by having the **vendor** register their PMSI in the goods being financed and then have that vendor assign that interest to the incoming financier, when the financier finances the goods. We believe that this is not a solution, for several reasons:

- First and most importantly, it is complex, and will add significantly to the transaction costs when the whole purpose of the act is to reduce them.
- Second, it assumes that each vendor will itself have a PMSI. If a vendor elects not to have a retention of title provision in its supply terms (or not to register such an interest), the proposal would not assist. Financiers could make it a condition of financing that the dealer obtain and register the PMSI, but again that adds to the costs and will require additional due diligence.
- Third, a PMSI which was just a retention of title provision and secured the purchase price would be automatically discharged when the purchase price was paid. The PMSI obtained by the dealer would need to be drafted in a peculiar fashion to secure not only the purchase price but also any financing provided by an assignee of the PMSI. A PMSI arising out of a retention of title by the vendor would be a different type of PMSI than the PMSI which would vest in a financier (as lessor or chargee), and it is doubtful that the vendor's PMSI could be "transferred" to a financier, unless it was very carefully drafted.
- Finally, as assignee the financier would be affected by any conduct or misconduct of the assignor before the assignment which in some way prejudices the security agreement or gives rise to a set off or counterclaim. It is for that reason that financiers are generally reluctant to rely on transferred security interests.

Similar issues arise on point 2, in relation to refinancing. In order to obtain the priority for its PMSI, it might be suggested that the financier would need to take an assignment of the existing PMSI from the financier it is refinancing. The drafting of that PMSI may not be suitable, the financier would need to incur transaction costs checking it and having it amended. In any event it is unlikely to be acceptable to financiers, as their security could be prejudiced by acts and omissions of the assignor, the original financier. The policy of the Act should be to encourage competition, making it easy for consumers to refinance their credit facilities.

Even if these issues could be overcome, we believe that rather than leaving this issue as a 'policy matter' for financiers to implement, the solution should be provided for in the legislation. Without a legislative solution, one financier in the market with a more relaxed approach, who did not require a vendor to register their PMSI over goods prior to providing finance for those goods, may have a commercial advantage over a financier who will only provide finance if a vendor has registered their PMSI and undertaken to transfer it. As a result, to remain commercially competitive, all financiers might have to adopt a policy of not insisting on vendors registering their PMSI and therefore all asset financiers would face a higher risk that they may lose their PMSI priority.

Section 62(2) in relation to inventory also presents similar practical issues, particularly in relation to serially numbered goods.

For all of the above reasons, for points 1 and 2 date of finance being provided, rather than the date of the grantor obtaining possession, is practically more manageable as a point of reference (with perhaps a period of 10 business days after financing applying to registration of security interests in serially numbered inventory).

In relation to point 3, that is, transitional security interests which are PMSIs, the concept of a very short time-frame following possession (or financing) for registration of the PMSI does not work at a practical level, and specific transitional provisions should be considered. Possibly, PMSIs should be taken to have been continuously registered as such if registered within 3-6 months of the *registration commencement time* (and if there are competing PMSIs registered over the same collateral within such period, ranking in order of the time of creation).

For point 4, consideration should be given to a different appropriate reference date for registration of PMSI interests over goods brought into Australia after the creation of those interests. For example it might be when the asset is brought into Australia.

Issue No. 2 - Water Rights.

Schedule 2, Items 11 & 14 (paragraph 8), extends the exclusion of water rights held by an irrigator and derived from a contract with the operator of the water corporation/co-operative responsible for the distribution of the water.

As a provider of finance to individual members of these water corporations this will apply to Westpac's dealings where our security interest is derived from shares or some other interest held by the irrigator in the operator of the water corporation.

The corporation holds the statutory licence and distributes the water to its members according to their shareholding or various other interests in the corporation.

There is inconsistency in the approach between these corporations / co-operatives. Some have spoken about registration of security interests on a new water register known as the National Irrigation Corporations Water Entitlement Register (NICWER). In our view this register would be unnecessary when the same could be achieved by registration on the Personal Property Security Register.

Issue No. 3 - The need to attend immediately to Transitional Security Interests.

The 2 year transitional period is designed to give time to register transitional security interests so that secured parties do not suffer a massive administrative burden. Some features of the legislation may make this illusory so that the bank and others will need to attend to massive numbers of transitional security interests on before the start of the period.

There are two issues that need to be addressed. Failure to address both may mean that we need to take steps in relation to our transitional security interests at the beginning of the transitional period.

1. The first issue is that all the various priority and extinguishment rules will apply to transitional security interests from the registration commencement time.

In a number of ways those rules operate so as to require either:

- (a) the register to record certain things; or
- (b) for the secured party to do certain things in order to maximise protection against loss of priority or the asset being taken by another party free of the security interest.

In relation to attending to the register referred to in (a) the most likely situations are as follows:

- Where the serial number for collateral noted on the register is incorrect or missing. This will most likely happen where the information is migrated from another register, particularly the ASIC register of company charges (which has no requirement for a serial number) and the REVS or VicRoad registers, where it is not uncommon to find dummy data (e.g. entries such as "11111111") to be entered where the secured party does not have all relevant numbers.
- In order for PMSIs to have priority, the secured party needs within a certain time to note on the register the fact that they are PMSIs (section 62). This will not be possible for most PMSIs granted before the registration commencement time as the period would have elapsed. In some cases like leases and ROT clauses, that may not matter as a practical concern. It can become significant when trying to extend the priority given to a PMSI to the proceeds of the PMSI.

The most relevant situation of the type referred to under (b) arise:

- where the holder of a security interest in property like shares wants to improve or preserve its priority position by taking control of the property (section 57(1)),
- under section 64, where the holder of a security interest in an account that represents proceeds of collateral subject to a PMSI wants to gain priority over the PMSI in relation to the proceeds under that section by giving a notice to the holder of the PMSI under section 64(2)(b).

Effectively it will be too late for the holder of the security interest to give a notice to the holder of the PMSI. However, we note that it seems that the timetable set out in section 64(2)(b) is virtually impossible to achieve in any event, and the section will rarely be operative.

2. Of greater concern is section 52. The amendments will mean that transitional security interests are stripped of one of the protections afforded by temporary protection under the transitional provisions. In a contest between the bank as holder of a transitional security interest over proceeds, goods, or negotiable documents of title, and a buyer or lessee for new value, the buyer or lessee would win. The bank won't get the same level of protection it would have had if it was registered.

To protect its security from such eventualities, the bank would need to register its security interest. This would entail checking tens of thousands of transactions to see which are effected, and then dealing with it.

Issue No. 4 - The interaction between section 337 and sections 164 and 165.

Sections 164 and 165 can render security interests ineffective to the extent of incorrect registrations. This can arise in relation to migrated security interests. Section 337 effectively allows a Registrar to override those sections in relation to migrated security interests. The difficulty from Westpac's point of view is the uncertainty and delay.

A Registrar is yet to be appointed and therefore industry has no indication as to which types of security interest would be subject to a declaration by that person. Given these answers are required now in order to know whether banks like Westpac need to undertake a full review of their portfolios, it is essential that industry is given certainty on this position.

With this in mind we ask for section 337 to be changed so that it automatically overrides sections 164 and 165 in relation to migrated security interests.

Issue No. 5 - Definition of 'property'.

With respect to Schedule 1, Corporations Act 2001 - section 51(F)(2) and section 441A(1)(b) and section 435(B), there appear to be conflicting definitions of 'property'.

Section 51(F)(2)) relates to the exclusion of retention of title property.

At section 435(B) the definition provides that retention of title property is included in the property of the company.

In the event of the appointment of an administrator to the company, does the security interest holder have an effective interest over the whole (or substantially the whole) of the company's assets to exercise its rights 'before or during the decision period'?

Issue No. 6 - Section 74 PPSA prejudices security over future property

One vital feature of security interests over assets is that they rank ahead of unsecured creditors, and, in particular, they are not prejudiced if an unsecured creditor obtains an order of execution against assets to enforce a judgement. Security interests traditionally rank ahead of orders of execution.

It has been brought to our attention that the current drafting of section 74 of the PPSA will considerably weaken this position, because it will have the effect that an order for execution will rank ahead of a security interest to the extent that the security interest affects property acquired after the order is made. This is because a security interest does not "attach" to an asset until it is acquired.

It is inconsistent with the policy of the PPSA to weaken security in this manner and we submit that the opportunity be taken to correct it.

Westpac looks forward to the completion of the legislative review process so we may move forward with certainty for our IT development and procedural changes. If you have any questions about any of the matters raised in this submission, please don't hesitate to contact me.

Yours sincerely,

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