

Papua New Guinea's
Personal Property Security Regime

May 2016





An overview

1 AN OVERVIEW

The *Personal Property Security Act 2011* came into operation on 4 May 2016. It is one of the most significant pieces of legislative reform for the Papua New Guinea financial sector, and commerce generally, for many years. While the Act has its greatest impact on financiers, the changes also impact in some way on virtually all commercial enterprises, and many individuals.

The Act rewrites previous Papua New Guinean law relating to:

- how security interests are formed
- how security interests can be enforced
- how priority disputes are to be resolved where more than one security interest is given over the same property
- the circumstances in which a security interest can be extinguished against the wishes of the secured party.

The Act also rewrites a number of established principles of commercial law.

The changes made by the Act will affect business documentation and procedures, the way businesses conduct their trading relationships, and the extent to which they can rely with confidence on the terms of those relationships to provide them with the level of security and certainty that they had previously expected.

Parties have 180 days (until 31 October 2016) to register their existing security interests or risk losing priority.

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THE ACT APPLIES TO ALMOST ALL PROPERTY OTHER THAN LAND

The Act applies to security interests over almost all types of property other than land, oil and gas licences and mining tenements. It applies both to physical assets, and to intangible property such as intellectual property, licences, payment obligations and financial instruments such as shares and debentures. It also applies to physical assets that are attached to land (fixtures).

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SECURITY INTERESTS – A NEW “FUNCTIONAL” APPROACH

The Act takes a “substance over form” approach to determining what is a security interest. This is a substantial shift from previous PNG law, which generally has regard to the legal form of a transaction to determine its consequences, rather than its underlying commercial effect. The Act applies to transactions that in substance create a security interest, which is:

“a legal interest in personal property that secures payment or performance of an obligation...”

The Act will apply to existing forms of security such as chattel mortgages, conditional sales, floating charges, pledges, trust indentures and trust receipts. Because of the “functional” definition, though, the Act applies to many commercial arrangements that are not currently treated as securities, such as retention of title arrangements, hire purchase agreements and leases. The Act also deems some transactions (transfers of accounts or chattel paper, commercial consignments and leases for a term of more than one year), to be security interests whether or not they are in substance a security.

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NEW RULES FOR CREATING SECURITY INTERESTS

The Act will establish new rules for the creation of effective security interests. Different rules will apply to determine:

- when a security interest will be enforceable against the debtor and third parties (called “attachment”); and
- what steps can be taken to protect a security interest from being defeated by a competing interest (called “perfection”).

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ATTACHMENT

A security interest attaches to personal property (that personal property is then referred to as “collateral”), making the security interest enforceable against the debtor and third parties, if:

- value is given;
- the debtor has rights in the collateral (or the power to transfer rights in the collateral to a secured party); and
- either:
 - the debtor has signed a security agreement that describes the collateral;
 - the collateral is in the possession of the secured party and is capable of being perfected by possession; or
 - the collateral is in the control of the secured party and is capable of being perfected by control.

A security agreement is effective according to its terms against purchasers of the collateral and execution creditors if it is in writing and describes the security interest.

While most traditional security interests will satisfy these requirements, the requirements are likely to cause problems for some commercial relationships that have not previously been regarded as security interests, such as retention of title provisions under supply arrangements.

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PERFECTION

Even if a security interest has attached to collateral, it will be important in most cases that the security interest also be perfected. If it is not perfected, the secured party will be exposed to the risk that its security interest could rank behind other security interests in a priority dispute, or even be extinguished entirely (for example, if the debtor transfers the collateral to another person).

A security interest that has attached to collateral can be perfected in up to five different ways, depending on the nature of the collateral.

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| REGISTRATION | The Act establishes an online security register called the Personal Property Security Register www.ppsrpng.com . A secured party is able to perfect its security interest by lodging a notice in relation to that security interest in the Register. Importantly, a secured party can lodge the notice before the security agreement is concluded or the security interest attaches to the collateral. The secured party can however only lodge the notice with the debtor’s consent, unless the interest was created before commencement of the Act. |
| POSSESSION | A secured party can perfect its security interest over some types of personal property by taking possession of the collateral. |
| CONTROL | A secured party can perfect its security interest over some types of personal property, being deposit accounts and some types of investment property, by taking “control” in a manner specified in the Act. |
| TEMPORARY PERFECTION | The Act provides for a number of situations in which a security interest will be taken to be temporarily perfected, without any act by the secured party - for example, where an instrument is delivered for sale or exchange, presentation, collection or renewal, or registration of a transfer. |
| DEEMED PERFECTION | In some limited situations, the Act also deems a security interest to be automatically perfected – for example, in some circumstances where collateral under a perfected security interest is disposed of, and the security interest attaches to the proceeds. |

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RULES FOR RESOLVING PRIORITY DISPUTES BETWEEN SECURITY INTERESTS

The Act establishes new rules for resolving priority disputes between security interests over the same collateral, replacing the old approach of the common law and equity, which together formed part of PNG's underlying law. Broadly, the priority rules work as follows:

- Priority between two or more perfected security interests is determined by the order in which they were registered, or perfected in some other way.
- A perfected security interest has priority over an unperfected security interest.
- Priority between unperfected security interests is determined by their order of attachment.

These rules are subject to numerous exceptions. For example, a security interest that is perfected by control will usually have priority over all other security interests, even if they were perfected first. The Act also introduces a new concept of purchase-money security interest ("PMSI"). A PMSI is a security interest taken in certain types of collateral to secure all or part of its purchase price or to secure funding that was used to acquire the collateral. It also includes the interest of a lessor of goods under a lease for more than one year, and the interests of a consignor under a commercial consignment. In most cases, a PMSI will have priority over other security interests even if the other security interest was perfected first (unless the other secured interest is perfected by control).

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RULES TO DETERMINE WHEN A SECURITY INTEREST CAN BE EXTINGUISHED

The Act provides as a general rule, if collateral is dealt with, that the security interest continues in the collateral in the hands of the transferee. In a number of circumstances, however, a transfer of collateral can result in the security interest being extinguished, for example:

- if the security interest was unperfected, and the transferee gave value for the collateral
 - if the property was sold or leased by the debtor in the ordinary course of its business
 - if the collateral is a car or truck that is held by the debtor primarily for personal use, and it was not registered by its serial number
 - if the collateral is goods that are acquired as consumer goods, or goods bought for farming, if the acquirer gave value and the purchase price or market value was less than K5,000.
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SPECIAL RULES FOR PARTICULAR TYPES OF PROPERTY

The Act contains other special rules for particular types of property, such as:

- crops (including trees)
- accessions
- commingled or processed goods
- ships
- aircraft
- fixtures
- investment assets
- bank accounts
- minerals.

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RULES FOR ENFORCING SECURITY INTERESTS

The Act contains rules that deal with the way in which a secured party can enforce a security interest in personal property.

These rules will not always apply. For example, the rules do not apply to the holder of a “deemed” security interest (such as a transferee of an account or chattel paper or a lessor under a lease for a term of more than one year), the interest of an execution creditor (including a trustee in bankruptcy or a liquidator), or a transaction in which a person pledges property to a pawnbroker.

Where the enforcement provisions do apply, they set out a number of rules about the way in which a secured party may enforce its security interest. For example, the rules will require that the secured party dispose of the collateral in a “commercially reasonable manner”.

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NEW DUTIES ON THE SECURED PARTY

The Act will impose a number of duties on a secured party, including:

- to care for collateral in its possession or control; and
 - to provide information about the collateral or the secured obligations to the debtor.
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CONFLICT OF LAWS RULES

The Act contains a set of rules that regulate whether PNG or a foreign law is to be used to determine the validity, perfection and consequences of perfection (or non-perfection) of a security interest. The applicable law depends on factors such as the type of the personal property, and the location of the personal property or the debtor.

These rules only determine which jurisdiction’s laws are to apply to the security interest itself. Parties will continue to be free to choose the law that is to apply to the other contractual obligations in their security agreements.

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TRANSITIONAL ARRANGEMENTS

The Act sets out some rules for the transition from the current law to the regime established by the Act.

Secured parties have until 31 October 2016 to register their pre-PPSA security interests in order to preserve their existing priority in the collateral.



Our team leaders

The Personal Property Security Act has revolutionised the law of secured finance in Papua New Guinea. To work out how the Act affects your business, contact one of our experts.

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