

LegalUpdate

15 March 2010

***Land law
applying to
personal
property
security
interests***

Personal property securities reform has arrived with the commencement of the Personal Properties Securities Act 2009 (Cth) (PPS Act) on 15 December 2009.

The PPS Act establishes a national Personal Property Securities Register which is likely to take effect on 1 February 2012. The purpose of the Register is to provide a system for determining the priority status of security interests (mortgages, charges, etc) in personal property.

The PPS Act impacts upon real property laws in two ways.

First, the Act applies to some types of property classified at general law as real property.

Secondly and most importantly, the Act gives security holders a right, in some circumstances, to enforce their security interests in personal property under land law, as if they were security interests in land.

Those with security interests in real property and personal property must ensure that they have a basic understanding of the PPS regime.

1. Personal property / real property distinction

The personal property / real property distinction has existed for centuries and has evolved, in simple terms, to be essentially a distinction between interests in land and interests in things other than land.

Essentially, the PPS Act applies to interests in things other than land and generally does not apply to interests in land save for three exceptions.

First, the Act applies to interests in unharvested crops and trees (potentially real property at general law) and mortgage-backed securities (pooled, securitised mortgages).

Secondly, the Act provides for land law to apply to security interests in personal property. This allows interests in land to be dealt under land law in the same proceedings as the interests in personal property.

Thirdly, section 8(3) of the Act provides that the regulations may override the exclusions in section 8(1) and prescribe an interest to which the Act applies.

2. Application of PPS Act to some limited forms of real property

2.1 Effect of difference between general law and PPS Act

Practitioners should be aware that the PPS Act conception of the real property / personal property distinction is subtly different to that at general law.

By consequence, certain security agreements, such as those under which “all [the grantor’s] real property is charged”, may, depending upon the construction of the term “real property” in the agreement, invoke the operation of the PPS Act.

Registration under the PPS Register may therefore be necessary to “perfect” (protect) that portion of the security interest which pertains to what is personal property for the purposes of the Act.

Arguably, indefeasibility of title conferred by Torrens legislation will not protect security interests in real property to the extent to which the PPS Act applies to it, due to the operation of section 109 of the Constitution..

2.2 Application of PPS Act to mortgage-backed securities

The drafters of the PPS Act intended that mortgage-backed securities (MBSs) would fall within the operation of the Act. MBSs are not treated as “interests in land” for the purposes of the Act, because documentation for such securities do not usually identify the specific parcels of land charged by the underlying mortgages.

3. Application of land law to security interests in personal property

Where an obligation is secured by interests in personal property and land, highest-ranked secured parties (or lower-ranked secured parties with written permission from all higher-ranked secured parties) may elect to have those security interests in personal property dealt with under land law together with their security interests in land.

Many security agreements, in commercial legal practice purport to “charge all property, real or personal”. Such agreements will allow secured parties to elect to enforce their interests under land law.

3.1 Security interests in personal property

The PPS Act defines “security interest” broadly. A non-exhaustive list of security interests given in the legislation includes fixed charges, floating charges, chattel mortgages, retention of title arrangements, consignments, assignments and security interests over bank accounts.

3.2 “Interest in land”

“Interests in land” is also defined broadly in the Act. Familiar security interests in land include mortgages and charges. We suggest that certain arrangements involving leases, sub-leases, leasebacks, transfers of Torrens land or declarations of trust may also constitute “interests in land” for the purposes of the PPS Act if the effect is, in substance, to secure an obligation (eg repayment of loan monies).

3.3 Obligations secured by security interests in personal property and land

The drafters of the PPS Act were mindful that in practice, “security agreements in relation to commercial transactions often use both personal property and land to secure the same obligation”. Currently, secured parties under such agreements must take separate proceedings to enforce their rights in respect of the

personal property and the land. Under the new regime, if a secured party’s interest in the personal property has the highest priority or if every other higher-ranked secured party agrees to it in writing, the secured party can choose to have their security interest in the personal property dealt with under land law together with their security interest in land. The advantage to this is that only one set of rules applies to the enforcement of the security. If legal proceedings need to be taken in order to enforce the security interests, both types of interest can be dealt with in the one court hearing, reducing the secured party’s enforcement costs.

3.4 “Land law”

Land law is defined in the PPS Act as “those provisions of a law of a State or Territory, or of the general law, that relate to the enforcement of the interest in land that secures the obligation”. In New South Wales, for example, the main “land laws” would be the *Real Property Act 1900* (NSW), the *Conveyancing Act 1919* (NSW) and the common law of New South Wales. However, as an Act of the Commonwealth Parliament, the PPS Act has Australia-wide application and therefore the meaning of “land law” will differ from jurisdiction to jurisdiction. The meaning will also change over time in line with changes to statute and general laws.

3.5 Enforcement of a security interest in personal property “in the same way... as the interest in the land may be enforced under land law”

Section 118 of the *PPS Act* provides that secured parties seeking to enforce their security interests in personal property “may enforce the security interest in the same way, with any necessary modification, as the interest in the land may be enforced under the land law” and that the “law in the same terms as that of the land law applies under [the PPS] Act for the purposes of the enforcement of the security interest”. Details as to what exactly this will involve are not given. We note that there is, appropriately, a power under subsection (5) to make regulations facilitating the application of the law to the land law enforcement of security interests in personal property, although no regulations have been tabled as at the time of writing.

3.6 Required conduct of a secured party exercising their power of sale over personal property under land law

In addition to the standards of conduct imposed by various State land laws on security holders exercising their power of sale, section 117 of the *PPS Act* imposes additional standards, requiring them to have regard to the following:

- (a) the respective values of the personal property and the land
- (b) whether there is any connection between, and the nature of any connection between, the personal property and the land
- (c) whether the land and the personal property are both located in the same State or Territory, and
- (d) such other matters as are relevant to the efficient enforcement of the security interest and the interest in the land.

4. Final comments

Due to the far-reaching consequences of the PPS reform, it is prudent for those with security interests in real property and personal property to ensure that they have a sufficient understanding of the operation of the *PPS Act* both generally and in the specific context of land law.

In particular, security holders should begin considering now whether they will need to transition their security interests to the new system in 2012.

Individuals or companies who acquire real or personal property security interests on a semi-regular basis (eg credit providers) may need to modify their business systems or practices so as to ensure that the interests are registered in a timely manner.

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