SOME IMPORTANT ISSUES IN RELATION TO FINANCING STATEMENTS UNDER THE PPSA

This article provides general information only and is not intended to constitute legal advice.

This short article focuses on several issues in relation to financing statements under the Personal Property and Securities Act 1999 (PPSA). They relate to matters that are often not well understood (including by professional advisers).

Financing Statements are only part of the story

It's important to realise that a financing statement is only a means by which a security interest can be perfected i.e. a means by which a security interest can gain priority over other security interests. A financing statement doesn't create a security interest.

Whether there is a valid security interest depends upon the underlying arrangement between the parties. This point is particularly important for accountants who act as receivers and liquidators, for example, because they cannot assume that a creditor has a valid security interest simply because a financing statement has been registered.

In some circumstances, persons searching the register will only want to know whether a financing statement has been registered. However, where it is important to ascertain whether a party has a security interest, it will be necessary to look to the underlying documents (such as an equipment lease, terms of trade relating to the sale of goods or a loan agreement whereby security is given for a loan).

General Priority Issues

Once it has been established that there is a valid security interest, then, where there are other security interests, questions of priority arise. In that regard, there are various priority rules set out in the PPSA.

An important general rule is that a perfected security interest will have priority over an unperfected security interest (s66(a)). As noted above, a security interest can be perfected by registering a financing statement. (In relation to some types of property, perfection can also be achieved by taking possession of the property.) As general rule therefore, a security interest in respect of which a financing statement has been registered will have priority over a security interest where no financing statement has been registered.

Another important rule is that where there is more then one perfected security interest, priority is given to the interest that is first perfected (s66(b)). Accordingly, timing is important for priority purposes.

However, an important qualification to s66(b) is that perfected purchase money security interests (PMSI's) will have priority over other perfected security interests even if the other interests were perfected first. The details are set out in ss73-75. Perfected PMSI's give secured parties super priority – in essence, they beat all other security interests.

PMSI's include, for example, the interest of a lessor under an equipment lease (notwithstanding that the property is owned by the lessor) and the interest of seller of goods under reservation of title (again, notwithstanding that the goods are the property of the seller).

The reasons why perfected PMSI's have super priority is obvious. Why would an equipment lessor lease equipment to a lessee if the equipment would automatically be covered by a general security agreement in favour of a bank, over all of the lessee's present and future personal property, and if the bank would have priority over the lessor? Similarly, why would a supplier sell goods on credit, on the basis of reserving title, if the goods would automatically be covered by a general security agreement in favour of a bank, over all of the buyer's present and future personal property, and if the bank would have priority over the supplier? In these examples, under the PPSA, the bank has a security interest in the leased equipment or the goods supplied but the important point is that the lessor and the supplier have priority over the bank provided that they have perfected their interests as required by the PPSA, notwithstanding that the bank may have perfected its interest first.

The critical thing in obtaining super priority status in relation to a PMSI is to ensure that a financing statement is registered within the time prescribed by the PPSA. The timing is slightly different depending upon the type of property involved e.g. whether it is inventory or intangibles or other property. (See ss73-75.)

Failure to comply with the time limits does not mean that the secured party under a PMSI will not have a security interest or even that they will not have a perfected security interest. The failure to comply with the time limits will prevent them from having a super priority over other perfected security interests.

I make the point in passing that there is no time limit to register a financing statement. For example, it is possible to register a financing statement against a company after the company has gone into liquidation. Timing relates to priority. Also, an unperfected security interest is still a valid security interest. If there are no other security interests, it may be valid as between the secured party and the debtor. So, for example, if a supplier sells goods and reserves title, and there are no security interests over the buyer's property, the seller should generally be able to rely on their reservation of title clause. (The position might be different if the debtor were to go into liquidation because preferential creditors might have a superior claim under the Companies Act.)

Changed circumstances

There are also priority rules that relate to changed circumstances. In certain circumstances priority can be lost if the PPSA register is not updated to take into account those changed circumstances.

For example, priority can be lost where the secured party learns of a change of name of the debtor e.g. the debtor is a company and changes its name, or where the secured party learns that the debtor has transferred the relevant property to another person. In those circumstances, there are precise time limits within which the secured party must register a financing change statement. Should they not do so, they will lose priority to some perfected security interests. (See ss88-91.)

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