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REFORMING THE LAW OF SECURITY INTERESTS: NATIONAL AND INTERNATIONAL PERSPECTIVES

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Back in 1996, a Sub-Committee of the Singapore Academy of Law recommended comprehensive reform of the law of security interests.[1] The suggested model for reform was Article 9 of the U.S. Uniform Commercial Code as refined in other common law jurisdictions.[2] New Zealand enacted similar reforms in 1999 with the new legislation coming into force in 2002.[3] 2002 also saw the publication of a report by the Law Commission in England which advocated Article 9 type legislation in England.[4] The question arises whether the 1996 report by the Singapore Academy Sub-Committee should be dusted down and whether the law should proceed along the reform path. This paper will consider the arguments for and against reform as well as some of the potential pitfalls in enacting reforming legislation.

I. BACKGROUND

Singapore has been a great economic success story of the late 20th century. The country has moved from Third World to First World status in a

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1 Report of the Sub-Committee on Review of the Bills of Sale Act, online: Singapore Academy of Law <http://www.sal.org.sg> [Reform of the Bills of Sale Act Report].

2 Article 9 was first introduced in the 1950s by two sponsoring organisations: the American Law Institute and the National Conference of Commissioners on Uniform State Laws. Article 9 has since been revised on many occasions with the most recent (1998) revision coming into force on 1 July 2001. For the revised text of Article 9, see <http://www.nccusl.org>. See also C. Cooper, ed., *The New Article 9*, 2nd ed. (Chicago: American Bar Association, 2000) and J. Honnold, S.L. Harris and C.W. Mooney, *Security Interests in Personal Property*, 3rd ed. (New York: Foundation Press, 2001). The new Article 9 is also discussed in (1999) 74 Chicago-Kent L. Rev. 3.

3 *Personal Property Securities Act 1999* (N.Z.), 1999/126, as amended. On the legislation see generally L. Widdup and L. Mayne, *Personal Property Securities Act: a conceptual approach*, revised edition (Wellington: Butterworths, 2002) [Widdup and Mayne]: M. Gedye, R. Cuming and R. Wood, *Personal Property Securities in New Zealand* (Wellington: Brookers, 2002) [Gedye].

4 Consultation Paper No. 164, "Registration of Security Interests" (July 2002).

remarkably short period of time.[5] The new millennium presents Singapore with a new set of economic problems, in particular the problem of maintaining its internationally competitive position in the face of a changing global order. To this end the Economic Review Committee has produced an impressive report detailing the changes that need to be faced if Singapore is to respond positively to the new economic realities.[6]

One of the changes in Singapore in recent years has been a growing American influence. The country has successfully built on an inheritance of British law and public administration but more recently American models have increasingly been invoked in various spheres.[7] The university sector is a case in point.[8] In the field of Credit and Security Law Singapore has a body of British precedents that, over the years, have fostered economic activity. The English law has however come under criticism for being fragmented and conceptually incoherent as well as for inefficiencies and inconsistencies in the registration process and in determining priorities between competing security interests in the same property.[9] Article 9 of the U.S. Commercial Code, on the other hand, is conceptually tighter and more rigorous; arguably more responsive to commercial needs and moreover, contains more consistent and rationally more grounded rules for determining priorities between competing security interests. All transitions, however, contain adjustment costs and the move from a predominantly English based law of security interests to one founded on the American Article 9 is likely to involve teething difficulties. In particular, lawyers and bankers will have to learn a whole new terminology. There is also a danger that old controversies on the legitimate scope of security rights will be resurrected.[10] The 1996 report from the

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5 See the second volume of memoirs by Senior Minister Lee Kuan Yew, *From Third World to First: The Singapore Story 1965–2000* (New York: Harper Collins, 2000) [Lee Kuan Yew].

6 "New Challenges, Fresh Goals—Towards a Dynamic Global City", 6 February 2003, online: Economic Review Committee <http://www.erc.gov.sg>, and refers to Singapore at para. 1 as a "dynamic global city, thriving in a changed world."

7 See the comments of Senior Minister Lee Kuan Yew, *supra* note 5 at 428: "My generation was Anglocentric, my son's generation is more focused on America. Loong and his contemporaries have to understand the United States. . .. I lived under Pax Britannica; Loong's generation has to cope under Pax Americana."

8 One could instance the establishment of Singapore Management University which is modelled on Wharton Business School in the United States.

9 See generally the report by Professor Aubrey Diamond commissioned by the Department of Trade and Industry, "A Review of Security Interests in Property" (H.M.S.O., 1989) and see also the Cork Committee Report, "Insolvency Law and Practice" (Cmnd. 8558, 1982) and the Crowther Report, "Consumer Credit" (Cmnd. 4596, 1971).

10 According to Professor Michael Bridge, if England were to adopt an Article 9 statute, hard-won gains by banks on the scope of security rights would be surrendered for something new whose implications would take some time to be felt: see "How Far Is Article 9 Exportable? The English Experience" (1996) 27 Canadian Business Law Journal 196 at 221. For an argument that the U.S. system is more pro shareholder than pro creditor, see R. La Porta,

Singapore Academy Sub-Committee obtained a mixture of responses from industry professionals. There were some positive comments but also some negative. The Asian financial crisis in 1997 dashed hopes for early implementation of the recommendations. Stormclouds of economic uncertainty continue to loom large over the horizon and this suggests that caution should be exercised before proceeding with fundamental reforms in the sphere of Credit and Security.[11] After all, the present system has served the country well over the years; furthermore, some of the more bureaucratic and cumbersome features of the English registration system have been eliminated in Singapore.[12] Before examining these arguments in greater detail however, it is appropriate to look at the reasons why the law should recognise security rights in the first place.

II. The Case For Security

Credit and Security Law is a branch of Commercial Law and, while most observers would subscribe to the view that a central function of the law should be to foster commercial activity and to resolve disputes between parties in an equitable fashion, opinions differ as to whether Credit and Security law properly serves these goals.[13] A central effect of recognising security rights is to prefer one creditor over another creditor in the event of a debtor's insolvency. This runs counter to the intuitive notion that creditors should be treated in like manner with each receiving a rateable proportion of what is due to him, *i.e. pari passu* distribution.[14] There are countervailing

F. Lopez-de-Silanes, A. Shleifer and R.W. Vishny, "Law and Finance" (1998) 106 Journal of Political Economy 1113.

11 The Company Legislation and Regulatory Framework Committee (CLRFC) Final Report in October 2002 stated in Chapter 2 para. 4.1.3: "In the light of the continuing consultation in the U.K. and the review in Singapore of the possibility of an overhaul in favour of a U.C.C. model we do not recommend any immediate revisions to the current system of registration of charges at this time."

12 Part 12 English Companies Act 1985 is based on the principle that the registrar of companies compares the instrument of charge with prescribed particulars whereas under the Singapore statute this checking function is not performed as a matter of course as there is no obligation to submit the instrument of charge alongside the prescribed particulars.

13 See generally R. Mokal, "The Search for Someone to Save: A Defensive Case for the Priority of Secured Lending" (2002) 22 O.J.L.S. 687.

14 As one writer says: "The normal rule in a corporate insolvency is that all creditors are treated on an equal footing—*pari passu*—and share in insolvency assets *pro rata* according to their pre-insolvency entitlements or the sums they are owed. Security avoids the effects of *pari passu* distribution by creating rights that have priority over the claims of unsecured creditors"—V. Finch, "Security, Risk and Insolvency: Who Pays the Price" (1999) 63 M.L.R. 633 at 634. But as R. Mokal has pointed out, the *pari passu* principle is not as extensive, pervasive and all-embracing in practice as it appears to be in theory since empirical evidence suggests that the vast bulk of a company's assets is distributed other than on a *pari passu* basis: "Priority as Pathology: The *Pari Passu* Myth" [2002] C.L.J. 581.

considerations, however, that support the institution of security. One such consideration is the property rights or freedom of contract argument, *i.e* security is a fair exchange for the extension of credit. In other words, a creditor has bargained for security vis-à-vis the debtor and the law should respect and uphold that bargain in the event of the debtor's insolvency.[15]

There are also other more instrumental reasons for upholding the institution of security. Security is said to lower the cost of credit and also to encourage creditors to advance loans that might not otherwise be made. The argument proceeds on the basis that the risk of non-payment is one of the matters factored into the equation when deciding whether or not to extend credit. Security minimises the downside risk as far as a creditor is concerned in that the creditor may take enforcement proceedings against the secured property in the event of debtor default. If a loan is perceived of as being potentially risky, then the taking of security may be the decisive factor that persuades a cautious lender to advance funds. The proposition that security lowers the cost of credit involves a more sophisticated analysis based as it is on the notion that risk of default is a matter to be factored into the calculation of interest rates by a lender on a loan. As security is supposed to reduce downside risks, then borrowers who provide security are faced with lower financing costs. In this way, security reduces the cost of credit and, at a macro level, economic activity is stimulated. On the other hand, lenders are likely to impose whatever interest rate they think that the market will bear; irrespective of whether or not security is provided in a particular transaction. Experience at the micro level tells us that a borrower who is regarded as a poor credit risk may only be able to borrow on the condition that security is provided and, moreover, may be faced with high interest rates. Highly rated lenders, by contrast, may be able to borrow on an unsecured basis and also to obtain the most advantageous interest terms.[16] There are also contrarian theorists who suggest that the taking of security is

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[15] See generally Professors Steven Harris and Charles Mooney, "A Property-Based Theory of Security Interests: Taking Debtors' Choices Seriously" (1994) 80 Va. L. Rev. 2103.

[16] For a sophisticated analysis of the various factors that influence the decision whether or not to take security, see generally Ronald J. Mann, "Explaining the Pattern of Secured Credit" (1997) 110 Harv. Law Rev. 626. Mann states at 668: "The possible benefits include not only the direct enhancement of the lender's ability to collect its debt forcibly, but also indirect effects that substantially increase the likelihood that the borrower will be in a position to, and choose to, repay the debt without forcible collection. All of these benefits work together to lower the lender's pre-loan perception of the risk of non-payment, allowing the lender to make a profitable loan at a lower interest rate or on more lenient terms. On the downside, the parties also must consider the corresponding burdens. For large companies, secured credit is likely to carry with it a significant increase in the information costs of the lending transaction. More generally, secured credit imposes costs on all borrowers—large and small—by diminishing their operating flexibility."

a "zero-sum game" rather than being in any way economically efficient.[17] They would suggest that if one creditor by taking security is assuming a lower risk and imposes a lower interest rate in consequence, then another creditor who advances funds while unsecured is accepting a higher risk and imposes a correspondingly higher interest rate to compensate.[18] The two matters cancel one another out and, overall, there is no efficiency gain from security.[19] It may be however that this is too much of a laboratory example where averages and means conceal a wealth of detail and divergence in individual cases. With the Law of Credit and Security, the devil may really be in the detail.

Be that as it may, history demonstrates the persistence of security and banks generally clamour for stronger and more effective security rights rather than weaker ones. One might mention in this connection what is now section 13 of the Civil Law Act[20] which, following uncertainties generated by the English decision in *Re Charge Card Services Ltd.*,[21] expressly legitimated security interests in deposit accounts. Moreover, the institution of security appears to be accepted as a global good. In recent years, multilateral institutions have been progressing with various initatives in the sphere

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17 The whole efficiency of secured credit debate was started by Professors Thomas Jackson and Anthony Kronman in an article in 1979 in the Yale Law Journal: "Secured Financing and Priority Among Creditors" (1979) 88 Yale L.J. 1143.

18 See the article by L. Bebchuk and J. Fried, "The Uneasy Case for the Priority of Secured Claims in Bankruptcy" (1996) 105 Yale L.J. 857.

19 Perhaps the most vocal critic of secured credit from a law and economics perspective is Professor Alan Schwartz. Professor Schwartz has argued strongly that the favourable treatment by the law of secured credit is without a plausible economic rationale and he rejects several efficiency justifications commonly offered for security. These include the reduction of overall costs incurred in monitoring the debtor, the fact that secured credit may serve as a signal to other creditors; the proposition that properly staggered debt enhances profits; reduction in levels of creditor uncertainty and the fact that security interests may serve to shift risk from more to less risk-averse creditors: see A. Schwartz, "A Theory of Loan Priorities" (1989) 18 J. Legal Stud. 209; "Security Interests and Bankruptcy Priorities: A Review of Current Theories" (1981) 10 J. Legal Stud. 1; "Taking the Analysis of Security Seriously" (1994) 80 Va. L. Rev. 2073; "The Continuing Puzzle of Secured Debt (1984) 37 Vand . L. Rev. 1051.

20 *Civil Law Act* (Cap. 43, 1994 Rev. Ed. Sing.) [*Civil Law Act*].

21 [1997] Ch. 150, but see now *Re BCCI (No. 8)* [1998] 1 A.C. 214; on which see, *inter alia*, McCormack [1998] Company, Financial and Insolvency Law Review 111. For Singaporean authority, see *Ho Dwan Tiauw v. Banque Nationale de Paris* [1993] 2 S.L.R. 329. The Civil Law Act provision, first introduced as section 9A in 1993, provides: "For the avoidance of doubt, it is hereby declared that a person ("the first person") is able to create, and always has been able to create, in favour of another person ("the second person") a legal or equitable charge or mortgage over all or any of the first person's interest in a chose in action enforceable by the first person against the second person, and any charge or mortgage so created shall operate neither to merge the interest thereby created with, nor to extinguish or release, that chose in action." In *Tam Wing Chuen v. Bank of Credit and Commerce Hong Kong Ltd.* [1996] 2 B.C.L.C. 69, the Privy Council held that a similarly-worded provision was effective to create a charge over a bank deposit.

of secured transactions law.[22] The International Institute for the Unification of Private Law (Unidroit) has produced conventions on International Factoring (Ottawa Convention) and also on high value mobile equipment.[23] The United Nations Commission on International Trade Law (Uncitral) has produced a convention on the assignment of receivables in international trade[24] and is in the process of formulating a Legislative Guide on Secured Transactions more generally. International financial institutions have also been active with work done by, amongst others, the World Bank[25] and the Asian Development Bank.[26] The European Bank for Reconstruction and Development (EBRD) has gone so far as to produce a Model Law on Secured Transactions and also Principles of a Modern Secured Transactions Law. According to these principles, the law of credit and security in a particular jurisdiction should be founded on five key elements.[27] Firstly, the security right must adhere to the essential qualities of a property right (right *in rem*). Secondly, the law should provide for the granting of security in the widest possible range of circumstances. Thirdly, the existence of a security right over property must be effectively publicised. Fourthly, there should be a rapid and cost-effective means of recovering the debt from the secured asset

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22 The doyen of English commercial lawyers, Professor Sir Roy Goode, for example, argues that without an adequate legal regime for personal property security rights, it is almost impossible for a national economy to develop: see R. Goode, "Security in Cross-Border Transactions" (1998) 33 Tex. Int'l L.J. 47.

23 Cape Town Convention 2001 and see generally the work done by Unidroit, online: <http://www.unidroit.org>.

24 New York December 2001 and see generally <http://www.uncitral.org>. See also Spiros Bazinas, "UNCITRAL's Work in the Field of Secured Transactions" in J. Norton and M. Andenas, ed., *Emerging Financial Markets and Secured Transactions* (London: Kluwer, 1998).

25 According to the World Bank, the widespread insistence on security for payment indicates that credit extension is not simply a function of price and, in many cases, a prospective borrower who is unable to furnish adequate security will be refused credit altogether rather than being charged a higher rate of interest than a borrower offering security. In its view, credit expansion, and the facilitation of economic activity requires not only an orderly system for the collection of debts but also a legal regime which recognises and accommodates security rights in both real property and personal property: see World Bank, "Building Effective Insolvency Systems" (World Bank 1999), a report from the Working Group on Debtor-Creditor Regimes at 3.

26 See generally the Asian Development Bank website for their technical assistance projects in the area of secured transactions and insolvency law reform: online, Asian Development Bank <http://www.adb.com>.

27 See Fairgrieve, "Reforming Secured Transactions Laws in Central and Eastern Europe" [1998] E.B.L.R. 254; G. McCormack and F. Dahan, "The EBRD Model Law on Secured Transactions: Comparisons and Convergence" [1989] Company, Financial and Insolvency Law Review 65; L. Mistelis, "The EBRD Model Law on Secured Transactions and Its Impact on Collateral Law Reform in Central and Eastern Europe and the Former Soviet Union" (1998) 5 Parker School Journal of East European Law 455; J. Simpson and J. Menze, "Ten years of secured transactions reform" (Autumn 2000) Law in Transition 20.

and, fifthly, the cost of creating, maintaining and exercising the right should be kept at a reasonable level.[28]

III. Essentials of Singapore Law

Singapore law certainly respects the principles held dear by the international lending community. Security rights are recognised as property rights and such rights are valid and effective vis-à-vis third parties. It is possible to take security over after-acquired property. Future advances may be secured and security may be created over the entirety of a debtor's business operations. All this can be done with the very minimum of formalities and restrictions. The floating charge security is an ingenious device which combines managerial freedom on the part of the debtor with effective security for the creditor. Under the security, a debtor is authorised to carry on business in the ordinary way until some event occurs to bring about the security taker's intervention. The floating charge is fully recognised in Singapore, as was made clear by the decision of the Singapore Court of Appeal in *Dresdner Bank v. Ho Mun-Tuke Don*[29] where Thean J. quoted approvingly the words of Lord Macnaghten in *Government Stocks And Other Securities Investment Co. Ltd. v. Manila Railway Co. Ltd.*:[30]

> A floating security is an equitable charge on the assets for the time being of a going concern. It attaches to the subject charged in the varying condition in which it happens to be from time to time. It is of the essence of such a charge that it remains dormant until the undertaking charged ceases to be a going concern, or until the person in whose favour the charge is created intervenes. His right to intervene may of course be suspended by agreement. But if there is no agreement for suspension, he may exercise his right whenever he pleases after default.

In some jurisdictions the floating charge occupies a relatively weak priority position in that the security taker is only paid after all preferential debts have been satisfied. This is not so in Singapore where preferential debts are subdivided into debts owing to the State and debts arising in respect of employment entitlements such as retrenchment benefits *etc*. It is only the latter that are paid before floating charges.[31] Fixed charges will be paid

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[28] See also the Preface to the Model Law on Secured Transactions (1994), published by the European Bank for Reconstruction and Development (E.B.R.D.): online, E.B.R.D. <http://www.ebrd.com>.

[29] [1993] 1 S.L.R. 114.

[30] [1897] A.C. 81 at 86.

[31] Sections 226 and 328 of the *Companies Act* (Cap. 150, 2000 Rev. Ed. Sing.) [*Companies Act*]. There have, however, been suggestions in the Malaysian Courts that federal taxes take priority by virtue of section 10 Government Proceedings Act (Act 359, 1956): see *Anuarul*

ahead of all preferential debts and a security taker in the instrument of charge may supplement a general floating charge with a fixed charge on specific assets including receivables belonging to the debtor. Singapore law also upholds various "quasi-security" devices that in functional economic terms may be regarded as the equivalent of security but are not characterised by the law as such. Examples include the assignment of receivables;[32] reservation of title clauses in sale of goods contracts[33] and sale and repurchase agreements in respect of shares ("repos"). Section 131 of the Singapore Companies Act requires that most security agreements by way of charge should be registered but if an agreement is not regarded as creating a charge then it falls outside the scope of the company charge registration scheme. As Dr. Gough explains in a leading text, *Company Charges*:

> With regard to the companies registration system, it is the policy of the courts still to treat normal financial arrangements with the security of recourse to property which can be effected by means other than a transaction of loan and charge as not being registrable even though such transactions might fully, and to identical economic effect, be carried out through a form of transaction which was registrable. This remains so, notwithstanding that the form of transaction was used or selected for the very purpose of 'evading' or 'defeating' the need for registration . . .[34]

Repos were given a very firm stamp of approval by the Singapore Court of Appeal in *Thai Chee Ken v. Banque Paribas*[35] where the sentiments expressed in *Gough* were strongly approved. In a robust judgment, Yong Pung How C.J. observed:

> Freedom of contract should be respected to the extent that it must be recognised that different legal forms can be used to achieve the same economic object or end, and that some legal forms legitimately fall outside the statutory provisions. In the latter situation, it is not correct to speak of evasion of the law but rather there has to be recognition of the fact that lacunae exist in the statute which the legislature, and the legislature alone, has to decide whether or not to close . . . Moreover, the court ought to take notice of the constant development of new financing arrangements and should not be strapped by precedents based on

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Aini v. Ketua Pengarah Kastam dan Eksais Diraja Malaysia [1991] 1 M.L.J. 360; *Global Pacific Textile Industries Sdn Bhd v. Ketua Pengarah Jabatan Kastam dan Eksais* [1994] 3 M.L.J. 175.

32 As has the Federal Court of Malaysia in *Public Finance Bhd v. Scotch Leasing Sdn Bhd* [1996] 2 M.L.J. 369.

33 *Gebrueder Buehler AG v. Peter Chi Man Kwong* [1987] I M.L.J. 356 (High Court); [1988] 2 M.L.J. 69 (Court of Appeal) [*Gebreuder* cited to [1988] 2 M.L.J. 69].

34 1st ed. (London: Butterworths, 1978) at 258.

35 [1993] 2 S.L.R. 609.

> arrangements which are outmoded in topicality. Each case must be seen in its own particular circumstances and commercial reality.[36]

IV. Criticisms of the Law

Singapore law undoubtedly facilitates secured financing. On the other hand, the law, like English law, can be accused of conceptual incoherence with the different treatment accorded functionally equivalent legal devices. Moreover, priority determinations may be difficult since a number of matters influence the question of priorities if there is more than one security interest over the same item of property: time of creation, registration, notice, whether the charge is fixed or floating or indeed whether it is a quasi-security, in which case it will enjoy super-priority over "ordinary" security interests. These points have been well put by the Singapore Academy of Law Sub-Committee who point out:

> . . .[T]he development of security transactions adds to the complexity of the law, as essentially similar transactions are treated differently for the purposes of creation, registration, enforceability, priority etc. . . Where new security interests in personal property are devised, the present law also does not make the determination of priorities between competing security interests easy and certain (especially when they are equitable in character), creating an impediment to sophisticated and structured secured credit financing.[37]

On the other hand, some of the factors which led to the enactment of comprehensive personal property security law in other common law jurisdictions like New Zealand are not present in Singapore. Apart from the Companies Register and the Bills of Sale register, Singapore does not have a multiplicity of registers of security interests in personal property.[38] These registers, be they transaction-based in the case of conditional sales or asset-based in the case of accounts receivables or motor vehicles, can add both to the costs and the risks of secured lending. Furthermore, the company charge registration system seems to less cumbersome and administratively expensive in Singapore than in England. As the English Law Commission has pointed out in a critique of the English system, the English legislation seems premised on the assumption that the staff at the registry of companies compare the filed particulars of charge with the instrument of charge and only if satisfied that there is concordance between the two can they issue a certificate of

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[36] *Ibid*. at 614.

[37] Reform of the Bills of Sale Act Report, *supra* note 1, paras. 7–9.

[38] Singapore does however have registers to record interests in intellectual property rights (apart from copyright) and interests in ships.

due registration.[39] With complicated security agreements (instruments of charge) the task imposed on the staff at the registry is not one that is capable of easy fulfilment and, additionally, there is the long stop possibility of liability if a discrepancy or discrepancies between the charging instrument and the filed particulars have not been detected. Under the Singapore statute all that is required to be lodged is a statement of the prescribed particulars and also an affidavit verifying the execution of the charge and verifying the correctness of the statement. The instrument by which the charge is created or evidenced need not be lodged but must, if requested, be produced for the registrar's inspection.[40] Some law firms, it appears, as a matter of practice lodge the instrument of charge along with the prescribed particulars but this does not have to be done as a matter of course and it seems that the registrar is under no duty to check for concordance.

There are other incongruities, however, in the registration apparatus, not least the references to bills of sale. Section 133(3)(d) makes registrable a charge or an assignment created or evidenced by an instrument which if executed by an individual would require registration as a bill of sale. The Bills of Sale Act dates from 1886 and is complicated and obscure.[41]As the Singapore Academy Sub-Committee has pointed out, the march of twentieth century commerce has rendered the Bills of Sale Act archaic in many respects.[42] The sub-committee were of the view that the Act represented a rigid and restrictive approach to personal property security and it should be replaced by a comprehensive personal property security law that applied irrespective of whether the property in question was goods or a chose in action or whether the debtor was a corporate or a non-corporate person. In the words of the Sub-Committee, the new law will be

> ... more rational and comprehensive than the Bills of Sale Act, will require secured creditors who desire priority for their security interests to publicise their interests promptly, will resolve priorities of competing security interests clearly and efficiently, and will enable would be creditors to ascertain the existence of prior security interests, if any, in any

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39 Law Commission Consultation Paper No. 164 on "Registration of Security Interests"—summary of the consultation paper at para. 17.

40 *Companies Act, supra* note 31, section 131 (1A).

41 The Singapore Academy Sub-Committee at para. 2 point out the two-fold objective of the Bills of Sale Act: "first, to require registration of all transactions (known as bills of sale) which pass title to but not possession of personal chattels or which create a charge or right of seizure but leave possession where it is; and second, to prescribe a statutory form of bill of sale for the protection of needy debtors who might otherwise be pressured into giving a bill of sale without fully comprehending its nature and consequences."

42 Reform of the Bills of Sale Act Report, *supra* note 1, para. 6.

> proposed collateral readily. Such a law will lower the costs of taking security from both corporate and non-corporate debtors.[43]

V. Main Features of a New Law

What would be the main features of a new law? There are certain fundamental concepts that underlie Article 9 of the Uniform Commercial Code and systems that build upon it, namely the notions of attachment and perfection of security interests and a general first to file or perfect has priority principle subject to an exception for purchase money security interests *i.e.* security interests created where the advance of funds is specifically linked to the acquisition of new assets. Also fundamental to the Article 9 scheme is a broad definition of "security interest". The Singapore Academy Sub-Committee were sensitive to this consideration and recommended that the law should define the security interest as an interest in personal property created by a transaction which in substance secures payment or performance of an obligation.[44] This statutory statement would be supplemented by a list of specific inclusions and exclusions. One may ask: if there is a specific list, why have the general statement? Part of its function is to serve as a backstop so as to accommodate new financing techniques that may not have developed or been contemplated at the time of the legislation. It can also "handle" omissions in the legislation. Considerable care however needs to be given in the framing of the statutory list and a number of difficult determinations have to be made. Some matters are reasonably straightforward: Article 9 and P.P.S.A. legislation generally encompass the assignment of receivables and reservation of title clauses in sale of goods transactions. But even here there may be a case for specific exclusion to deal with transactions that are not inherently financing in nature, *e.g.* the assignment of receivables as part of the transfer of a business.[45] Moreover, there may be a case for modifying certain aspects of the general statutory scheme in the context of assignments of chooses in action. This seemingly schizophrenic attitude on the part of the law has perturbed certain commentators, even advocates of the Article 9 approach, like Professor Ron Cuming who writes:

> There are two features of the U.C.C., Art. 9 approach that appear to be troublesome even to those who are attracted to it. The first is the total reconceptualisation that it requires in the context of types of transactions that traditionally are not viewed as secured financing devices . . . The

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[43] *Ibid*. at para. 15.

[44] *Ibid*. at para. 17. It was recommended that the personal property security law should be comprehensive, applying equally whether the debtor is an individual, partnership, association or corporation and whether the property which is to be collateral is goods or a chose in action.

[45] See Article 9-109(d)(4).

> second feature . . . is the extent to which it requires a bifurcated approach to the characterisation of certain types of transactions. Since a title retention sales contract or a lease falls within a secured financing regime because it functions as a security device, it follows that the seller or lessor is not the owner of the goods sold or leased . . . What is troublesome is that outside this regime, the recharacterisation might not be acceptable with the result that the same transaction is viewed differently depending on the legal issues being addressed.[46]

It should be stressed that a reformed law would apply irrespective of the location of title. It would not matter whether title belonged to the debtor or to the secured party.[47] The statute applies regardless. This is a major innovation and some trade associations need a lot of convincing as to its merits. For instance, the Association of Hire Purchase and Finance Companies in its comments on the Sub-Committe proposals commented:

> It is established that a hire-purchase agreement is not a moneylending transaction as in essence it is a contract for the delivery of goods on hire under which the hirer is granted an option to purchase the goods which he may or may not exercise. Consequently, until such time when he has exercised the option to purchase he has no proprietary interest in the goods and the goods are not his personal property . . . Neither can he be classified as a debtor in the legal sense of the word.[48]

But Article 9 and P.P.S.A. legislation in other common law jurisdictions characterise matters differently. In the new framework, finance and other professionals are obliged to change their conceptual thinking. A mind shift is required. The Singapore Academy of Law Sub-Committee specifically recommended that hire purchase agreements should be included within the new legislation.[49]

Opinions differ about how reform of personal property security law should deal with leases of personal property. The Uniform Commercial Code in Article 2A tries to distinguish between finance leases and other leases and draws up a detailed list of matters to be brought into the reckoning in the classification exercise. Generally, the Canadian and New Zealand legislation are more direct by subjecting all leases over a certain length, normally one year, to the new regime no matter whether the lease is properly

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[46] "Internationalisation of Secured Financing Law" in Ross Cranston, ed., *Making Commercial Law: Essays in Honour of Roy Goode* (Oxford: Oxford University Press, 1999) at 522–3.

[47] Article 9-202 states that, except as otherwise provided, "the provisions of this article with regard to rights and obligations apply whether title to collateral is in the secured party or the debtor."

[48] Letter dated 3 May 1996 which is reproduced in an appendix to the Reform of the Bills of Sale Act Report, *supra* note 1.

[49] *Ibid*. para. 18.2.

classified as a finance lease or not.[50] This technique was also recommended by the Singapore Academy of Law Sub-Committee.[51] This approach is more sweeping in its scope but may be productive of greater certainty.

Of perhaps greater importance is the legislative treatment of sale and repurchase agreements; particularly in respect of shares and other investment securities. One could subject such transactions to the general regime but then exempt them from certain aspects of its operation or else exclude them entirely. But whatever approach is adopted, care should be exercised to avoid disrupting the smooth functioning of the securities markets and thereby jeopardising a vital national resource.[52]

VI. Attachment and Perfection of Security Interests

Attachment refers to the process whereby a security interest becomes enforceable as between the creditor and the debtor or, in the language of Article 9, "when it becomes enforceable against the debtor with respect to the collateral . . ."[53] For this to occur generally speaking three conditions must be satisfied. Firstly, the creditor must have given value. Secondly, the debtor must have rights in the collateral and thirdly the debtor must have assented in some way whether in writing or by electronic means to the creditor having security. It is important that the legislation should be sensitive to technological innovation and should admit the possibility of authenticating a security agreement in electronic form. Security over after-acquired property should also be permitted but the security interest will not attach unless and until the debtor acquires rights in the collateral.

The second key concept is perfection and this refers to the process whereby the security interest becomes effective against third parties.[54] Attachment must occur before a security interest becomes perfected though a security interest may be perfected on attachment if the necessary steps to

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[50] Section 17(1)(a) of the New Zealand P.P.S.A. 1999. According to the Saskatchewan Law Reform Commission in *Proposals for a Saskatchewan Personal Property Security Act* (1977) at 7: "True consignments and leases have one feature in common with security agreements. They create a potential for deception of innocent third parties who deal with the lessee or consignor, as the case may be, in the belief that no one else has a claim to the property involved."

[51] Reform of the Bills of Sale Act Report, *supra* note 1, para. 18.2. In the Sub-Committee's view, leases for a term exceeding one year include those for a lesser term but renewable for one or more terms, the total of which may exceed one year.

[52] See the discussion of security rights in the context of book-entry securities at text accompanying footnotes 114–120, *infra*.

[53] See Article 9-203.

[54] According to Article 9-308, a security interest is perfected if it has attached and all of the applicable requirements for perfection have been satisfied. A security interest is perfected when it attaches if the applicable requirements are satisfied before the security interest attaches.

achieve perfection such as filing take place before attachment. The normal method of perfecting a security agreement is by filing a financing statement though other methods may be permissible in certain circumstances. One such method that is universally recognised is the taking of possession of the collateral by the secured party.[55] Filing a financing statement is unnecessary in this instance since, as the Singapore Academy of Law Sub-Committee points out, the "fact of possession in the creditor will give notice of the existence of a prior security interest."[56] In other words, the common law pledge is validated in the new statutory context and will take priority from the date of possession over competing non-possessory security interests that purport to cover the same property.

The U.C.C. also recognises perfection by "control" with this concept being developed in response to developments in the international securities markets with the growth of immobilisation and dematerialisation of securities.[57] A secured party is regarded as being in control of shares and other investment securities if the custodian or securities intermediary agrees to honour instructions from the secured party rather than from the debtor.[58] P.P.S.A.s in other jurisdictions generally do not "acknowledge" the concept of control but it is submitted that the Article 9 notion has much to tell us on how to reconcile market exigences with the design of a secured financing system. What is more questionable, however, is Article 9's expansion of "control" from the sphere of the securities markets where it serves a perfectly legitimate function to security over letter of credit rights and deposit accounts. The latter are well settled areas of law and the Article 9 approach in this context leaves something to be desired.[59] Section 13 of the Civil Law Act[60] makes it clear that it is possible for the depositary bank to take a security interest in a deposit account. Another financier may take a security interest in the same deposit account though this will probably rank after any claim by the depositary bank. The new Article 9 goes further and permits the depositary bank to veto the grant of a security interest in the deposit to any other lender. It is submitted that this power of veto goes too far and

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55 See Article 9-313.

56 Reform of the Bills of Sale Act Report, *supra* note 1, at para 20.4.

57 Article 9-314 states that a security interest in investment property, deposit accounts, letter-of-credit rights, or electronic chattel paper may be perfected by control of the collateral.

58 For "control" of investment property, see Article 9-106. It should be noted that under Article 9-309(10) a security interest in investment property created by a broker or securities intermediary is automatically perfected upon attachment, *i.e.* no need for registration. The official comment explains that this special perfection rule is designed to facilitate current secured financing arrangements for securities firms as well as to provide sufficient flexibility to accommodate new arrangements that develop in the future.

59 See generally J. Ziegel, "Canadian Perspectives on the Law Lords' Rejection of the Objection to Chargebacks" (1999) 14 Banking & Finance Law Review 131.

60 *Civil Law Act, supra* note 20.

has no place in a statute that is supposed to be enabling and facilitative of security.[61]

Article 9 also sanctions automatic perfection of security interests in certain circumstances.[62] This is merely a convoluted way of saying that certain security interests are valid without registration. Examples include a purchase money security interest in consumer goods and the assignment of a payment intangible. The latter refers essentially to the sale of loan participations. The loan syndication and participation market is high volume and fast moving and participants in the market were concerned that registration requirements would impede commercial activity.[63] Hence the ingenious compromise struck by the new Article 9 which brings the Article 9 priority rules into play but leaves the existing state of affairs in terms of non-registration intact.

VII. Effect of Non-Perfection of Security Interests

Under section 131 Companies Act,[64] a registrable but unregistered charge is "invalid against the liquidator and any creditor of the company". While the wording of this provision is somewhat obscure it has been interpreted to mean that the charge is invalid in the event of the security giver's liquidation.[65] The same basic result obtains in the United States. In formal bankruptcy proceedings, the bankruptcy trustee, representing unsecured creditors, can claim the mantle of a hypothetical judicial lien creditor and

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61 See the comment by Bruce Markell, "From Property to Contract and Back: An Examination of Deposit Accounts and Revised Article 9" (1999) 74 Chicago-Kent Law Review 963 at 1027: "Revised Article 9's provisions on deposit accounts do have complexities that bear more than one reading. The more one reads, the more one confirms that these complexities do indeed fit together, and snugly. More often than not, however, the result of these re-readings will confirm what one initially suspected; the depositary bank always wins, or at least starts out the game far ahead. "

62 Article 9-309.

63 For an explanation of the provision, see C. Bjerre, "Secured Transactions Inside Out: Negative Pledge Covenants, Property and Perfection" (1999) 84 Cornell L. Rev. 305 at 392, who suggests that the imposition of a filing requirement would impose a large and needless burden on the loan participation market. Loan participations are created when the originator of a loan sells part of it, *i.e.* an undivided interest in the loan and any security given in respect of the loan to a third party, which would normally be another financial institution. The loan participation business is a way in which banks may reduce their exposure to particular borrowers or get loans off their balance sheet for capital adequacy purposes.

64 *Companies Act, supra* note 31.

65 For a discussion of the scope of the provision see *Smith v. Bridgend County Borough Council* [2002] 1 A.C. 336 and see also E. Ferran, *Company Law and Corporate Finance* (Oxford: Oxford University Press, 1999) at 543. For a Singaporean perspective see *Ng Wei Teck Michael v. Oversea-Chinese Banking Corporation Ltd* [1998] 2 S.L.R. 1 which is discussed by Tan Cheng Han, "Unregistered Charges and Unsecured Creditors" (1998) 114 L.Q.R. 565; see also *The Asiatic Enterprises (Pte) Ltd v. United Overseas Bank* [2000] 1 S.L.R. 300.

have an unperfected security interest set aside.[66] This position has been criticised.[67] It is argued that bankruptcy trustees are thereby given an incentive to litigate the issue of perfection and to plead errors in a financing statement that would not in fact have misled any reasonable searcher. Unsecured creditors gain an undeserved windfall, so the argument goes, if a filing is held to be defective.[68] By deciding not to require collateral, unsecured creditors are agreeing to be subordinated to later-in-time perfected secured parties. Even if an unsecured creditor does search and rely upon the existing state of the register, subsequent events could render the information of little value. In other words, the filing system cannot possibly protect an unsecured creditor from having its claim primed by a secured party, because the day after the unsecured creditor's search is made, the debtor could grant a security interest which is then perfected by filing.

Addressing the current law in England, Professor Sir Roy Goode accepts that the effect of avoidance is to give unsecured creditors who did not act in reliance on the want of registration an apparently unjustified windfall. Nevertheless, in his view, there are sound policy reasons for the avoidance of unregistered securities:[69]

> In the first place, the avoidance rule reflects the law's dislike of the secret security interest, which leaves the debtor's property apparently unencumbered and at common law was considered a fraud on the general creditors. Secondly, the registration provisions help to curb the fabrication or antedating of security agreements on the eve of the winding-up. Thirdly, though unsecured creditors have no existing interest in the company's assets outside winding up, [upon winding-up] ... their rights become converted from purely personal rights into rights more closely analogous to that of beneficiaries under an active trust. Fourthly, there may well be unsecured creditors who were misled by the want of registration into extending credit which they would not otherwise have granted. But it would be expensive and impracticable to expect the liquidator (or administrator) to investigate each unsecured creditor's claim to see whether he

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66 Article 547 of the U.S. Bankruptcy Code.

67 See the statement by J. McCoid, "Bankruptcy, the Avoiding Powers, and Unperfected Security Interests" (1985) 59 American Bankruptcy Law Journal 175 at 190 that "invalidation of unperfected security interests by the bankruptcy trustee takes from innocent secured parties to give to unsecured creditors who are not prejudiced by the failure to perfect. Even if avoidance did not take time and effort, one might seriously question this structure which requires those who meant no harm to compensate those who have not been injured, particularly when both bargained for the extension of credit on a different assumption."

68 See E. Smith, "Commentary" (1995) 79 Minn. L.R. 715 at 718; see also more generally C. Scott Pryor, "Revised Uniform Commercial Code Article 9" (1999) 7 American Bankruptcy Institute Law Review 465.

69 *Principles of Corporate Insolvency Law*, 2nd ed. (London: Sweet & Maxwell, 1997) at 420-1.

> did or did not act on the assumption that the unregistered charge did not exist. So a broad brush approach which in effect assumes detriment to unsecured creditors at large is justified. Finally, the registration provisions serve a general public notice function as well as being a registration requirement . . .

These arguments were not accepted in New Zealand where, in a conscious departure from the Article 9 and Canadian P.P.S.A. models, a notice-filing system was introduced without any invalidation of unperfected security interests in liquidation.[70] One of the New Zealand Law Commissioners, responsible for the preparation of the legislation, specifically took issue with the propositions advanced by Professor Goode and suggested that they rested on an outdated conception of how business was actually conducted.[71] The policy against secret security interests was misplaced because nowadays there was little danger of a creditor being induced to give credit on the assumption that goods in the debtor's possession are the debtor's own property. In his view, the reliance on apparent ownership to extend credit argument was seriously out of date in the light of modern business conditions.

It is submitted that, on balance, the New Zealand approach is not one that should be followed in Singapore.[72] While an unsecured creditor may not actively seek a proprietary right against the company, the register provides important information about the existence of creditors who possess such rights.[73] A wider reliance interest is promoted in that the general credit assessment of the company would involve the receipt of such information.

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[70] See the New Zealand Law Commission Report No. 8, "A Personal Property Securities Act for New Zealand" (1989) at 115: "In practice, only two parties are possibly misled by the absence of a registration statement. The first is the prospective creditor who would normally advance credit only against a first ranking security in a debtor's goods. Under the proposed statute, if such a creditor files a registration statement, it is protected against any unperfected security interests . . . Creditors, who supply goods or funds on an unsecured basis are generally either not concerned about the presence of outstanding interests or assume that such interests exist. Prospective buyers and lessees, like prospective secured creditors, also rely heavily on the ostensible ownership of their transferor. Accordingly, they are protected from unperfected security interests . . . unless they have knowledge of the security interest."

[71] See D.F. Dugdale, "The Proposed PPSA" [1998] New Zealand Law Journal 383 at 384.

[72] The Dugdale view is not one that appeals to all New Zealand commentators. See, for instance, D. McLauchlan, "Unperfected Securities under the PPSA" [1999] N.Z.L.J. 55 who argues that if the policy objective of adherence to the perfection requirement is to be achieved then failure to perfect should have the meaningful penalty of defeating the security interest on the insolvency of the debtor. In McLauchlan's view, this is a bare minimum step that the law should take in redressing the balance somewhat in favour of unsecured creditors.

[73] See J. De Lacy, "Ambit and Reform of Part 12 of the Companies Act 1985 and the Doctrine of Constructive Notice" in J. De Lacy, ed., *The Reform of UK Company Law* (London: Cavendish, 2002) at 362–3 [J. De Lacy] but *cf.* D. Baird, "Notice Filing and the Problem of Ostensible Ownership" (1983) 12 J. Legal Stud. 53 at 60.

Regular inspections of the register enable an unsecured creditor to police any negative pledge covenants that might exist in the loan agreement and also to police the borrower more generally.[74] The presence of a security interest on the register could cause an unsecured creditor to alter the conditions of the loan or the other terms of the business relationship with the debtor. The fact that a particular individual unsecured creditor may not have relied on the register in this way is irrelevant. As one commentator notes:

> The hypothetical nature of the unsecured creditor in this context is designed to remove complex factual inquiries that would otherwise occur at considerable expense to the liquidation process thereby prejudicing creditors as a whole. Indeed the concept of reliance in this context would be exceedingly difficult to establish or refute were it be made fact specific.[75]

As far as secured parties are concerned, registration does not seem too high a price to pay to assume priority over unsecured creditors. Allowing unperfected security interests to prevail over unsecured creditors would contribute to the further marginalisation of the latter in the insolvency process and this state of affairs may not be acceptable.

VIII. Notice Filing and the Consequences of the Same

Article 9 and systems that derive from it are based on notice rather than transaction filing.[76] Instead of registering details of a particular security agreement that has already been executed, a secured party would merely file notice that he intends to take a security interest in all the debtor's property. Filing could take place either before or after a security agreement has been executed and filing would not be tied to a specific security agreement.[77]

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[74] On the possible prejudice that may be suffered by unsecured creditors through "springing" security interests and so-called affirmative negative pledge clauses see Tan Cheng Han, "Charges, Contingencies and Registration" (2002) 2 Journal of Corporate Law Studies 191.

[75] J. De Lacy, *supra* note 73 at 356-7. De Lacy refers in this connection to the observations of Lord Wilberforce in *Midland Bank Trust Co Ltd v. Green* [1981] A.C. 513 at 530.

[76] For a discussion of the pro and cons of notice filing versus transaction filing and indeed of having a registration system at all see the symposium in the 1995 Minnesota Law Review.

[77] For the following panegyric to notice filing see para. 1.50 of the English Law Commission Consultation Paper on "Registration of Security Interests" (July 2002): "A system of notice-filing would make it substantially easier for companies ... to register security interests. Filing could be done electronically by the completion of a simple on-screen form and the information filed would appear on the public register without imposing on registry staff the burden of checking the information submitted. Although less information would have to be submitted, there would be little reduction in the practical value of the register as a source of information about the company's financial affairs. Further, a potential creditor could have confidence that any charge it filed would have priority over any earlier charge that does not

In other words, by a single filing, a creditor could effectively perfect any actual or potential security agreements with the debtor. To avoid the register being cluttered up however with useless or even possibly malicious filings legislation may require the authorisation of the debtor before registration can be effected. Moreover, there should be a mechanism whereby registrations that do not relate to any actual or contemplated borrowings can be removed from the register.[78]

One issue that needs to be addressed is the interaction between notice filing and the priority of future advances under existing agreements. At common law, under the rule in *Hopkinson v. Rolt*,[79] notice of an intervening security interest terminated the ability of a secured party to make further advances that would have priority over later lenders. Article 9 systems generally state that a security interest has the same priority in respect of all advances, including future advances. This effectively abolishes the rule in *Hopkinson v. Rolt* and is a sensible provision given the inherent features of notice filing. Under notice filing, priority of security agreements dates from the date of filing a financing statement that may be a general umbrella statement covering more than one security agreement. If a second secured lender arrived on the scene after the first secured party had taken a security agreement and filed a financing statement and the first secured party wanted to make further advances to the debtor that took priority over the intervening creditor, one approach would be to get the debtor to execute another security agreement and then to make advances under this subsequent agreement. Priority of loans under the later agreement would date back to the original financing statement and outrank the intervening creditor. If this result may be achieved by the expedient of executing a subsequent security agreement then there seems little sense in precluding it by the simpler strategy of making further advances under the initial security agreement.[80]

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appear on the register and any subsequent charge (other than a purchase-money interest). The system would permit filing in advance of the creation of the security, in order to preserve priority during negotiations; and a single financing statement could be filed to cover future transactions, thus obviating the need to register successive security interests as and when they are created. This might lead to an increase in the amount of information available to the public, as it would be possible to register charges that, under the present system, have to be excluded from registration requirements because registration of each charge is impractical."

78 See section 162(d) of the New Zealand P.P.S.A.

79 (1861) 9 H.L. Cas. 514.

80 See generally Widdup and Mayne, *supra* note 3 at 134–5. The authors point out that since the future advance provisions are quite powerful, secured parties should always be wary of taking a subordinate interest. It is the counsel of prudence to obtain a priority agreement from the prior registered secured party.

IX. Priority Between Competing Security Interests

New priority rules embodied in a statutory scheme should be an improvement on the existing position. The difficulties in determining priorities are compounded by the fixed/floating charge distinction. Generally speaking a fixed charge will rank ahead of a floating charge irrespective of the dates of creation of the two charges unless it appears that a prior floating charge contains a restrictive clause and the subsequent fixed charge holder has actual notice of the restrictive clause.[81] A restrictive clause is a clause in the instrument containing the floating charge that precludes the creation of subsequent security interests ranking prior to or passu with the floating charge. Actual notice rather than merely constructive notice is required, however, before the fixed chargeholder loses priority though the Singapore courts have made it clear that the onus is on the subsequent fixed security interest holder to show that it is without actual notice.[82] What is less clear though is the precise effect of the relevant statutory form which allows details of a restrictive clause to be included in the particulars delivered for registration.[83] Does this signify a form of statutory imputed notice if the restrictive clause particulars are included? One might argue not on the basis that this particular is merely an optional extra rather than being mandatory. On the other hand, if a later secured party searches the register and discovers the particular then he is infected with notice.[84]

The priorities as between the fixed and floating charge is complicated enough but what adds to the complexity is the difficulty in distinguishing between the two. The Singapore High Court and Court of Appeal came to different conclusions on the characterisation issue in *Dresdner Bank v. Ho Mun Tuke Don*.[85] The *Ho Mun Tuke Don* case concerned the nature of security over shares but, fortunately, Singapore has been spared the abundance of litigation concerned with charges over receivables that has plagued England

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81 See *Kay Hian & Co. (Pte.) v. Jon Phua Ooi Yong* [1989] 1 M.L.J. 284 [*Kay Hian*]; *United Malayan Banking Corp v. Aluminex* [1993] 3 M.L.J. 587 and see generally Tan Cheng Han, "The Negative Pledge as a Security Device" (1996) Singapore Journal of Legal Studies 415.

82 *Kay Hian, supra* note 81. On the point see generally Hans Tjio, "Of Prohibitions on Assignments, Restrictive Covenants and Negative Pledges in Commercial Law: Clogs on Commerce" (1994) 6 S. Ac. L.J. 159 at 172–4.

83 For access to the latest Companies forms in Singapore see online: Registry of Companies and Businesses <http://www.bizfile.gov.sg/>.

84 See the comment in Walter Woon and Andrew Hicks, *The Companies Act of Singapore: An Annotation*, looseleaf (Singapore: Butterworths, continually updated) [Walter Woon] at para. 7251: "Form 34 of the Companies Regulations makes provision for noting the restrictions or prohibitions on the company in connection with the charge (para. 7) and some salient covenants or terms and conditions of the instrument of charge (para. 8). Since a person who does a search will presumably come across such matters if noted, should there not be constructive notice of these?"

85 [1993] 1 S.L.R. 114.

and certain other common law jurisdictions.[86] The Privy Council, though, has introduced a welcome measure of clarification by holding in *Agnew v. Commissioner of Inland Revenue*[87] that before a fixed charge designation over receivables can be upheld the security giver must be restricted in what it can do with the proceeds of the receivables.

Article 9 schemes sweep away the fixed/floating charge distinction. The two types of security interest are assimilated. One leading commentator has remarked that the greatest insight of drafters of reformed personal property security legislation has been to recognise that a security interest is not necessarily incompatible with a freedom on the part of the debtor to dispose of assets used as security in the ordinary course of business.[88] This insight applies across the board. All security interests under a new dispensation are of the same character. One of the present day mysteries of the floating charge is deciding when it crystallises, *i.e.* gets converted into a fixed charge. The courts have also recognised "automatic crystallisation" and "de-crystallisation".[89] These concepts, while useful, contribute to the difficulty in expounding the law. A new system would excise these complications from the law. The new system may, however, have to put in place measures to protect the position of preferential creditors. Under sections 226 and 328 of the Singapore Companies Act[90] employee benefits including retrenchment benefits but not unpaid tax claims are paid ahead of floating charge holders in a receivership or liquidation. These provisions afford a measure of protection to employees but the protection is quite limited since secured creditors can effectively outflank the statutory scheme by taking fixed, rather than floating, charges, over as wide a range of assets as possible. Nevertheless, there is a residual protection which employees may be loath to lose, especially in days of economic retrenchment. Law reformers in other jurisdictions have grappled with the problem of how to protect existing preferential entitlements in a new statutory environment. In New Zealand, security interests in inventory and receivables, other than purchase money

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86 See *e.g.* cases like *Re New Bullas Trading Ltd.* [1994] 1 B.C.L.C. 485 and *Supercool Refrigeration and Air Conditioning v. Hoverd Industries Ltd.* [1994] 3 N.Z.L.R. 300.

87 [2001] 2 A.C. 710 and see also *Smith v. Bridgend County Borough Council* [2002] 1 A.C. 336. For commentary on the *Agnew* case (which is often termed "*Brumark*" as it was called in the New Zealand courts before it reached the House of Lords) see G. McCormack, (2002) 23 Company Lawyer 84; P. Watts, (2002) 118 L.Q.R. 1; A. Berg, [2001] J.B.L. 532; P. Wood, [2001] C.L.J. 472.

88 See generally R. Goode, "The Exodus of the Floating Charge" in D. Feldman and F. Meisel, eds., *Corporate and Commercial Law: Modern Developments* (London: L.L.P., 1996) at 202-3.

89 *Re Brightlife Ltd.* [1987] Ch. 200 and see generally Tan Cheng Han, "Automatic Crystallisation, De-Crystallisation and Convertibility of Charges" [1998] Company, Financial and Insolvency Law Review 41.

90 *Companies Act, supra* note 31.

security interests, are postponed to preferential claims[91] whereas in England the Law Commission recommended that preferential claims would still be payable ahead of loans secured by a security interest that allows the debtor a continued power to dispose of assets in the ordinary course of business.[92] It might be argued that neither of these approaches is entirely satisfactory. The New Zealand legislation apparently suffers from flaws in drafting[93] whereas the English approach depends on a continued fixed/floating charge distinction that Article 9 schemes were intended to eliminate.

Assimilation of fixed and floating charges would require certain other adjustments to company and insolvency legislation in Singapore. For instance, the holder of a floating charge over the whole or substantially the whole of a company's assets has a power of veto over the appointment of a judicial manager to an ailing company[94] but if it was desired to preserve the substance of the veto, the provision could easily be altered to refer to the holder of a security interest rather than the holder of a floating charge. Likewise with section 330 Companies Act,[95] which invalidates floating charges granted to secure past indebtedness within six months prior to winding up of the corporate debtor. With the disappearance of the floating charge *per se* the provision could be widened to cover all security interests granted within this time frame.

X. Priorities And the Purchase Money Security Interest

In the Article 9 framework, priority between competing security interests would turn on the date of filing a financing statement subject to an exception for purchase money security interests or P.M.S.I.s.[96] The special recognition accorded P.M.S.I.s is a hallmark of Article 9 and is designed to prevent the first creditor on the scene from having a security monopoly over the assets of the debtor and thereby to restrict the debtor's access to further funds.[97] A P.M.S.I. arises where a creditor advances funds on condition that it is used for the acquisition of particular property; the funds are so used and the debtor takes security in the property acquired as a result. The

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91 See generally the Seventh Schedule to the Companies Act 1993 as amended by the P.P.S.A. legislation.

92 See para. 4.136 of the Law Commission Consultation Paper No. 164 on "Registration of Security Interests".

93 See generally Widdup and Mayne, *supra* note 3 at 287–288 and Gedye, *supra* note 3 at 21–22.

94 *Companies Act, supra* note 31, section 227B(5).

95 *Companies Act, supra* note 31.

96 See Article 9-324.

97 See generally Thomas Jackson and Anthony Kronman, "Secured Financing and Priorities Among Creditors" (1979) 88 Yale L.J. 1143 at 1171–8.

P.M.S.I. holder ranks ahead of an earlier creditor with an after-acquired property clause. The rationale of this special priority principle is to widen the base of potential lenders. If the first creditor refuses any further finance, then later lenders may be reluctant to lend either with later-ranking security or on an unsecured basis. Recognising and "privileging" the P.M.S.I. may free up the channels of credit.[98] The P.M.S.I. may also be seen as, at worst, neutral as far as earlier lenders are concerned in that the injection of funds and consequent security is balanced by the acquisition of the asset. Moreover, the P.M.S.I. could be seen as potentially value-enhancing for earlier creditors in that the new assets may enable the debtor's business to generate sufficient income so as to repay the earlier loans. The Singapore Academy of Law Sub-Committee embraced the notion of the P.M.S.I. In its view, purchase money security interests represent the injection of new value into the debtor's business and the injection of new value which keeps the business going should be encouraged and rewarded with super-priority. It added: "This will not subtract from the assets available to a prior security interest holder since the super-priority is given in respect only of new assets which the purchase money has brought in into the business."[99]

The policy rationale underlying the P.M.S.I. was articulated in this part of the world by the Malaysian Supreme Court in *United Malayan Banking Corporation v. Aluminex* in the following terms:

> In a contest between the holder of a charge over after acquired property and the holder of a purchase-money security interest taken to secure the price of an asset falling within the ambit of the class defined by the after acquired property clause, the merits would appear to lie with the holder of the purchase money security interest; after all, it was he who provided the necessary financial assistance required to purchase the after acquired property and it would appear to be neither right not fair that the holder of the charge over after acquired property could now, as it were, scoop up the asset or its proceeds to the exclusion of his opponent.[100]

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98 But for a contrary perspective see W.J. Gough, *Company Charges* 2nd ed. (London: Butterworths, 1996) at 436: "It assumes that financial accommodation for the purpose of, for example, paying wages and salaries through cheques drawn on an overdrawn account is less important than for the purchase of stocks or plant and equipment. This is not a real world distinction. Credit, as a matter of business need, is indivisible in the sense that all business inputs, including wages, overheads, equipment and supplies are all vital to an ongoing business."

99 Reform of the Bills of Sale Act Report, *supra* note 1 at para. 22.1.

100 [1993] 3 M.L.J. 587 at 603; on which see generally Hans Tjio, "Personal Property Security Interests in Singapore and Malaysia" (1995) 16 Company Lawyer 28 at 30–1.

The court added however:

> . . . [O]ur research into the authorities shows that neither in England nor in Australia is there any policy for the protection of the holder of the purchase money security interest; instead, the approach adopted by the courts there in resolving the dispute, is a technical one, everything depending upon whether the equitable rights of the holder of the purchase money security interest be he mortgagee or chargee, under the contract to make the loan advance, attaches to the property before the borrower company concerned acquires the legal ownership of it on completion of the purchase.[101]

While the recognition of P.M.S.I.s in Article 9 and P.P.S.A. systems is almost universal, jurisdictions differ on the conditions that must be satisfied before P.M.S.I. status can be obtained and the lengths to which super-priority may be claimed. Article 9 distinguishes between a P.M.S.I. over inventory and a P.M.S.I. over capital goods with the latter being more easy to establish. Basically before P.M.S.I. status in inventory can be attained the secured party must give notice to holders of potentially conflicting security interests in the same property that he intends to take a P.M.S.I. in inventory.[102] The notice must describe the inventory. The notification requirement is designed to safeguard the position of an earlier creditor who releases funds periodically to the debtor upon the acquisition of inventory. Notice will enable the ongoing financier to adjust his position accordingly.[103] Nevertheless, the notification requirement obviously goes wider than this specific situation and it may be that it dilutes unnecessarily the simplicity of the statutory structure. The responsible authorities should consider carefully whether it is a necessary part of any new legislation. The Singapore Academy Sub-Committee thought otherwise, observing:

> [N]otification of a prior secured creditor is unnecessary since the requirement that a financing statement describing the purchase money security interest be filed within a specified period from the time of acquisition of the inventory or equipment already implies that the prior secured creditor

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[101] [1993] 3 M.L.J. 587 at 603.

[102] Article 9-324(c).

[103] See the explanation offered in the Official Comment to Article 9-324: "The arrangement between an inventory secured party and its debtor typically requires the secured party to make periodic advances against incoming inventory or periodic releases of old inventory as new inventory is received. A fraudulent debtor may apply to the secured party for advances even though it has already given a purchase-money security interest in the inventory to another secured party . . . Inasmuch as an arrangement for periodic advances against incoming goods is unusual outside the inventory field, [the provision for capital equipment] does not contain a notification requirement."

> who wishes to make more advances to the debtor can check the register and discover the exact nature of the new inventory or equipment.[104]

Legislation will also need to address the question whether a P.M.S.I. loan should lose its P.M.S.I. character if it is refinanced or consolidated with another loan. The 1999 revision of Article 9 provides valuable guidance by stipulating that "transformation" in this way does not have a destructive impact on the P.M.S.I. security. Moreover, the revised Article 9 expressly affirms that a P.M.S.I. may have dual status, *i.e.* it may validly secure non-purchase money obligations without forfeiting its P.M.S.I. character.[105]

A more controversial question is whether the P.M.S.I. can legitimately extend into proceeds and products or whether such claims by a financier will be regarded as a general security interest that does not attract any special priority protection. The point becomes clearer if one takes the example of a seller of goods who employs a retention of title clause in the sale of goods contract. If the seller registers a financing statement and complies with the other conditions the seller will have a P.M.S.I. in the goods supplied, *i.e.* the seller's claim has super-priority and outranks that of a general creditor of a buyer whose security extends to the buyer's after-acquired property. But if the goods are resold by the buyer producing proceeds the question arises whether the conditional seller's claim has super-priority vis-à-vis the proceeds? This is generally the position in New Zealand[106] but, under Article 9, the requirements for obtaining a P.M.S.I. in proceeds are more stringent.[107] It may be that the New Zealand position is explicable on the basis of the favourable treatment accorded proceeds of sale retention of title clauses at common law and a wish on the legislature's part not to disturb such favourable treatment. In New Zealand, the courts in cases like *Len*

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104 Reform of the Bills of Sale Act Report, *supra* note 1 at para. 22.3.

105 Article 9-103(f). For a discussion of these general issues see J. Honnold, S.L. Harris and C.W. Mooney, *Security Interests in Personal Property*, 3rd ed. (New York: Federation Press, 2001) at 247–52.

106 Sections 73–75, New Zealand P.P.S.A., 1999.

107 Under Article 9-324, the P.M.S.I. status of a perfected security interest in inventory will only extend to identifiable cash proceeds of the inventory and will not, for example, apply if the proceeds of the inventory are, say, receivables. The official commentary to the Revised Article 9-324 explains: "Debtor creates a security interest in its existing and after-acquired inventory in favour of SP-1, who files a financing statement covering inventory. SP-2 subsequently takes a purchase-money security interest in certain inventory and, under subsection (b), achieves priority in the inventory over SP-1. This inventory is then sold, producing accounts. Accounts are not cash proceeds, and so the special purchase-money priority in the inventory does not control the priority in the accounts. Rather, the first-to-file-or-perfect rule of Section 9-322(a)(1) applies." The point is also discussed by Catherine Walsh, "The Floating Charge is Dead; Long Live the Floating Charge" in Agasha Mugasha, ed., *Perspectives on Commercial Law* (St. Leonards, NSW: Prospect, 1999) at 139-40.

Vidgen[108] upheld claims by the original seller to proceeds of goods supplied under a reservation of title agreement. In England, by contrast, while such a claim was recognised in the seminal *Romalpa* case in 1976,[109] since then claims have been rejected on a variety of grounds so much so that it is difficult to visualise a fact situation where such a claim would now be upheld.[110] Direct authority on the issue is absent in Singapore but the tendency of the courts as manifested in *Gebreuder*[111] has been to limit the scope of retention of title clauses. This being so it is submitted that a Singapore court is more likely to follow the English approach towards proceeds of sale retention of title. While this requires considerable extrapolation and supposition, the Singapore Parliament may take a narrow view on recognising P.M.S.I.s in proceeds.[112]

XI. Chattel Paper and Special Priority Rules

Under the Article 9 scheme of things, written conditions of sale embodying a retention of title clause or a written finance lease is said to represent chattel paper in the hands of the conditional seller or lessor as the case may be. The conditional seller/lessor may refinance its activities by using the chattel paper as security. Moreover, a financier who takes possession of the tangible chattel paper may be able to assert super-priority over earlier general creditors of the conditional seller/lessor that are claiming the chattel paper either as original collateral or as the proceeds of other collateral.[113] The Singapore Academy of Law Sub-Committee suggested that chattel paper had some of the attributes of negotiability and, to accommodate this fact, a purchaser of chattel paper taking possession of the chattel paper in the ordinary course of his business should have priority over a security interest in the chattel paper of which he has no knowledge.[114] To avoid the risks of losing priority, a prior secured party could stamp or note the assignment to him on the chattel paper. The Sub-Committee, however, also recommended that a "purchaser of chattel paper taking possession of the chattel paper in the ordinary course of his business should also have priority over a security interest in the chattel paper, notwithstanding his knowledge of the

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[108] *Len Vidgen Ski & Leisure Ltd. v. Timaru Marine Supplies Ltd.* [1986] 1 N.Z.L.R. 349 and see also in *Australia Associated Alloys Pty. Ltd. v. Metropolitan Engineering & Fabrications Pty. Ltd.* (2000) 202 C.L.R. 588.

[109] *Aluminium Industrie Vaassen B.V. v. Romalpa Aluminium Ltd.* [1976] 1 W.L.R. 676.

[110] See generally *Pfeiffer Weinkellerei v. Arbuthnot Factors* [1988] 1 W.L.R. 150; *Compaq Computer Ltd. v. Abercorn Group Ltd.* [1991] B.C.C. 484.

[111] *Gebreuder, supra* note 33.

[112] See generally on this whole area Widdup and Mayne, *supra* note 3 at 196–199 and 217–225 and Gedye, *supra* note 3 at 281–294.

[113] Article 9-330 deals with the priority of purchasers of chattel paper.

[114] Reform of the Bills of Sale Act Report, *supra* note 1, para. 24.1.

security interest, when the security interest is claimed merely as proceeds of inventory subject to a security interest."[115]

A couple of comments are appropriate. Firstly, one wonders whether chattel paper financing is so distinct from receivables financing more generally that special priority rules are warranted. Why not subject chattel paper to the normal first-to-file-has-priority principle, like assignments of choses in action? At the time that Article 9 was first formulated in the 1950s, chattel paper financing represented a distinct discrete category and special rules were adopted.[116] The Canadian and New Zealand P.P.S.A.s mirror the Article 9 scheme but it may be that the provisions are more a historical remnant than a barometer of contemporary financing and industry practices.[117] Secondly, the new Article 9 equates "control" of electronic chattel paper with possession of physical chattel paper. If Singapore went down the route of recognising chattel paper as a special category of collateral meriting special rules, then consideration should be given to extending the provisions to embrace electronic chattel paper.[118]

XII. Security Over Investment Property and "Control" as A Superior Method of Perfection

Another revised Article 9 provision that is worth considering in Singapore is the notion of "control" of collateral. According to certain commentators,

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115 Reform of the Bills of Sale Act Report, *supra* note 1, para. 24.3.

116 For a criticism of the privileged treatment afforded chattel paper financing see J. Zekan, "Chattel Paper Financing: Metaphysical Property and Real Money" (1992) 29 Idaho L. Rev. 723 at 744–46, who argues that the super-priority principle rewards ignorance on the part of chattel paper financiers as well as undermines the more general policy underlying Article 9 which is based on the primacy of the filing system. In her view, chattel paper no longer merits special treatment if it ever did. For more standard accounts and justifications see J. Levie, "Security Interests in Chattel Paper" (1969) 78 Yale L.J. 935 and D. Rapson, "Receivables Financing under Revised Article 9" (1999) 73 American Bankruptcy Law Journal 133.

117 See the comments of the New Zealand Law Commission in Report No. 8, "A Personal Property Securities Act for New Zealand" (1989) at 81–2 when proposing draft new legislation for New Zealand: "The term chattel paper has no counterpart under current New Zealand law. It includes hire purchase agreements, finance leases and conditional sale contracts. Such writings serve primarily to document rights and obligations of the parties to the particular transaction. However, the bundle of rights arising under such an agreement comprises a distinct form of personal property. The proposed statute facilitates the use of this property as an independent source of credit. Parties who inject new value into the debtor's business by purchasing or lending against chattel paper enjoy priority over creditors who claim the paper as proceeds or after-acquired property."

118 In the main, control of "electronic chattel paper" is equated with possession of tangible chattel. For a discussion of the rules pertaining to electronic chattel paper see J. Winn, "Electronic Chattel Paper under Revised Article 9: Updating the concept of Embodied Rights for Electronic Commerce" (1999) 74 Chicago-Kent Law Review 1055; Gross and Jones, "The Treatment of Electronic 'Chattel Paper' under Revised Article 9" (1998) 31 U.C.C. L.J. 47.

the revised Article 9 embodies a perfection hierarchy with "control" being recognised as a superior method of perfection than filing a financing statement.[119] In other words, a secured party that is perfected by control will have priority over another secured party perfected by filing irrespective of the dates of creation of the two security interests. In the context of the securities market and security over securities, if a custodian or securities intermediary agrees to respond to instructions from the secured party rather than from the debtor, then the secured party is regarded as having control of the collateral and will take priority over a competing security interest. It is still perfectly possible to perfect a security interest in the standard way through notice filing but this is clearly second best. Having the securities intermediary execute a control agreement is preferable from the priority point of view.[120] Also, it should be noted that a security interest created by a broker or a securities intermediary is automatically perfected, *i.e.* the security interest is valid without registration.[121]

Singapore may care to replicate such provisions but, it is submitted, should not follow the approach recommended by the English Law Commission who suggested that "control" be the sole permissible method of perfecting a security interest over shares and other investment securities.[122] This stance is very restrictive and forecloses the possibility of having, in the new statutory set-up, any equivalent of the existing floating charges over shares. This form of security is weak in that it may easily be trumped by a competing security interest holder. Nevertheless, it may be intended to form part of an overall security package and, given the general objective of facilitating security interests, it does not seem sensible to preclude the possibility of such a security arrangement.

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[119] See generally R. Picker, "Perfection Hierarchies and Nontemporal Priority Rules" (1999) 74 Chicago-Kent L. Rev. 1157 who argues that the Revised Article 9 does a better job than previously of matching collateral taken and reliance on it, assuming that control is a good proxy for reliance.

[120] Article 9-328. As the Official Comment explains: "The control priority rule does not turn on either temporal sequence or awareness of conflicting security interests. Rather, it is a structural rule, based on the principle that a lender should be able to rely on the collateral, without question if the lender has taken the necessary steps to assure itself that it is in a position where it can foreclose on the collateral without further action by the debtor."

[121] Article 9-309. As one commentator has explained, the principle of automatic perfection of security interests created by securities intermediaries arises because in this situation there is "a presumption of encumbrance—ostensible non-ownership"—see J. Schroeder, "Is Article 8 Finally Ready This Time? The Radical Reform of Secured Lending on Wall Street" [1994] Columbus L. Rev. 291 at 399.

[122] See para. 5.24 of Consultation Paper No. 164 on "Registration of Security Interests" (July 2002). In fairness, however, to the Law Commission it asked respondents to the consultation exercise whether it should be possible to perfect a charge over shares by filing a financing statement as an alternative either to taking possession of the certificates or taking control—see paras. 12.59-1260.

In making provision for security over investment securities, any new legislative framework would have to consider integrating the provisions of section 130N Companies Act.[123] Sections 130A-130P Companies Act set out the legal framework for the operation of a book entry or scripless system for the transfer of securities. The regime applies to book-entry securities of listed securities of Singapore-incorporated companies and was introduced as the legal response to increasing automation and paperless trading on the Singapore Stock Exchange.[124] As Professor Walter Woon explains:[125]

> . . . [G]oing scripless did not mean doing away with share certificates altogether. What happened was that the registered shareholders of a listed company transferred their shares to the Central Depository Ptd Ltd ('CDP', a wholly-owned subsidiary of the Stock Exchange of Singapore Ltd.), which then appeared in the listed company's books as the holder of those shares. CDP maintains accounts for each 'depositor'. When a depositor sells his shares, CDP debits his account and credits the account of the buyer. Since no change is made to the registered shareholding, no transfer form has to be lodged with the registered company.

Under section 130N there is a special statutory procedure for creating security interests in book-entry securities. Compliance with the procedure is necessary to ensure the validity of the security interest though there is a saver for floating charges.[126] A security interest in book-entry securities may be created in favour of any depositor either by way of assignment or by way of charge. It is not possible to create successive security interests using the statutory form though you might have a statutory security interest followed by a general floating charge over all the security giver's property including book entry securities. While the matter is not specifically addressed in section 130N, presumably the statutory security interest would win any priority contest on normal priority principles. Section 130N(4) provides that charges over book-entry securities should be registered in a register of charges maintained by the Depository but this register is only open to inspection by the chargor, the chargee and their authorised representatives.

While the details are different the fundamentals of the Singaporean scheme for security interests in book-entry securities equate with the Article 9 "control" approach. The section 130N statutory procedure essentially involves the Depository (which is the custodian of the securities) responding

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123 *Companies Act, supra* note 31.

124 See W. Woon, "The Changing Market—Whither the Law? Implications of the Central Depository System" in *The Regulation of the Financial and Capital Markets* (Singapore: Singapore Academy of Law, 1991) at 157–166; W. Woon "The Scripless Trading System in Singapore" (1993) 1 International Journal of Law and Information Technology at 77–89.

125 See Walter Woon, *supra* note 33 at para. 6338.

126 *Companies Act, supra* note 31, section 130N(19).

to instructions from the security taker rather than the security giver vis-à-vis the securities. The continued possibility of taking a floating charge could be likened to the Article 9 alternative of perfecting a security interest over securities by filing rather than by control but, like the floating charge in Singapore, the filing alternative carries less clout in a priority contest.

XIII. Protecting the Integrity of the Market Place and Good Faith Purchase

Where goods subject to a security interest are sold legislation should enable a good faith purchaser of such goods to take free of the security interest. This is necessary to protect the integrity of the market place. At the moment the grantor of a floating charge has an implied authority from the grantee to dispose of assets free from the security interest in the ordinary course of business.[127] Even with a fixed charge, however, a buyer of goods will take the goods free from the charge if he is unaware of it.[128] This position remains the same even if the charge has been registered since the buyer is not somebody who might reasonably be expected to search the register.[129]

New legislation would have to work out how knowledge of a security interest would affect the precise position of a purchaser. The courts have consistently held that constructive notice ("what a purchaser ought to have known") has no general role in commercial transactions and constructive notice should not stage a re-emergence under the new dispensation. Purchasers of low value consumer items, *i.e.* items intended for personal or household use cannot reasonably be expected to check a register to discover whether such items are subject to security interests.[130] The same holds true for purchasers of investment securities or negotiable instruments. Under the New Zealand P.P.S.A., purchasers of such securities or instruments will take free of security interest even if they know of the existence of the security interest provided that they do not know that the sale breaches the terms of the security agreement.[131]

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[127] This is inherent in the very nature of a floating charge, on which see generally *Dresdner Bank AG v. Ho Mun-Tuke Don* [1993] 1 S.L.R. 114.

[128] A buyer of goods would take subject to a legal mortgage over the goods as where the equities are equal the first in time prevails. A security interest in goods however is much more likely to be legal rather than equitable—see *Holroyd v. Marshall* (1862) 10 H.L. Cas. 191 and *Tailby v. Official Receiver* (1888) 13 App. Cas. 523.

[129] The equitable doctrine of constructive notice is said not to apply to commercial transactions—see *Manchester Trust v. Furness* [1895] 2 Q.B. 539 and *Feuer Leather Corporation v. Frank Johnstone & Sons* [1981] Com. L.R. 251.

[130] See Widdup and Mayne, *supra* note 3 at 125 and Gedye, *supra* note 3 at 231–234.

[131] Sections 96 and 97 P.P.S.A.

The Singapore Academy of Law Sub-Committee recommended a more blanket exclusion of consumer transactions from the scope of new legislation, stating that

> ... any security agreement creating interests in consumer goods ... of less than $50,000 in aggregate value should be excluded so as not to clutter up the proposed register of personal property security interests. Another important consideration is that the regulation of secured credit financing for commercial purposes is more important than secured credit financing for consumer purposes; a consumer good is unlikely to be the subject of a second security transaction.[132]

On the other hand, one hardly wants the archaic Bills of Sale Act to survive just to apply to consumers. Perhaps a better approach might be to adjust the new legislation in places so that it is tailored to consumer transactions. Article 9 is instructive in this regard for a purchase money security interest in consumer goods is deemed to be automatically perfected, *i.e* the security interest is valid without registration. This approach has the beauty of subjecting consumer transactions to some of the general rules on validity, creation, attachment and priority of security interests but at the same time avoiding the inconvenience and bureaucracy of filing.[133]

XIV. Remedies

Part 6 of Article 9 contains remedies for the enforcement of security interests but these must be read in conjunction with Chapter 11 of the U.S. Bankruptcy Code which contains provisions for a moratorium or embargo on the enforcement of security when a corporate debtor is undergoing reorganisation proceedings.[134]

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[132] Reform of the Bills of Sale Act Report, *supra* note 1, para. 23.1. It should be noted that the average price of a new motor vehicle in Singapore is in excess of $50,000 and, consequently, security interests over motor vehicles would be included in the new legislation.

[133] The provisions of Article 9-204(b) should also be noted. These provide that, as a general rule, a security interest will not attach under an after-acquired property clause to consumer goods unless the debtor acquires rights in them within ten days after the secured party gives value.

[134] On Chapter 11 see generally R. Broude, "How the Rescue Culture Came to the United States and the Myths that Surround Chapter 11" (2000) 16 Insolvency Law and Practice 194. The economic efficiency *etc.* of Chapter 11 is discussed in M. Bradley and M. Rozenweig, "The Untenable Case for Chapter 11" (1992) 101 Yale L.J. 1043; E. Warren, "The Untenable Case for Repeal of Chapter 11" (1992) 102 Yale L.J. 437; T. Eisenberg, "Baseline Problems in Assessing Chapter 11" (1993) 43 University of Toronto Law Journal 633; K. Kordana and E. Posner, "A Positive Theory of Chapter 11" (1999) 74 New York University Law Review 161.

The issue of remedies is a large one and the English Law Commission in its report on the registration of security interests wished to push it to the third phase of reform.[135] In its conception, the first phase would involve the introduction of notice filing for companies; the second phase would entail the extension of the notice filing system to individuals and the third and final phase would consist of a comprehensive restatement of the law of security interests including provisions on remedies. In New Zealand, it was initially proposed to leave remedies out of the P.P.S.A. but they were eventually included to avoid posssibly compromising the integrity of the statutory scheme.[136] Question marks remain, however, in New Zealand about the relationship between the P.P.S.A. and the Receiverships Act.[137] This issue of the interaction between P.P.S.A. remedies and receivership and judicial management is also of vital importance in Singapore. An unsatisfactory feature of the New Zealand P.P.S.A. is that only a secured party with priority is entitled to exercise the default remedies provided for in the legislation.[138] As leading commentators have noted: "[r]estricting the right to seize and apply collateral to the secured party with priority deprives secured parties without priority from exercising contractual rights. Personal property security legislation in other jurisdictions enables a subordinate secured party to seize and sell collateral. This is not objectionable because, even if the subordinate secured party did not pay out the prior secured party's claim from the proceeds of sale, the prior secured party is protected because the security interest is not extinguished upon the sale of the collateral."[139]

As far as Article 9 is concerned, while it contains no equivalent of privately-appointed receivership, which is the mainstay of creditor enforcement procedures in Singapore, it does contain quite extensive provisions on enforcement of security interests. Article 9-601 provides that a secured party "may reduce a claim to judgment, foreclose, or otherwise enforce the claim [or] security interest . . . by any available judicial procedure . . ." The remedies of a secured party are expressly stated to be cumulative and may be exercised simultaneously. Where the collateral includes accounts, then once

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135 Consultation Paper No. 164 on "Registration of Security Interests" (July 2002).

136 According to Professor John Farrar, "New Zealand Considers a Personal Property Security Act" [1990] Canadian Business Law Journal 328 at 330, the initial omission "was an unfortunate mistake likely to undermine totally the whole reform since the old forms will not have been decently buried and, through their remedial regimes, will be capable of ruling from their graves." Professor Farrar was a co-author of the New Zealand Law Commission Preliminary Paper No. 6, "Reform of Personal Property Security Law" (May 1988).

137 Section 106 New Zealand P.P.S.A. provides that Part 9 does not apply to a receiver but for continuing uncertainties: see Widdup and Mayne, *supra* note 3 at 307 and Gedye, *supra* note 3 at 385–386.

138 Sections 108–109 P.P.S.A.

139 See Widdup and Mayne, *supra* note 3 at 308 and for a somewhat different perspective on the effect of the relevant provisions see Gedye, *supra* note 3 at 392–397.

the debtor has defaulted on the loan, the person obligated on the accounts may be required to make payment directly to the party enforcing the security interest.[140] Of course it is not uncommon for debtor and secured party to agree that the secured party should collect the accounts even before default by the debtor and provision is made for this in Article 9-607. As we have seen, Article 9 applies both to absolute sales and the creation of security interests in accounts but the distinction, nevertheless, retains some importance. In the case of a security interest, the assignor retains an equity of redemption, *i.e.* once the loan has been discharged the assignor is entitled to the accounts back free from the security interest. In the case of a "true" sale, on the other hand, the seller of accounts has no equity of redemption. Article 9-607(c) reflects, to a certain extent, this distinction but does not mirror it entirely. The provision requires a secured party or buyer of accounts to exercise collection rights in a commercially reasonable manner if the secured party/buyer has a right of recourse against the debtor/seller. With respect to most outright sales of accounts the buyer will not have a right of recourse against the seller if the accounts do not prove as lucrative as expected and therefore, the "commercial reasonableness" standard will not apply. With some sales, however, the buyer might have a right of recourse against the seller if the accounts fail to come up to the mark and, therefore, the provision will apply.

The "commercial reasonableness" requirement applies throughout Part 6 of Article 9 and, in the context of collection of accounts, would govern things like settlement and compromise of claims against the account debtor. The use of the "reasonableness" expression is productive of a degree of uncertainly and invites litigation. Nevertheless, failure to comply with Article 9-607(c) is potentially very serious for a secured party is concerned becomes it brings into play the provisions of Article 9–625. Article 9-625 stipulates that if a secured party is not proceeding in the approved manner, a court may order or restrain collection, enforcement, or disposition of collateral on appropriate terms and conditions. Moreover, there is a liability in damages in the amount of any loss caused by a failure to comply with the statutory requirements and this includes any loss resulting from the debtor's inability to obtain, or increased costs of, alternative financing. There is a further sting in the tail for the secured creditor who is proceeding against the debtor for a deficiency in situations where the value of the realisations fall below the amount of the secured debt. In these circumstances, there is a rebuttable presumption that the amount that would have been realised had the secured party behaved in the appropriate manner is equal to the amount of the secured debt.

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[140] Article 9-607(a)(3).

Article 9 goes into considerable detail on sales by the secured party of the collateral. According to Article 9-610(b), "[e]very aspect of a disposition of collateral, including the method, manner, time, place and other terms, must be commercially reasonable. If commercially reasonable, a secured party may dispose of collateral by public or private proceedings, by one or more contracts, as a unit or in parcels, and at any time and place and on any terms." Everything is subordinated to the requirement of "commercial reasonableness" but there is a specific provision allowing the secured party to buy the collateral at a public disposition or at a private disposition "if the collateral is of a kind that is customarily sold on a recognised market or the subject of widely distributed standard price quotations."[141] The secured party is required to give properly authenticated reasonable notice of an intended disposition to the debtor and other interested parties like guarantors of the secured debt.[142] What constitutes "reasonable notice" is deemed to be a question of fact[143] but in non-consumer transactions, ten days is stated to be reasonable notice.[144]

Article 9 also attempts to provide some guidance where an apparently low price has been obtained on a disposition of collateral. Article 9-627 states that the fact that a greater amount could have been obtained by a disposition at a different time or in a different method from that selected by the secured party is not of itself sufficient to preclude the secured party from establishing that the disposition was made in a commercially reasonable manner. The provision goes on to state that the commercial reasonableness test is satisfied if the disposition is made "(1) in the usual manner on any recognised market; (2) at the price current in any recognised market at the time of disposition; or (3) otherwise in conformity with reasonable commercial practices among dealers in the type of property that was the subject of the disposition." With the overriding requirement of reasonableness, it seems clear that under Article 9 a secured creditor does not have a completely free hand when it comes to timing the disposition of collateral. Reasonableness is the name of the game and it is possible to envisage circumstances where a sale might have to be postponed so as to obtain a better price for the collateral. This is an area where there is a possible divergence between the Article 9 regime and the existing Singapore law pertaining to receivers. It is arguable that, under current law a receiver, *prima facie*, has a free hand to sell the secured property even if market conditions are very unpropitious[145] but this minimalist conception of a receiver's duties may

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[141] Article 9-610(c).

[142] Article 9-611.

[143] Article 9-612.

[144] Article 9-611(c).

[145] See generally *Kian Choon Investments (Pte.) Ltd. v. Societe Generale* [1990] 2 M.L.J. 74; *Industrial and Commerical Bank Ltd v. Li Soon Development Pte. Ltd.* [1994] 1 S.L.R. 471;

be open to reconsideration in the light of other authorities.[146] A final point worth noting is that Article 9-627(c) provides a statutory "safe harbour". A disposition which has been approved in any judicial proceeding or by any *bona fide* creditors' committee or representative of creditors is conclusively deemed to be commercially reasonable.

Such provisions are worth considering in a statutory statement of a secured creditor's remedies. The statement would also have to deal with the position where sale of the collateral by a secured party produces a surplus after the debt plus expenses have been paid off. It is the hallmark of a security interest that a creditor is not entitled to recover from the secured property more than the debt plus interest plus realisation expenses.[147] Any surplus belongs to the debtor whereas in the case of a transaction where a party retains or acquires title to an asset that party is entitled to any profit element when the asset is disposed of. Thus, in a sale of goods subject to a reservation of title clause where the buyer fails to pay the price and the seller then repossesses the goods and resells for more than the original contract price, the seller is prima facie entitled to keep the profit on the resale. While this entitlement was read down by the English Court of Appeal in *Clough Mill Ltd v. Martin*,[148] the theoretical point though is clear. If the retention of title clause is reconceptualised as being in substance a security interest then the buyer would be entitled to any surplus or profit on a resale. This result does not seem undesirable as a matter of policy and practice but the considerations are different in the case of the absolute assignment of debts. Here the buyer or factor has paid a purchase price for the debts and commercial practicality dictates that the factor should be entitled to any surplus realised from the debts as its "profit" or "turn" on the deal. Where there are clear advantages in subjecting assignments of debts to the priority and perfection rules of any new regime (greater clarity, ease in assessing risk *etc*.) the general enforcement rules cannot apply without modification.

How Seen Ghee v. Development Bank of Singapore Ltd. [1994] 1 S.L.R. 526; *Ng Mui Mui v. Indian Overseas Bank Ltd.* [1986] 1 M.L.J. 203; *Overseas Union Bank v. Chua Kok Kay* [1993] 1 S.L.R. 686.

146 *Medforth v. Blake* [2000] Ch. 86 which was accepted as correct by Lai Kew Chai J. in *Roberto Building Material Pte. Ltd. v. OCBC Ltd.* (2002, unreported at the time of writing but available on Lawnet).

147 See the classic statement by Romer L.J. in *Re George Inglefield Ltd.* [1933] 1 Ch. 1 at 28–9.

148 [1985] 1 W.L.R. 111. Robert Goff L.J. suggested that if the seller of goods chose to exercise its power under a retention of title clause to repossess goods that were worth considerably more than the outstanding debt, an implied term would prevent it repossessing and reselling more than was necessary to pay the outstanding debt. *R.V. Ward Ltd v. Bignall* [1967] 1 Q.B. 534 suggests a different result however.

XV. Conflicts of Laws

One important area that is not addressed directly in the report by the Singapore Academy of Law Sub-Committee is that of conflicts of laws as far as attachment, perfection, priority and enforcement of security interests in collateral is concerned. The issue has however particular resonance in Singapore given the open nature of the economy and the country's position as a gateway for international trade. What happens if an asset-security over which has been perfected in another jurisdiction is then brought to Singapore? In the absence of registration requirements pertaining to the asset in Singapore, a Singapore-based creditor may have no means of discovering the existence of the security interest and is consequently prejudiced. On the other hand, the foreign creditor may not know that the asset has been relocated to Singapore and would be prejudiced if registration lapses upon relocation. Legislation may provide for temporary registration for a limited period if an asset subject to a security interest that has been perfected in another jurisdiction is brought to Singapore.[149] Knowledge on the part of the foreign creditor that the asset is being moved may serve to lessen this period of temporary perfection. Legislative choices become even more difficult where a security interest has merely attached but not become perfected in the foreign jurisdiction or where the law of the foreign jurisdiction does not provide for any public act of perfection such as registration or the filing of a financing statement. Exercising legislative decision-making can be acute when the asset in question is an intangible one such as a receivable. What law governs perfection and priority *etc*.? Is it the location of the debtor or the location (*situs*) of the debt, which may be different. Does relocation of the debtor alter existing perfection arrangements? The legislature is faced with a series of difficult choices but the work done by the Hague Conference on Private International Law may ease the path of deliberation somewhat.[150]

XVI. Conclusion

Singapore has made enormous economic strides over the past few decades. That is certain. In an age of increased global insecurity what is less certain is the proper way forward. The British influence has waned in recent years and enhanced Americanisation seems to offer an alternative and attractive path to the future. This may be the case in the sphere of Credit and Security law. The British inheritance has served the country well and provided a stable base for conducting commercial transactions. Moreover, lawyers and

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[149] Section 27 New Zealand P.P.S.A. 1999.

[150] For the work of the Hague Conference see online: Hague Conference on Private International Law <http://www.hcch.net/>.

financiers are comfortable and familiar with the precepts of existing law in the Credit and Security field which is essentially the same as English law.[151] Nevertheless, the present law suffers from a degree of conceptual dysfunctionality with essentially similar transactions being treated in different ways. In addition, the law can be complex and the complexities are compounded in the determination of priorities between more than one security interest in the same item of property. The American Article 9 approach is conceptually neater and contains clearer and more rationally based priority rules. The Article 9 strategy is also gaining ground internationally with common law jurisdictions like Canada and New Zealand enacting legislation based upon its essential elements. If England follows suit, as has been recommended by the Law Commission,[152] then it may be difficult for Singapore to resist. Nevertheless, the obstacles to reform should not be underestimated. Lawyers and financiers would have to learn a whole new vocabulary with expressions like "attachment" and "perfection" taking the place of old favourites such as fixed and floating charges and crystallisation. Mindsets and traditional ways of thinking about title and property would also have to change. Given the fact that the present law works tolerably well it is easy to understand why practitioners are not in the vanguard of the reform constituency.

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[151] The distinguished Canadian commentator Professor Jacob Ziegel has also presciently remarked in "Canadian Perspectives on How Far is Article 9 Exportable?" in (1996) 27 Canadian Business Law Journal 226 at 231: "Non-banking financiers also have a vested interest in maintaining the status quo since there is a general aversion in the United Kingdom to expanding existing registration requirements to hire-purchase and conditional sale agreements and to various forms of consignment and discounting agreements for the financing of inventory and accounts receivable."

[152] English Law Commission Consultation Paper No. 164 on "Registration of Security Interests" (July 2002).