Ship mortgages in New Zealand

The conflict between the Personal Property Securities Act 1999 and the Ship Registration Act 1992

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Introduction

In the eight years since the Personal Property Securities Act 1999 (PPSA) came into force, great weight has been placed on the primacy of the Personal Property Securities Register (PPSR) as the key system in determining priority between security interests. The PPSA sets up a simple framework, allowing creditors to register their security interests in personal property and determining priority between such interests. In general, the security interests of those who fail to perfect in accordance with the Act, will be subordinate to those who do perfect.

However, the PPSA is not alone in purporting to provide an exclusive regime by which the priority of securities is to be determined. The Ship Registration Act 1992 (SRA) provides for the registration of mortgages against New Zealand registered vessels. The Act grants priority in order of registration, and provides that unregistered securities cede priority to those registered under the SRA.

This creates obvious difficulties where competing securities in the same vessel have both been registered under different Acts. The problem is partially mitigated by s23(e)(xi) of the PPSA, which excludes ships over 24m in length from the operation of the Act. However, as both the PPSA and SRA continue to apply to ships under this length, the conflict between the legislation remains prevalent. Parliament has provided no indication as to which register should prevail or as to how priority conflicts between the dual registration schemes should be resolved.

A partial solution is provided in respect of foreign registered ships, as s70 of the SRA provides that securities over such ships are to be treated as if registered under the SRA. This indicates that, where a foreign registered vessel is the subject of competing securities under the dual registration schemes, the SRA must prevail in order to give effect to s70 and to recognise New Zealand's international obligations. However, these factors are not relevant to competing securities over a New Zealand registered vessel and as such offer not guidance as to which Act should prevail.

This dissertation will examine various approaches to resolving this conflict, in order to establish a viable solution for reform. Part one explores the nature and peculiarities of maritime securities, which are unlike ordinary forms of chattel security. The conflict of laws principles, which govern ships on international waters and in foreign jurisdictions, also prove important due to the inclusion of foreign registered ships within the two conflicting regimes.

The writing then goes on to examine ship registration and the operation of the New Zealand SRA, with particular regard to the objects of s70, before outlining the relevant provisions of the PPSA. The conflict between the legislation is then analysed in greater depth.

Part two seeks to shed light on which Act should be afforded priority. This part looks first to international law in an effort to elucidate policy considerations that may be persuasive in deciding which Act should prevail. Both international conventions and similar conflicts between legislation in other jurisdictions form the subject of analysis. The section then goes on to examine New Zealand's domestic law. Guidance is sought from the law governing aircraft securities, which share many similarities with maritime securities, as well as a recent High Court decision which directly addresses the conflict between the two Acts.

Finally, part three considers options for legislative reform. The section outlines four options for reform and comments on their desirability at a policy level, analysing their effect on the objects and purpose of both the PPSA and the SRA. The possible solution of dovetailing the Acts, whereby the PPSA operates as a fallback regime, is considered in greater depth. Ultimately, it is determined that a modified version of this solution presents the best option for reform, as it allows the SRA to prevail with regard to registered vessels, while providing a means of registering securities in unregistered vessels by way of the PPSA.

PART I: MARITIME SECURITIES AND THE PPSA

1. Maritime Securities Law

1.1 Maritime Securities

The origins of international maritime law can roughly be traced back to the laws of Oleron, a small island off the mouth of the Charente in the Bay of Biscay. These laws formed the basis of English admiralty law, which has contributed significantly to the development of international maritime law. The laws of Oleron, dating back to at least 1266, expressly acknowledged the possibility that a master of a vessel could pledge his ship to a lender in return for an advance.[1] Thus, maritime securities have been prevalent from the very conception of maritime law, and continue to play a vital role in the shipping world today.

Maritime securities have always been problematic as ships frequently move between jurisdictions and thus require special rules to prevent them falling subject to the laws of these jurisdictions. Furthermore, they spend much time traveling over international waters, which do not fall subject to the laws of any particular jurisdiction. As the validity and ranking of maritime securities varies between jurisdictions, the system of law governing a particular security interest is of the utmost importance.[2]

There are five basic types of claim that a ship may become subject to. As a general rule, the five categories of claim are ranked in the order set out below. The area of contention that exists relates to the recognition and priority given to claims within each category, rather than the ranking of the categories themselves.[3]

(i) Special legislative rights

Special legislative rights often give rights of detention or possession, and are usually given first priority. These rights are for the benefit of the state or state corporations,

[1] P R Wood *Comparative Law of Securities and Guarantees* (Sweet & Maxwell, 1995) 119.
[2] W Tetley *International Conflict of Laws* (International Shipping Publications, 1994) 537.
[3] Above n 2, 539.

and usually relate to outstanding dock, harbour and canal expenses, wreck removal, pollution or narcotics offences.[4]

(ii) Costs of arrest, judicial sale and custodia legis

Second in priority are court costs, which include the costs of court ordered arrest, judicial sale and custodia legis (the costs incurred while keeping the ship in custody for the period after its arrest and before its sale).[5]

(iii) Maritime liens

Next in priority are maritime liens, which follow in third position.[6] Maritime liens are extraordinary legal creatures, distinct from ordinary security interests. Claims giving rise to a maritime lien include: claims to seamen's, salvage, collision (tort) and, in rare cases, masters' disbursements. Bottomry and respondentia[7], also traditional maritime liens, are now virtually obsolete.[8]

Although this dissertation is primarily concerned with registered securities and mortgages, an awareness of the existence and operation of maritime liens is necessary.

Maritime liens are secret in that they do not usually have to be registered and their existence does not depend upon possession. In contrast to normal priority principles, maritime liens often rank in the inverse order of their creation. They are also indelible in that they cling to a ship, even if it is bought by a purchaser with no notice of the lien. They will, however, be terminated by a judicial sale.

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[4] Above n 2, 538.
[5] Above n 2, 538 - 539.
[6] Above n 2, 539.
[7] Bottomry was a primitive form of ship mortgage, whereby the master pledged his ship (its "bottom" and keel) for a loan, by way of "bottomry bond". Respondenia was the similar pledging of the cargo. These proved useful before the growth of modern methods of communication, as they allowed the master to raise the funds needed to purchase goods and services required to complete the voyage.
[8] W Tetley *International Maritime & Admiralty Law* (Les Editions Yvon Blais Inc, 2002) 482. See also the authoritative English list of traditional maritime liens enunciated in *The Ripon City* [1897] P. 226, 242, which include: "bottomry, salvage, wages, masters' wages, disbursements and liabilities, and damage."

(iv) Ship mortgages

Most jurisdictions operate a ships register, recording title to vessels and allowing for the registration of mortgages in respect of registered vessels. Where a ship mortgage is registered in this way, it obtains the status of a 'preferred statutory ship mortgage' or 'legal mortgage'. These interests will usually rank fourth in priority.[9] An unregistered mortgage remains enforceable as an equitable mortgage, but cedes priority to all registered mortgages.[10]

(v) Contract liens

Contract liens are rights against the ship arising from contracts for the supply of goods and services to the vessel. These rights are granted to: suppliers of necessaries, repairmen, stevedores, and tug operators.[11] In the United Kingdom and Commonwealth countries, contract liens give rise to a "statutory right *in rem*", which arises only at the time of the ship's arrest, rather than the time the services are rendered or the damage incurred. Statutory rights *in rem* rank behind registered mortgages.[12] However, it should be noted that, in the United States many contract liens are afforded the status of true maritime liens.[13]

This writing will focus mainly on ship mortgages, as seen in category four. However, it is necessary to bear in mind the existence of other types of claim, ranking both above and below ship mortgages.

1.2 Conflict of Laws

Two major conflict of laws problems arise in respect of maritime securities. There is also the preliminary issue of jurisdiction, regarding the court's ability to permit the arrest of the vessel and to hear the case. However, this is not of particular importance for present purposes. The first key issue is recognition of the security. What law should be applied

[9] Above n 2, 539.
[10] C Hill *Maritime Law* (5th ed, LLP, 1998) 30-31.
[11] W Tetley *International Maritime & Admiralty Law* (Les Editions Yvon Blais Inc, 2002) 482.
[12] For a discussion of the comparisons between true maritime liens and statutory rights *in rem*, see D C Jackson *Enforcement of Maritime Claims* (3rd ed, LLP, 2000) paras 18.13-18.14.
[13] Above n 11, 491.

to determine the validity of a foreign security; and should a court recognise a foreign security that would not be recognised under the law of the forum (*lex fori*)? The second problem is ranking of securities. Which law should determine the priority afforded to the various security interests?[14]

Ordinarily, securities over chattels are governed by the *lex situs* (the law of the country where the chattel is situated at the time the security is created).[15] Dicey's Rule 120(3) states that a chattel's *situs* is the country where that chattel it is situated at any given time.[16] This principle is clearly inappropriate with regard to ships, due to the fluidity of the *lex situs* where a ship moves frequently between jurisdictions. Furthermore, the craft may be on international waters at the time the security is created.[17] As a result, different conflict of laws principles have developed in relation to maritime securities, based largely on ship registration. Thus, there exists an exception to Rule 120 in the case of ships: vessels are sometimes deemed situate at their port of registry.[18]

Where a ship is on international waters, the principle of 'the freedom of the high seas' will apply. This principle is "one of the longest and best established principles of international law"[19] and includes the freedom of navigation, fishing, laying of submarine cables and pipelines and overflight.[20] The principle requires that ships on the high seas fall under the exclusive jurisdiction of the flag State.[21] This proposition is affirmed in article 92 of the 1982 United Nations Convention on the Law of the Sea (UNCLOS), to which New Zealand is a signatory. Article 87(2) requires that the freedoms of the high seas be exercised by all states with due regard for the interests of other states in their exercise of the freedoms.

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[14] Above n 2, 542 - 543.
[15] Above n 1, 183.
[16] L Collins (Ed) *Dicey, Morris and Collins on The Conflict of Laws* (14th ed, Sweet & Maxwell, 2006) 1116.
[17] Above n 11, 258.
[18] Above n 16, 1130.
[19] *Sellers v Maritime Safety Inspector* [1999] 2 NZLR 46
[20] P D O'Connell *The International Law of the Sea* (Clarendon Press, 1984) 798. Article 2 of the 1958 High Seas Convention listed these four freedoms as examples of high seas freedoms. The 1982 Law of the Sea Convention has further added to this non-exhaustive list.
[21] R R Churchill & A V Lowe *The Law of the Sea* (3rd ed, Manchester University Press, 1999) 208.

This principle extends only to vessels on the "high seas": parts of the sea that are not included in a State's exclusive economic zone, territorial sea, internal waters, or archipelagic waters.[22] Thus, securities created while a vessel is on the high seas will be governed by the law of the state of registration ("the law of the flag"). But what of ships that have entered a foreign jurisdiction?

Ordinarily, where a vessel enters the waters of another state, the artificial *situs* (the state of registration) is displaced by the actual *situs*.[23] This rule is effective with regard to some forms of maritime security, particularly maritime liens. This is because their validity is normally governed by the law of the place where the lien was created, although some jurisdictions[24] refuse to recognise liens that would not exist under the *lex fori* (the law of the forum). It should be noted, however, that the priority of such securities will usually be determined according to the *lex fori*.[25]

This is in stark contrast to ship mortgages, which remain subject to the laws of the state of registration.[26] A statutory ship's mortgage comes into existence by virtue of registration in accordance with the relevant legislation of the flag state. While most states operate statutory ship registration regimes (under which mortgages are also registered), this legislation usually applies only to ships owned within the particular jurisdiction. It would therefore be anomalous to apply either the *lex fori* or the law of the actual *situs,* as opposed to the artificial *situs* (the flag state), as the laws of these jurisdictions would not apply to the foreign ship. Even where the laws of a jurisdiction do purport to provide for foreign ships, it would introduce an unwarranted element of arbitrariness if the proper law to be applied was dependent on the chance location of the

[22] 1982 United Nations Convention on the Law of the Sea, Article 86.
[23] *Trustees Executors and Agency Co Ltd v IRC* [1973] Ch. 254, 263.
[24] Jurisdictions such as the United Kingdom, South Africa and Cyprus have all refused to recognize foreign liens that were dissimilar to liens recognised in their jurisdiction. (*The Halcyon Isle, (Bankers Trust v Todd Shipyarts)* [1981] AC 221, 235; *Transol Bunker BV v Andrico Unity* 1989 (4) SA 325, 354; *Hassanein v The Hellenic Island* [1989] 1 CLR 406.)
[25] Above n 2, 548 – 551.
[26] Above n 2, 548 – 551.

ship within a particular port of registry.[27] As a result, there has developed a general rule that the validity and priority of mortgages are therefore determined by flag law.[28]

However, it should be emphasised that conflict of laws issues regarding maritime securities are inherently uncertain, and the approach taken varies considerably between jurisdictions. This is particularly the case with regard to maritime liens. Fortunately, the position of ship mortgages is somewhat more certain, and there has been greater uniformity of approach between jurisdictions.

As the present focus is on ship mortgages, it is sufficient to note that validity and priority should, *in theory*, be determined by the law of the state of registration. This approach is justified either by the principle of the freedom of the high seas (where a ship is on the high seas at the time security is created) or by the general rule that flag law should govern ship mortgages (where a vessel has entered the waters of another jurisdiction). However, as will be seen, these principles are not always applied in practice.

[27] *Tisand Ltd v Owners of the Ship MV Cape Moreton* [2005] FCAFC 68, [146]-[148].
[28] M Davies & A Dickey *Shipping Law* (3rd ed, Lawbook Co., 2004) 132; D C Jackson *Enforcement of Maritime Claims* (LLP, 1985) 343; G Bowtle & K McGuiness *The Law of Ship Mortgages* (LLP, 2001) para 7.88; *The Angel Bell* [1979] 2 Lloyd's Rep 491, 495; *The Byzantion* (1922) 12 Llyod's LR 9.

2. Ship Registration

2.1 Ship registration generally

Most nations provide a system of registration for ships flying their flag, due to their national importance in terms of defence and employment. Such registration schemes perform the important function of conferring jurisdiction on the state of registration and enhance the ability to finance the vessel through a system of registered mortgages. Common consequences of title registration include:

- jurisdiction is conferred on the flag state of the ship;
- the flag state is obliged to accept international obligations for the ship;
- diplomatic protection afforded by the flag state to its nationals is conferred on the ship;
- registration may be evidence of title, though in many states such evidence is not conclusive. [29]

In order to avoid the expense and inconvenience of overcrowding the register with small vessels, many jurisdictions limit registration of ships to those over a certain size. Most states base registration upon the nationality of the owner, and prohibit registration of foreign owned vessels. Thus, a ship's country of flag and country of registration are generally coincident. However, "open register" states (such as Liberia, Cost Rica, Honduras, Uruguay, Vanuatu, Bahamas and Hong Kong), accept the registration of foreign owned ships, giving rise to flags of convenience.[30]

At present, around 40 percent of the world's international fleet sail under flags of convenience[31], despite the requirement in most international conventions of a "genuine link" and "control" by the flag state.[32] The prevalence of flags of convenience and 'flag

[29] Above n 1, 203-204.
[30] Above n 1, 204 - 205.
[31] Above n 2, 583.
[32] See the 1958 Geneva Convention on the High Seas, the 1982 Law of the Sea Convention and the 1986 Registration of Ships Convention.

shopping' has lead to dissatisfaction with the principle of the exclusive jurisdiction of the flag state. Many academics now argue for a proper law approach to maritime securities, whereby the law with the closest and most real connection would apply.[33] This is an issue that may prove significant in resolving the conflict between New Zealand's legislation, and will be examined further in chapter six.

2.2 Ship registration in New Zealand

Ship registration in New Zealand was originally governed by the Merchant Shipping Act 1894 - a UK statute providing a system of ship registration for the UK, its dominions and colonies. This Act was replaced by the Shipping and Seamen Act 1952, which set up the modern day New Zealand register of ships. The ship registration provisions of the Act were then replaced by the Ship Registration Act 1992 (SRA), which currently governs ship registration in New Zealand.[34]

The Act applies to all New Zealand owned ships and ships on demise charter to New Zealand based operators. It establishes a register which is divided into Parts A and B. Registration under Part A confers nationality on a ship, is evidence of title, and allows for the registration of mortgages. Registration under Part B confers nationality only.

The Act draws a distinction between ships under 24m in register length, and those that are larger. This is a common size division, frequently used to distinguish ships that are more likely to enter international waters from those that are not.[35] It is compulsory for ships 24m and over to be registered under Part A. However, there is an exception in the case of pleasure vessels, ships engaged solely on inland waters of New Zealand, barges that do not proceed on voyages beyond coastal waters and certain other ships exempted by the Director of Maritime New Zealand.[36] These ships over 24m, which are excluded

[33] Above n 2, 586 - 587.
[34] The relevant provisions of the Shipping and Seamen Act 1952 (ss382-444) were repealed by s88(1) of the SRA.
[35] See for example Australia's Shipping Registration Act 1981 and the UK's Merchant Shipping Act 1995, both of which implement the 24m length distinction.
[36] SRA, s6(1).

from the mandatory registration requirement, as well as all ships under 24m, are still entitled to register under Part A at the option of the owner.[37]

Registration under Part B is limited to pleasure vessels and ships under 24m in length. Part B registration is optional.[38] However, where a pleasure vessel or ship under 24m proceeds on an overseas voyage, it must be registered on either Part A or B.[39]

Registration under Part A

Part A	**<24m register length**	**> 24m register length**
Required to be registered	New Zealand owned ships (including pleasure vessels of any size) that proceed on an overseas voyage. However, these ships can be registered in Part B, rather than Part A, at the owner's option.	All New Zealand owned ships, except: pleasure vessels, ships engaged solely on New Zealand inland waters, barges used solely for voyages on coastal waters.
Permitted to be registered	New Zealand owned ships and other ships on demise charters to New Zealand based operators.	Pleasure vessels, ships engaged solely on New Zealand inland waters, barges used solely for voyages on coastal waters.

The result is that almost any New Zealand owned ship, regardless of size, may be registered on Part A and have statutory ship mortgages registered in respect of it. Registered mortgages take priority over unregistered mortgages, and rank in order of registration.[40]

2.3 Foreign registered ships

Mortgages over foreign registered ships cannot be registered under the SRA. However, s70 provides that:

> Where a question arises in New Zealand as to the priority of instruments creating securities or charges in respect of a ship registered under the law of a foreign country, instruments

[37] SRA, s8(1).
[38] SRA, s8(2).
[39] SRA, s6(2).
[40] SRA, s40(1).

creating securities or charges in respect of the ship and duly registered in respect of the ship under that law shall –

(a) Have the same effect as a mortgage registered in respect of a ship under this Act; and

(b) Be accorded the priority that they would have been accorded if they had been registered under this Act.

This section was enacted in response to the widely criticised Court of Appeal decision in *The "Betty Ott"*[41] which was decided under the old Shipping and Seaman Act 1952. The case involved competing claims between an Australian registered mortgage and a later New Zealand debenture registered under the Companies Act, in respect of an Australian registered vessel.

Following the Privy Council's majority decision in *The Halcyon Isle*[42], the court held that priority between the securities was to be determined under New Zealand law. The Australian registered mortgage could not be recognised as equivalent to a New Zealand mortgage, as the mortgage was not registered in New Zealand (and thus not of a type recognised under New Zealand law). As a result, the later debenture was afforded priority over the Australian mortgage which was treated as unregistered and therefore equitable.

This "startling and narrow conclusion"[43] had far reaching implications for ship financiers, potentially depriving the holders of registered mortgages of adequate security in all jurisdictions apart from that in which the ship was registered.[44] It was, therefore, put to the select committee examining the Ship Registration Bill, that the 1992 Act should include a provision clarifying the proper status and legal effect of registered foreign ship mortgages.[45] The result was the inclusion of s70 when the SRA was enacted.

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[41] *The Ship "Betty Ott" v General Bills Ltd* [1992] 1 NZLR 655.
[42] *The Halcyon Isle, (Bankers Trust v Todd Shipyarts)* [1981] AC 221. In that case, the Privy Council classified a maritime lien as a remedy and therefore a matter of procedure, to be determined by the *lex fori.* For a thorough analysis of this decision, see P Myburgh "Recognition & Priority of Foreign Ship Mortgages: *The Betty Ott*" (1992) LMCLQ 155.
[43] D C Jackson *The Enforcement of Maritime Claims* (4th ed, LLP, 2005), para 23.89.
[44] P Myburgh "Recognition & Priority of Foreign Ship Mortgages: *The Betty Ott*" (1992) LMCLQ 155, 158.
[45] See P Myburgh "Submission to the Communication and Road Safety Select Committee" 5-7.

Although the *The Halcyon Isle* decision has not been overruled, and therefore remains as good authority, the general consensus is that, as the decision related to maritime liens, the Privy Council's reasoning should not extend to cases involving ship mortgages[46]. Even in England, the position remains that the validity and priority of ship mortgages are governed by the state of registration, although the priority of competing interests other than mortgages are determined in accordance with the *lex fori*.[47] Consequently, there has been no call for the legislatures in other jurisdictions to enact similar provisions to s70, which therefore remains unique to New Zealand.

This section has been criticised due to its failure to recognise the different priority status of various maritime claims. All claims arising from foreign registered securities or charges, which could conceivably include a diverse range of interests (such as registered contractual liens, preferred ship mortgages and debentures), are lumped together and treated as a registered mortgage. In failing to give effect to these securities' priority status under flag law, s70 effectively skews the nature of the foreign right. In this regard, s70 runs contrary to the well recognised principle that choice of law rules should not distort the nature of foreign rights. [48]

This point, relevant to the discussion of foreign rights with regard to New Zealand's international obligations, is examined later in this writing. For present purposes, it is sufficient to note that the SRA provides for the registration of ship mortgages over New Zealand ships of any size (provided they are registered on Part A), and treats foreign registered securities as identical to New Zealand registered mortgages. Furthermore, it purports to provide an exclusive and complete regime for determining priority between competing mortgages. However, this notion does not sit well with the Personal Property Securities Act 1999.

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[46] The majority in the *Halcyon Isle* saw the issue of recognition of foreign maritime liens as procedural or remedial, rather than substantive. The case can be distinguished with regard to ship mortgages, which, as the Privy Council itself acknowledged, create an "immediate right of property". As a result, ship mortgages, as substantive rights, should fall to be governed by the *lex situs*.
[47] G Bowtle & K McGuiness *The Law of Ship Mortgages* (LLP, 2001), para 7.88.
[48] P Myburgh "The New Zealand Ship Registration Act 1992" (1993) LMCLQ 444, 450.

3. Personal Property Securities Law

3.1 The Personal Property Securities Act (PPSA)

The New Zealand PPSA came into force on 1 May 2002, replacing the previous mixture of common law, equity and various specialised statutes "bristling with inconsistencies and contradictory or outmoded policies".[49] The PPSA established a single system which sought to achieve simplicity, clarity, transparency and certainty in application.[50]

The Act, which is based on the equivalent Canadian and US legislation, has revolutionised New Zealand's securities law, shifting the focus to the substance of a transaction, rather than its legal form, when determining whether a security interest has arisen. As such, traditional concepts of ownership have been rejected in favour of the PPSA rules and registration requirements.[51]

3.2 How the Act works

The Act establishes a Personal Property Security Register (the PPSR) allowing for the registration of security interests. Unlike the asset based system of registration under the SRA, which provides for the registration of title to vessels, the PPSR is based on the identity of the debtor granting security over the asset. This is due to the instability of most personal property, which is often indistinguishable from other items of the same type and easily moved, created or destroyed. As such, an asset based system of registration is inappropriate. However, ships, being items of great value, justify the additional requirements necessary to enable an asset based system of registration.[52]

Rather than recording all goods and details of ownership within the jurisdiction, the PPSR provides notice that a particular debtor has granted a security interest in a particular

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[49] S A Riesenfield *The Quagmire of Chattels Security in New Zealand* Occasional Pamphlet No. 4 (Legal Research Foundation of New Zealand, 1970), 15.
[50] B Allan *Guidebook to New Zealand Personal Property Securities Law* (CCH, 2002) 1.
[51] Above n 48, 2
[52] J Farrar & M O'Regan *Reform of Personal Property Security Law: A Report to the Law Commission* Preliminary Paper No. 6 (NZLC, 1988), 12.

item or class of personal property.[53] The PPSR is indexed primarily by debtor name, but in the case of cars and aircraft (provided they are not inventory), which are uniquely identifiable, the register may be searched on the basis of serial or registration number.

The Act provides priority rules for competing security interests in secured property. There is great incentive to register interests under the Act as unperfected securities rank behind those perfected in accordance with the Act, leaving unregistered interests unprotected. In order to perfect a security under the Act, the interest must qualify as a security interest under s17, which gives the following definition:

> **17 Meaning of "security interest"**
>
> (1) In this Act, Unless the context otherwise requires, the term **security interest –**
>
> (a) Means an interest in personal property created or provided for by a transaction that in substance secures payment or performance of an obligation without regard to –
>
> (i) The form of the transaction
>
> (ii) The identity of the person who has title to the collateral

Section 41 specifies two preconditions to the perfection of such security interests. The first requirement is attachment, which occurs when the secured party has given value, the debtor has obtained rights in the collateral, and the security agreement is enforceable under against third parties under s36.[54] Secondly, the secured party must have either registered a financing statement or taken possession of the collateral. While there are some exceptions to this which apply to limited types of secured property, these are not important for present purposes.

A perfected security is not necessarily guaranteed first priority, nor is it enforceable against all others. However, it will take priority over all unperfected interests.[55]

[53] M Gedye, R Cuming & R J Wood, *Personal Property Securities in New Zealand* (Brookers, 2002), 1.
[54] Personal Property Securities Act 1999, s40.
[55] Personal Property Securities Act 1999, s66(a).

3.3 Excluded transactions

The general effect of the PPSA is that any transaction qualifying as a security interest under s17 falls to be governed by the Act, unless it is of a type expressly excluded in s23. Section 23 establishes exceptions for various forms of property that would ordinarily fall subject to the PPSA, but are already governed by alternative regimes, providing their own priority rules. Security interests in fishing quotas and radio communication licenses are examples of such exclusions. There is also an exception in the case of certain ships:

> **23 When Act does not apply**
>
> This Act does not apply to –
>
> (e) An interest created or provided for by any of the following transactions:
>
> (xi) A transfer, assignment, mortgage or assignment of a mortgage of a ship (within the meaning of the Ship Registration Act 1992) that exceeds 24 meters register length (within the meaning of that Act), or any share in such a ship.

Clearly Parliament was seeking to exclude certain security interests in ships from the operation of the PPSA, and prevent any overlap between the parallel registration systems under the PPSA and the SRA. However, s23(e)(xi) does a poor job of achieving this. It would appear that Parliament intended for the Acts to dovetail, allowing the SRA to govern certain interests in ships registered on Part A, and leaving the PPSA to govern all other interests, thereby giving primacy to the specific register (the SRA) over the general PPSA register. However, the use of the 24m length distinction as the criterion determining the applicability of the legislation causes unnecessary ambiguities and creates overlap between the registration schemes.[56]

[56] A Tetley "Security Interests in Ships and Aircraft" (2006) NZLRev 689, 707.

4. Conflict Between the PPSA & the SRA

4.1 Problems with s23(e)(xi)

As it currently stands, s23(e)(xi) creates a number of difficulties:

1. The first and most important issue for the purposes of this writing is that ships under 24m (and therefore falling outside the s23(e)(xi) exclusion) potentially fall subject to both registration regimes. Where such a ship is optionally registered on Part A, a mortgage in respect of it may be registered under either the PPSA or the SRA. This creates obvious difficulties where competing securities are registered on different registers, raising the question of which Act should prevail? Each Act sees itself as the superior legislation, and purports to take priority over other Acts. The legislation itself, therefore, offers little guidance as to which Act should apply to determine issues of priority.

   Arguably, the fact that s23(e)(xi) fails to exclude ships under 24m indicates that the PPSA was intended to govern mortgages, transfers and assignments of such ships. However, this interpretation would frustrate the purpose of having two ship registers under the SRA, by eliminating the advantages of registration under Part A (evidence of title and the ability to register statutory mortgages against that title).[57] The reality is that Parliament has left open two registers in respect of ships under 24m, and failed to provide any mechanism for determining priority conflicts occurring when both registers are used.[58]

2. A similar problem arises with regard to foreign registered securities in foreign ships under 24m. Should a PPSA registered security take priority over a foreign registered mortgage, which by virtue of s70 is treated as if registered under the SRA? This poses essentially the same question outlined above, as to which Act should prevail, but with the additional consideration of New Zealand's international obligations with regard to foreign registered ships. Arguably, the

[57] Above n 56, 708.
[58] B Allan "Securities on ships: which channel?" (2007) NZLJ 94, 96.

need to recognise foreign registered mortgages in such ships justifies granting primacy to the SRA. It is possible that these notions of international comity may prove less persuasive in relation to foreign registered charges, which are of a lesser status than foreign registered mortgages. However, by their inclusion in s70, it would appear that Parliament intended to elevate charges to the same standing as mortgages and offer them equivalent protection.[59]

Allowing the PPSA to prevail would undoubtedly undermine the purpose and effect of s70, risking the resurgence of decisions in the vein of *The Betty Ott*. It is therefore submitted that the SRA should prevail in cases of foreign securities falling within s70.

An alternative solution would be to adopt the modern view that *The Halcyon Isle* does not apply to statutory ship mortgages. On this approach, courts would be free to determine priority in accordance with flag law, giving due recognition to the foreign security, without being required to read down the PPSA through a strained interpretation of s23(e)(xi).

However, there is presently no indication that New Zealand courts would be inclined to adopt this interpretation of *The Halcyon Isle* or to apply flag law in preference to s70. Rather than viewing s70 as a backstop measure to prevent obscure results, s70 has been seen as providing the sole means for determining the priority of mortgages over foreign ships, thus preventing the application of flag law.[60]

Thus, it would seem that the SRA should prevail in such cases. However, this does not justify the conclusion that the SRA should take precedence with regard to New Zealand registered ships, as there is no foreign element in such cases.

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[59] Above n 56, 709.

[60] See for example the decision in *KeyBank National Association v The Ship "Blaze"* (HC Auckland, CIV 2006-404-2266, 9 February 2007, Baragwanath J) where his Honour attributes the utmost importance to the principle of the exclusive jurisdiction of the flag state, yet applies s70 as opposed to flag law.

3. Further difficulties arise in relation to ships over 24m that are not registered on Part A. Such vessels include pleasure vessels, ships engages solely on inland waters that are over 24m where the owner elects not to register on Part A (as there is no compulsory registration of pleasure vessels), as well as ships over 24m owned by non-New Zealand nationals (for example, a permanent resident) that are therefore not entitled to registration on Part A. Section 23(e)(xi) clearly excludes these ships from the operation of the PPSA, and the absence of Part A registration prevents the registration of ship mortgages under the SRA. Thus, neither Act caters for the registration of mortgages over such vessels. This would appear to necessitate the revival of the old common law and equitable principles governing security interests.[61]

4. Finally, the infrequent cases of ships previously under 24m that are extended to over 24m in length raise additional problems. Should the PPSA continue to apply to mortgages registered before the extensions? The answer would appear to be yes, in order to avoid subordinating the PPSA security to prior unregistered securities. What then of a later mortgage registered under the SRA? This again gives rise to the problems of dual registration schemes alluded to in 1 above.

These examples clearly illustrate the difficulties created by the current drafting of s23(e)(xi). It is submitted that the judicial approach to the problems outlined in 2 & 3 should be fairly clear cut. Where a foreign registered ship is involved, the policy underlying s70 will dictate that the SRA must prevail or alternatively that flag law must be applied. Where the situation in 3 arises, it would seem that courts will have little choice but to apply the old common law. While these outcomes are not necessarily desirable and require legislative intervention, in both cases it is at least possible to justify the outcome with reference to the wording and policy of the legislation itself. This is in stark contrast to the situations in 1 & 4, where there appears to be no logical reason for granting primacy to one Act over the other.

[61] Above n 56, 707-708.

The remainder of this writing will examine possible judicial and legislative solutions to this issue. The problems arising in 2 & 3 are also relevant with regard to options for legislative reform. How a Court should resolve each of the aforementioned situations ultimately depends on which Act should be afforded priority.

PART II: WHICH ACT SHOULD PREVAIL?

5. International Guidance

A number of sources potentially offer guidance as to which Act should be afforded priority. This chapter will look first at international conventions governing maritime securities as both the principles and content of these conventions, as well as their respective success, may influence the importance that is to be placed on the provisions of the Acts. The chapter will then go on to examine how this issue has been resolved in other jurisdictions with similar or identical legislation to our own.

5.1 Current international conventions

In resolving the conflict between the two Acts, guidance may be sought from international conventions that New Zealand has, or is likely, to ratify. Equally, the reasons underlying our failure to ratify a particular convention may indicate policy concerns that can be applied in the present case. It is also necessary to examine the likely future position of maritime securities internationally. The direction that maritime law is headed internationally, as well as the emergence of new conventions, could provide persuasive reasons for choosing one Act over the other.

There have been numerous international conventions relating specifically to maritime securities that have sought to consolidate and unify the law internationally. As Goode points out, the law in this area is in a state of disarray, due to the lack of any uniform substantive law rules, or even uniform conflict of laws rules governing maritime securities.[62] Arguably, the best solution to this situation would be to create a cohesive system of internationally recognised law, through an international convention. Yet despite numerous attempts by both the Comite Maritime International (CMI)[63] and the

[62] R Goode "Battening down your security interest" (2000) LMCLQ 161, 162.
[63] The CMI is based in Belgium and was formally established in 1897, with the primary objective of unifying maritime laws. It is the oldest international organisation in the maritime world.

International Maritime Organisation (IMO)[64], international maritime conventions on security interests have proved unsuccessful. This is due, largely, to the reluctance of countries to deviate from their deeply entrenched traditional approaches to priorities between competing securities – approaches that inevitably vary between different jurisdictions! Common law countries that have inherited English admiralty practices have proved particularly inflexible, and as a result, most conventions have found favour in civil law countries only.[65]

Of the three[66] major conventions in this area, the first was ratified by civil law counties only; the second attracted insufficient support and never came into force; and the third was only slightly more successful, taking an 11 year period to acquire the requisite support of 10 ratifications necessary for the convention to come into force.[67] New Zealand is not a signatory to any of these. All three conventions provide for mortgages and charges registered in accordance with the law of a ship's flag to be taken as valid and upheld. They also define categories of maritime lien and provide for the ranking of various claims.[68] Although the specificity with regard to the types of claim that will qualify as a maritime lien was necessary to bridge the divergence between jurisdictions, the reluctance of many countries to relinquish their traditional approach to maritime liens has hampered the success of these conventions.[69]

Thus, New Zealand is not alone in its choice not to ratify any of the three international conventions. The effect of this decision is that our law on ship mortgages remains uninfluenced by these conventions, and more importantly, these conventions therefore offer little guidance as to which Act should prevail.

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[64] The IMO is a specialised agency of the United Nations, primarily concerned with the safety and security of international shipping.
[65] Above n 56, 691
[66] Three international conventions have been developed in this area. The first was the 1926 Brussels Convention on Maritime Liens and Mortgages. A modified version of this convention, based on the same framework, formed the second convention: the 1967 Brussels Convention on Maritime Liens and Mortgages. This convention never came into force. The third convention, the 1993 Geneva Convention on Maritime Liens and Mortgages finally came into force in September 2004.
[67] Above n 56, 691-694.
[68] Above n 56, 694.
[69] Above n 56, 691-692.

5.2 Conventions in the future

Is there any prospect of a new and more successful convention impacting on New Zealand's domestic law? The answer can be found by examining the law relating to aircraft securities.

Aircraft are similar to ships in that they are also ambulatory chattels, frequently moving between jurisdictions. Aircraft financing techniques and documentation are also similar to ship mortgages, although aircraft are often financed by financial leases as opposed to mortgages due to the wider availability of tax incentives.[70] However, the conflict of laws problems, seen with regard to maritime securities, are less prevalent in relation to aircraft. This is due to the success of international conventions on aircraft securities.

Right from the outset, the aviation community sought to devise an internationally acceptable form of international charge, recognised by treaty and grafted onto national laws.[71] While this was not achieved by the 1948 Geneva Convention, the 2001 Convention on International Interests in Mobile Equipment ("the 2001 Cape Town Convention") finally brought this goal to fruition, putting in place an effective system of international protection for securities over aircraft. Rather than attempting to harmonise disparate domestic laws, the 2001 Cape Town Convention was drafted to meet a particular commercial problem. It established a single international register for security interests, accessible over the internet, with relatively straight forward priority rules designed to protect international interests in the event of debtor insolvency.[72]

The 2001 Cape Town Convention, which has been described as "the most ambitious problem solving convention to date",[73] has now been ratified by fourteen countries.[74]
While ships were originally included within the ambit of the convention, they were removed after strong objections from maritime organizations throughout the shipping

[70] Above n 1, 200.
[71] Wilberforce "The International Recognition of Rights in Aircraft" (1948) 2 Int'l LQ 421, 423.
[72] Above n 56, 697-699.
[73] Goode, "Rule, Practice and Pragmatism in Transnational Commercial Law" (2005) 54 ICLQ 539, 557.
[74] Above n 56, 698.

world. Securities over ships were already adequately catered for – or so it was said – by the systems currently in place.[75]

The success of this convention and its adoption by the air world, compared with the lukewarm reception of international conventions in the maritime world, is largely due to the impetus of the Aviation Working Group (Boing/Airbus) and the favourable finance terms available to airlines located in countries that have ratified the convention.[76] Unlike ships, one-plane companies are uncommon, and many airline companies are owned by governments.[77] Thus, ratification of international aircraft conventions has been assisted by this corporate influence.

It would seem that similar financial incentives in key ship building countries will be required if international maritime conventions in matters of security interests are to succeed in the shipping world.[78] Until this happens, the law in this area looks set to remain unchanged. Thus, there is nothing on the international horizon that could conceivably affect New Zealand's maritime securities laws and perhaps indicate that primacy should be afforded to one Act in preference to the other.

5.3 The approach in other jurisdictions

A number of conflicts between shipping legislation and personal property securities regimes have arisen in other jurisdictions. Similarly, both shipping and securities legislation often conflict with rules and registration regimes under other Acts (most commonly Companies Acts). It was hoped that decisions addressing these instances of conflict would contain valuable discussion on the merits of granting priority to one Act over the other, shedding light on the approach to be taken by New Zealand courts. Unfortunately, the relevant decisions have mostly been based on federal rules and constitutional principles, which do not apply in New Zealand and therefore offer little guidance.

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[75] Above n 56, 711. See also the CMI Newsletter, No 2 (May/August 2001) 9-10.
[76] Above n 56, 712. For example, Ex-Im Bank (the official export credit agency of the United States) currently offers a one-third reduction on its risk premium/exposure fee for such airlines.
[77] Above n 1, 200.
[78] Above n 56, 712.

In Western Australia, a ship mortgage registerable under the Shipping Registration Act 1981 also constitutes a "security" within the meaning of the definition of "bill of sale" under s5 of the Bills of Sale Act 1899 (WA). The Bills of Sale Act requires registration of chattel mortgages if they are to be enforceable against third parties. However, the SRA purports to provide an exclusive regime for the registration of ship mortgages, conferring rights against the debtor, as well as third parties. The question therefore arises as to whether registration under both Acts is required, or whether one Act should be afforded priority. This issue is resolved by s109 of the Commonwealth Constitution that requires inconsistencies between state and commonwealth legislation to be resolved in favour of the commonwealth Act. As the Bills of Sale Act is state legislation, the SRA, which is a commonwealth Act, takes priority.[79]

The conflict between the Australian SRA and their previous companies legislation, which required registration of securities in company property, was resolved in the same way. *Ex parte North Brisbane Finance and Insurances Pty Ltd*[80] provided authority that s109 granted primacy to the SRA over the Companies Act 1981 (or the Companies Code of each state), which was state legislation. Thus, securities over ships registered under the SRA did not have to be registered on the companies register.

This stance has since been codified in s262(1)(d) of the Australian Corporations Act 2001, which excludes securities over registered ships from the registration requirements under the company charges regime.

Due to the central role of the Commonwealth Constitution and the absence of any equivalent New Zealand legislation, neither of these examples is of aid in resolving the issue as it stands in New Zealand. However, the New Zealand situation may provide valuable aid to the Australian legislature, which is currently in the process of drafting a personal property securities Act based on Article 9, as is the New Zealand Act. As the

[79] P McDermott, "Maritime Securities", in M White (ed) *Australian Maritime Law* (2nd ed, The Federation Press, 2000), 166.
[80] *Ex parte North Brisbane Finance and Insurances Pty Ltd* [1983] 2 Qd R 684.

proposed PPSA will be commonwealth legislation (on an equal footing with the Australian SRA), s109 will be ineffective to resolve inconsistencies, and care must therefore be taken to avoid the conflict that exists in New Zealand. It seems that the Australian Law Commission may already be on the right track, having acknowledged the existence of asset based registers for property including ships, and the need to bring these within the new personal property regime.[81]

As with the Australian situation, the position in Canada is equally unhelpful as the relevant conflicts between legislation have been resolved by the doctrine of federal paramountcy, which is again not applicable in New Zealand.

There, numerous conflicts have arisen between provincial PPSAs and the enforcement and registration provisions of the Bank Act (a federal Act).[82] These issues fall subject to the doctrine of federal paramountcy, which stems from s91 of their Constitution.[83] The doctrine requires that conflicts between federal and provincial legislation be determined in favour of the federal Act – in this case the Bank Act.[84] Although there has recently been a large degree of uncertainty surrounding the law in this area, this was due to disagreement over when and how the doctrine should be applied, rather than whether one Act should prevail over another.[85] The case law in this area[86], therefore, offers little guidance to New Zealand courts.

Unfortunately, the conflict between dual registration schemes arising under the Canada Shipping Act and provincial PPSAs (mirroring the conflict in New Zealand), is also

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[81] The Law Reform Commission – Australia, Report No 64 "Personal Property Securities" 129-130.
[82] R H McLaren *The 2002 Annotated Ontario Personal Property Security Act* (Thompson Canada Limited, 2001), 9.
[83] (Canadian) Constitution Act 1867, s91.
[84] The Bank Act falls subject to the doctrine of federal paramountcy as a result of s91(15) of the Constitution Act 1867.
[85] B Crawford "Must a bank comply with provincial legislation when enforcing a Bank Act security: *Bank of Montreal v Hall*" (1991) CBR 142, 142.
[86] Cases addressing the conflict between the Bank Act and provincial PPSAs include: *Rogerson Lumber Co v Four Seasons Chalet Ltd* (1980) 113 DLR (3d) 671; *Re Birch Hills Credit Union Ltd and Canadian Imperial Bank of Commerce* (1988) 52 DLR (4th) 113; *Re Bank of Montreal and Pulsar Ventures Inc* (1987) 42 DLR (4th) 385; *Royal Bank of Canada v Kreiser* (1986) 34 BLR 73.

resolved by this doctrine.[87] As federal legislation, the Canada Shipping Act takes primacy over provincial personal property regimes.

In the US, the security registration schemes available under both Article 9 and the Ship Mortgage Act potentially give rise to the same conflict seen between the New Zealand legislation. The 1962 version of Article 9 expressly excluded transactions falling under the Ship Mortgage Act 1920[88] (a federal statute), which sets out the formal requirements of a preferred ship mortgage, provides for registration, and includes rules for determining priority. However, later versions of Article 9 have abandoned this reference to ship mortgages.

Nevertheless, courts have held that perfection under Article 9 does not protect transactions covered by the Ship Mortgage Act.[89] The deletion of the express reference to the Ship Mortgage Act was for stylistic purposes only, and ship mortgages are still excluded by virtue of UCC § 9-109(c) which prevents the application of Article 9 to the extent that it is preempted by a federal statute.[90] As the Ship Mortgage Act provides a comprehensive regime governing the registration and priority of ship mortgages, it preempts Article 9. Although there is both academic[91] and judicial[92] support for the argument that Article 9 still applies to fill the gaps remaining in the federal Act, the problem of dual registration schemes does not arise.

[87] The reference to "shipping" in s91(10) of the Constitution Act 1867 means the Canada Shipping Act is protected by the doctrine of federal paramouncy.
[88] 46 USC §313.
[89] *McCorkle v First Pa. Banking & Trust Co.* 321 F. Supp. 149, 8 UCC Rep 981 (D. Md.1970).
[90] B Clark & B Clark *The Law of Secured Transactions Under the Uniform Commercial Code* (A.S. Pratt & Sons, 2006), 1-131.
[91] See G. Gilmore *Security Interests in Personal Property* (Little, Brown & Company, 1965) 408.
[92] See *Brown v Baker* 688 P2d 943, 39 UCC Rep. 1105 (Alaska 1984); *Morgan Guaranty Trust Co. v M/V Grigorios C. IV* 615 F Supp 1444, 42 UCC Rep. 603 (ED La. 1985); *Bank of America NTSA v Fogle* 637 F Supp 305, 2 UCC Rep. 2d 270 (ND Cal. 1985); and *In re McLean Industries, Inc* 15 UCC Rep. 2d 1062 (Bankr SDNY 1991).

6. New Zealand Law

New Zealand law may itself offer solutions to the conflict at hand. This chapter will look first at securities over aircraft, which bear many resemblances to maritime securities and also fall subject to the PPSA. It will then go on to analyse a recent High Court decision where the SRA was afforded primacy over the PPSA.

6.1 Aircraft and the PPSA

While the success of the 2001 Cape Town Convention explains the more favourable conditions surrounding aircraft finance at an international level, it should be noted that New Zealand is not presently a signatory to this convention (although there has been agreement for it to be ratified subject to an assessment of the legislative changes required).[93] Instead, aircraft securities in New Zealand remain governed by the PPSA.

Under the Personal Property Securities Regulations 2001, aircraft are subject to registration by serial number. The register may be searched by serial number, registration mark or nationality mark, rather than debtor name alone.[94] This provides greater protection for potential creditors.

Although the Civil Aviation Act 1990 provides for the registration of aircraft, this does not affect issues of title or security interests in aircraft. Unlike the SRA, the Civil Aviation Act does not provide for the registration of mortgages or securities over aircraft. As a result, there is no specialist regime relating to aircraft securities which might conflict with the PPSA in the way that the SRA does.

Nor are there problems of conflict between New Zealand PPSA registered securities and foreign registered securities (or securities internationally registered under the Cape Town Convention). This is due to ss30-31 of the PPSA, which allow for the validity and perfection (including the effect of perfection) of foreign securities to be determined by

[93] Above n 56, 713.
[94] Personal Property Security Regulations 2002, s16.

the law of the debtor's jurisdiction. These sections, which apply to goods that are normally used in more than one jurisdiction, are equally applicable to qualifying ships.[95]

The position with regard to aircraft therefore offers no direct guidance as to which Act should prevail. The absence of any conflict between the PPSA and foreign aircraft securities regimes demonstrates the adequacy of the PPSA's conflict of laws provisions, and may count as a reason in favour of granting primacy to the PPSA. However, it does not provide a definitive justification for choosing the PPSA in preference to the SRA.

6.2 The KeyBank case

The conflict between the two Acts has in fact been examined in the recent High Court decision of *KeyBank National Association v The Ship "Blaze"*.[96] The case involved an unusual blend of law, hinging on the interpretation to be given to the SRA and the PPSA in the context of international maritime and admiralty law.[97]

The ship in question was a 63 foot, New Zealand built vessel that therefore fell short of the 24m length exclusion in s23. The ship was sold to a US resident who duly registered the vessel in accordance with US law in 2000. A mortgage was then granted in favour of KeyBank, which was in turn also registered on the US register. The ship was then brought to New Zealand and sold to a Mr Walters, who on-sold the vessel to Barrington Charters Ltd – a company under his control. Unfortunately the mortgage in respect of the ship was never discharged and KeyBank sought to enforce its mortgage, having the vessel arrested. At this point, Mr Walters registered a security interest under the PPSA. Although the case is silent as to how Mr Walters' security interest arose, presumably it was the result of a loan from him to the company, secured by the vessel. Three days later, KeyBank's interest was also registered on the PPSR.

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[95] Above n 56, 711.
[96] *KeyBank National Association v The Ship "Blaze"* (HC Auckland, CIv 2006-404-2266, 9 February 2007, Baragwanath J).
[97] E Wah "Ships and PPSA" (2007) NZLJ 171,171.

Under the PPSA, Mr Walters' security took priority by virtue of s66 as the first registered security. However, s70 of the SRA required that KeyBank's US registered security be treated as if registered under the SRA and be afforded the same priority as an SRA registered security. Thus, the outcome of the case hinged on which Act was to apply. Under the PPSA, Mr Walters' security prevailed, while under the SRA KeyBank held the superior interest.

It should be noted that this problem of competing registration schemes under New Zealand law could have been avoided by simply applying US law which would have preferred KeyBank's US registered mortgage. However, this was not raised in argument by counsel, nor was it an approach that Justice Baragwanath chose to employ. He does, however, place great emphasis on New Zealand's international obligation to give effect to flag law.

His Honour's judgement can be very briefly summarised as follows. He rejects an *expressio unius* argument in relation to s23(e)(xi), preferring to treat the suggested implied inclusion of ships under 24m (within the ambit of the PPSA) as a default provision dealing with vessels not registered on Part A. This construction was justified due to the failure of the PPSA to expressly exclude the SRA in relation to ships under 24m, coupled with the continued existence of the SRA unamended.

The notion of an implied repeal of the SRA for security purposes in relation to ships under 24m was also inappropriate due to the practical consequences. There were at that time 1600 ships under 24m registered on Part A, of which nearly 20 percent were subject to registered mortgages. Allowing the PPSA to govern all securities over ships under 24m would invalidate these securities. As a reasonable alternative construction existed, it was inappropriate for the court to invalidate securities over 20 percent of the New Zealand register entries.

He was also particularly influenced by New Zealand's international obligations, reasoning that New Zealand legislation is not to be construed in a way that infringes these

obligations. He quotes *Sellers v Maritime Safety Inspector*[98] as authority that the flag state has exclusive jurisdiction over ships on the high seas, and concludes that in this case there are powerful reasons for applying US law. New Zealand was therefore obliged to respect property rights created under that law.

He refers to the fact that New Zealand is a Mecca for visiting yachts, many under 24m and sailing under foreign flags. These ships are subject actually or potentially to securities created under their foreign laws. An interpretation of the PPSA that allows the operation of s70 to protect such securities is in conformity with New Zealand's international obligations. It would be "bizarre" to construe the PPSA in a way that required owners and mortgagees of these ships to register a financing statement immediately upon the ship entering New Zealand waters.

Finally, he concludes that the appropriate reasoning can be found in the maxim *generalia specialibus non derogant*: statutes expressed in general language do not override earlier statutes dealing more specifically with the topic. Thus, KeyBank's security took priority.

However, the importance of this decision is that it is not limited to cases where s70 is invoked. His Honour concludes his judgment by finding that "the PPSA can have no application to securities that fall directly or (via s70) indirectly within the SRA." Consequently, wherever there is a SRA registered security, the PPSA has no application, irrespective of whether the case involves a foreign ship under s70.

6.3 Analysis and implications of the KeyBank decision

A number of issues arise with regard to the reasoning and outcome in this case. The primary policy concerns by which Justice Baragwanath justifies the decision are (i) the practical consequences of invalidating SRA securities; and (ii) New Zealand's international obligations. With respect to his Honour, it is contended that the decision is only justified insofar as it relates to foreign ships falling within s70.

[98] *Sellers v Maritime Safety Inspector* [1999] 2 NZLR 46-7

(i) The practical consequences

His Honour's reluctance to interpret the legislation in a way that would invalidate SRA securities is understandable. However, he does not appear to appreciate the corresponding invalidation of PPSR securities that results from his alternative interpretation. Unfortunately the PPSA does not provide a mechanism for calculating the number of PPSR registered securities in ships under 24m. The precise number of securities invalidated is therefore uncertain. Nevertheless, his Honour's argument with regard to invalidating SRA securities is less persuasive when the resulting invalidity of PPSR securities is taken into account.

Furthermore, he fails to consider the effect of granting priority to the SRA in all cases. It would not be uncommon for a ship, in respect of which securities have been registered on the PPSR, to be later registered on Part A. In this situation the rule formulated by Justice Baragwanath would grant primacy to any later SRA registered securities. This would allow a creditor to defeat prior securities registered under the PPSA simply by registering his security under the SRA.[99] To allow such manipulation of priority is clearly inconsistent with the policy of the Acts. Further, this may in some cases allow the SRA to be used as an engine of fraud, which is surely not a result Parliament would have intended!

(ii) New Zealand's international obligations

While there is no doubt that New Zealand must respect its obligations under international law, this argument justifies the decision in respect of foreign ships only. It is not sufficient to sustain the conclusion that *all registered mortgages* must prevail over any PPSR security. The very fact of registration on the New Zealand register means the ship is necessarily a New Zealand vessel, and thus does not warrant the protection required by international law.

[99] For discussion on this point see D Webb "Commercial Law" (2007) NZL Rev 373, 385.

It has also been suggested by Allan that New Zealand has already satisfied its international obligations through the provisions of the PPSA.[100] Firstly, it has excluded ships over 24m as these are more likely to enter international waters. Secondly, it provides for goods of a kind that are normally used in more than one jurisdiction. Section 30 provides that such goods (which must include ships operating internationally), remain governed by the law of the debtor's jurisdiction at the time of attachment. Securities will therefore be prioritised by the foreign law, as against security interests created in New Zealand. Finally, s27 provides for goods moved to New Zealand subject to a foreign perfected security. The creditor will retain the priority given by the foreign registration, provided the security is registered in New Zealand within 60 days of the goods arriving in New Zealand, or within 15 days of the creditor's knowledge of their arrival.[101]

Between them, these provisions appear to give effect to New Zealand's international obligations to respect the law of the flag insofar as the ship remains on the high seas. This is further supported by the fact that the conflict of laws provisions in ss27-31 are seen as sufficient to discharge New Zealand's international obligations with regard to aircraft securities. However, it is submitted that they do not give effect to flag law to the extent required by international maritime law principles.

Firstly, s30 applies the law of the debtor's location as opposed to the state of registration. While this has little effect where the debtor is located in the state of registration (as was the situation in *KeyBank*) difficulties occur where the debtor's location does not coincide with the state of registration, as s30 fails to give effect to the exclusive jurisdiction of the flag state. This could, however, be avoided if the ship were interpreted to be the debtor. As an action *in rem* is an action against the vessel itself, the ship should, in theory, be treated as the debtor. Flag law would therefore prevail (assuming the artificial *situs* principle applies) as the law of the ships location at the time of attachment. If this

[100] Above n 58, 96.
[101] Above n 58, 96.

interpretation is accepted, s30 adequately recognises New Zealand's obligations at international law.

However, even if the PPSA is given the benefit of the doubt with regard to s30, a further difficulty can be seen in relation to s27. While s27 allows for continuous perfection of foreign securities, this is only where the creditor registers a financing statement within the requisite time. Accordingly, s27 does not provide relief where a creditor is unaware that the vessel has been moved to New Zealand, or assumes that his registered mortgage will retain priority in accordance with flag law (as it would had the vessel been moved to almost any other jurisdiction), and therefore fails to perfect under the PPSA. In such cases, this section fails to give effect to the exclusive jurisdiction of the flag state.

In order to properly assess the effectiveness of the PPSA, particularly s27, in discharging New Zealand's international obligations, it is therefore necessary to determine precisely what these are. Does New Zealand have an absolute obligation to recognise foreign registered mortgages where the ship has been permanently moved to New Zealand? Or, is the possibility of continuous perfection under s27 (where a financing statement is registered within the requisite time) sufficient?

The fact that commentators now argue for a move away from the exclusivity of flag law supports the notion that s27 sufficiently discharges New Zealand's obligations with respect to international ships. In addition to this, Parliament was content to limit the priority rights of creditors of foreign registered vessels, by way of s70 SRA. This section effectively treats all foreign registered interests as registered mortgages, failing to give effect to their varying priority status under flag law. In enacting s70, Parliament itself may be seen as approving the limitation of the overriding importance of flag law.

However, regardless of the merits of such a shift away from the application of flag law, this does not change the fact that New Zealand is a signatory to UNCLOS which expressly acknowledges the exclusive jurisdiction of the flag state where ships are on the high seas. While this does not apply to ships having entered New Zealand waters, the

policy underlying the SRA provides an indication of what New Zealand's obligations should be in this situation.

One of the primary objects of the SRA was to bring New Zealand shipping law into line with maritime law internationally.[102] Consequently, New Zealand law must respect, as other jurisdictions do, the internationally recognised principle that ship mortgages fall subject to flag law and that creditor's can therefore rely on the priority afforded by a foreign registered mortgage. If the well established maritime laws relating to registered mortgages were to be abandoned in New Zealand, this would undermine the very purpose of the SRA.

It follows that New Zealand's international obligations, relevant in the present case, are as follows: (i) to give effect to the principle of the freedom of the high seas, which requires the application of flag law when determining interests or claims arising when a ship is on the high seas; (ii) to give effect to internationally accepted principles of maritime law, including the rule that the validity and priority of mortgages are to be determined in accordance with the law of the flag. While the PPSA goes some way in giving effect to foreign rights, it falls short of discharging these obligations.

Clearly, there are merits to the view that s27, operating in tandem with s30 to cover all foreign vessels (whether temporarily or permanently located in New Zealand), gives adequate recognition to foreign registered mortgages. After all, why shouldn't a creditor be required re-perfect his security in accordance with the laws of the country to which the collateral has been permanently moved? However, it is submitted that the need to comply with international norms, regarding the recognition and priority of ship mortgages, represents an absolute and overriding concern, outweighing the merits of the previous view.

The PPSA therefore falls short of discharging New Zealand's international obligations in respect of foreign registered mortgages. Consequently, his Honour's conclusion that the

[102] Report of the Select Committee on the Ship Registration Bill, NZ Parl. Deb., 2 June 1992, 8450-8451.

PPSA should not apply appears justified insofar as it relates to foreign ships. However, his conclusion simply cannot be justified with regard to New Zealand registered ships, as New Zealand's international obligations do not extend to these vessels. Further, his Honour's pronouncement that the SRA should prevail over all PPSA registered securities comes with the troubling consequence that creditors can now register securities on the SRA in order to defeat prior PPSR registered securities.

6.4 Practical effects of the KeyBank decision

It would appear that this decision is of little practical consequence in the commercial sphere. A survey[103] of New Zealand's major law firms and marine financiers has shown that typically ship mortgages are registered under both the SRA and the PPSA. All participants surveyed were aware of the *KeyBank* decision, but said that it had not affected their method of perfecting securities. One financing company registered mortgages solely on the SRA, and viewed the *KeyBank* decision as the correct assertion of the law, validating this practice. All others registered under both Acts due to the uncertainty as to which would prevail.

This practice of dual registration highlights the need for legislative reform. The current ambiguity of s23(e)(xi) has led to widespread commercial uncertainty. While the *KeyBank* decision may be justified insofar as it relates to foreign securities falling under s70, commercial actors are hesitant to rely on this judicial clarification of the law, preferring to continue to register under both Acts.

Furthermore, it is doubtful whether the *KeyBank* dicta can be justified with regard to New Zealand registered vessels. There are also a number of issues that the *KeyBank* decision fails to address. Ultimately, there simply does not appear to be a valid reason for one act to prevail over the other, with courts seemingly forced to pick one at random. If, due to an absence of persuasive policy concerns, an arbitrary choice between the legislation is required, this choice should fall to Parliament.

[103] The survey was completed by the author in July 2006. For full results, see appendix.

PART III: LEGISLATIVE REFORM

7. Reform

This chapter will first outline four options for reform and comment on their desirability at a policy level, analysing their effect on the objects and purpose of both the PPSA and the SRA. It will then go on to examine the practical difficulties associated with implementing the more attractive solutions, in order to ascertain the best option for reform.

7.1 Options for reform

Parliamentary intervention is clearly desirable in order to resolve the present conflict between the legislation. When considering options for reform, it should be born in mind that ship registration on Part A comes with the consequence that the vessel is marked with a registration number and that mortgages can then be registered against that vessel. The range of interests that can be registered as a mortgage under the SRA is relatively narrow when compared with the PPSA, and does not include securities over after acquired property.

What is required is an amendment that clarifies when each Act is to apply, while satisfying NZ's international obligations. Parliament is therefore left with four key options for reform:

(i) SRA as the sole means of registering securities in ships of any size

This could be achieved by amending s23 to exclude *all* ships from the operation of the PPSA. The SRA would provide the sole means for registering securities against vessels, regardless of size. If this solution were implemented, all current PPSR registered securities in ships would be invalidated. In order to avoid this, Parliament would need to provide for all current PPSR registered securities in ships to be transferred to the SRA under their current priority dates.

The major difficulty with allowing the SRA to govern all securities in ships is that creditors who take security in vessels not registered on Part A have no way of registering their interest, unless the PPSA is allowed to operate.

One way of preventing this would be to require compulsory Part A registration of all ships given as security, where this security would be registerable as a mortgage under Part A. However, this option is undesirable due to the cost of registration on Part A, which ranges from $899 to $1688.[104] This is not economical where a smaller vessel, not otherwise required to register on Part A, is given as security. In such cases, the cost of registration may well exceed the value of the debt secured or indeed the vessel!

It is therefore better if the Part A registration requirements could be left as they currently stand. This would mean mortgages of unregistered ships or those registered on Part B could not be registered and would remain equitable only. In this situation, many creditors would probably require Part A registration as a condition of any finance agreement. However, where creditors (no doubt charging a higher rate of interest) are happy to allow the common law to govern their security, it would at least remain possible for owners of vessels not registered on Part A to use their vessel as security.

If possible, it is preferable that securities over unregistered vessels or those registered on Part B remain registerable under the PPSA. However, it may not be possible to implement this as a workable solution. Should this be the case, allowing the SRA to govern as the sole means of registering securities in ships of any size presents a simple and practical solution that is easily implemented, and will bring necessary certainty to the law.

[104] Maritime New Zealand Registration Fees for Part A & Part B (internet) <www.maritimenz.govt.nz/ship_registration/reg_fees.asp> accessed 24/09/07.

(ii) Allow the PPSA to govern in all cases

An alternative solution is to grant absolute primacy to the PPSA by abolishing the registration of mortgages under the SRA. Allowing the PPSA to govern as the sole method of registering a security interest would bring requisite clarity to the law while ensuring all creditors are able to protect their security interests by registration. As in (i) above, the PPSA would need to provide for the transfer of all current SRA securities, in order to avoid invalidity.

However, this solution is unworkable for obvious reasons. Abolishing the registration of mortgages under the SRA would plainly defeat the objects of the legislation, which seeks to provide a single register of all details relating to a ship's title, by providing evidence of that title and all mortgages registered against that title. Entirely removing securities from the ambit of the SRA would clearly frustrate this purpose. Furthermore, as alluded to earlier, granting primacy to the PPSA would frustrate the purpose of having two registers under the SRA, by removing the incentives associated with Part A registration.

Allowing the PPSA to govern as the sole means of registering securities in ships is, therefore, not a viable option and can be discounted as an option for reform.

(iii) Grant priority in order of registration, regardless of the register used

An alternative solution, suggested by Allan, is to rank security interests in order of registration on either register.[105] Both registers would effectively be looked at together, with priority awarded in order of registration, irrespective of which register has been used.[106]

However, a number of difficulties arise with this proposal, due to the considerable divergence between the concepts of law underpinning the two Acts. The SRA establishes a Torrens type system of title, based on registration, which adheres to

[105] Above n 58, 96.
[106] Above n 58, 96.

traditional concepts of ownership. One of the primary objectives of the SRA was to establish a New Zealand register that provided evidence of title and mortgages registered against that title.[107] Undermining this objective is a necessary implication of adopting this solution, as the SRA will no longer provide evidence of all encumbrances registered against a ship. It is therefore necessary to look past the fact that evidence of securities over vessels will be spread across two registers, instead of one, in order to evaluate the merits of this solution.

However, allowing the PPSA to apply to ships registered on Part A would further thwart this objective, as the PPSA rejects the traditional importance of title and ownership in favour of perfection in accordance with the Act. It is now well established law in New Zealand that, under the PPSA, an owner's title to goods that are leased for more than one year (thereby creating a security interest[108]) will be subjugated to a registered security in those goods, unless the owner registers a security interest.[109] It is easy to envisage a situation where the owner of a ship registered on Part A, charters the ship for over a year to a lessee who has granted a general security purporting to include after acquired property (in this case, the ship). Where the owner fails to register a security interest, the lessee's creditor gains a superior interest. Thus, in circumstances where the owner retakes possession without the creditor's permission and sells the vessel to a third party, the owner commits an act of conversion. Section 23 of the Sale of Goods Act dictates that this third party, purchasing the vessel in reliance on Part A, receives poor title to the vessel.[110]

While Part 5 of the PPSA does provide some protection for bona fide purchasers for value, allowing them to take free of a perfected security in certain situations, none of the provisions apply to the scenario illustrated above. This does not sit

[107] Report of the Select Committee on the Ship Registration Bill, NZ Parl. Deb., 2 June 1992, 8449.
[108] PPSA s17(1)(b) provides that a "security interest" includes a lease for a term of mort than one year.
[109] See *New Zealand Bloodstock Ltd v Waller* [2006] 3 NZLR 629 (CA); *Graham v Portacom New Zealand Ltd* [2004] 2 NZLR 528.
[110] Sale of Goods Act s23 codifies the principle *nemo dat quod non habet* that a purchaser cannot receive better title than the seller had.

well with the SRA. If Part A does not provide evidence of title, which can be relied on by a purchaser in order to ensure they receive good title and are not party to an act of conversion, this runs contrary to the purpose of the SRA.

This factor emphasises the desirability of allowing securities over vessels registered on Part A to remain governed solely by the SRA if the integrity of the Part A register is to be preserved.

A further problem arises with regard to the enforcement and notice provisions contained in Part 9 of the PPSA, as equivalent provisions do not exist under the SRA. These provisions regulate a secured party's dealings with collateral, require notice of sale to be given to the debtor and other creditors, and provide rules for dealing with accessions. Allowing creditors to avoid the application of these provisions simply by registering their security under the SRA, rather than the PPSA, would circumvent the operation of the PPSA and prejudice creditors with securities registered on the PPSR.

However, this should not necessarily prevent the registers operating in unison. The integrity of the Part A register could be partly maintained by providing that any PPSA rights or interests that would not exist under the SRA or are not capable of registration under the SRA must be unenforceable where a vessel is registered on Part A. This means that where a previously unregistered vessel becomes registered on Part A, certain PPSA rights and interests are liable to be extinguished.

Creditors with PPSR registered securities would, therefore, be liable to have their rights under the PPSA, and indeed their security interest (where the security is not of a type that is registerable as a mortgage under the SRA) defeated. Nevertheless, creditors would have the option of refusing to grant finance unless the vessel is registered on Part A, or raising the cost of finance to reflect the risks associated

with registering under the PPSA. Thus, creditors would not be disadvantaged by this solution.

In practical terms, this solution is far better than having the SRA as the sole means of registering securities in ships, as suggested in (i). This prevents securities over ships not registered on Part A from falling subject to the common law, by allowing the PPSA to continue to apply. While it will in some cases result in the invalidation of PPSR registered securities, such as those arising out of leases for more than a year, or those purporting to include after acquired property, creditors are able to protect against such risks. Further, is submitted that any negative costs, associated with the loss of rights where a vessel becomes registered on Part A, are outweighed by the advantages of providing a means of registering securities in small ships, the vast majority of which will never become registered on Part A.

At a policy level, this solution both alters and curtails the operation of the PPSA to such an extent that it may be seen to undermine the aims of the legislation. However, these inconsistencies with the objects of the legislation need to be weighed against the practical benefits of the solution. In this case, the benefits of allowing the continued operation of the PPSA, in relation to small ships for which Part A registration is not practical, would seem to override concerns as to the effects of undermining legislative policy. In support of this is the fact that the operation of the PPSA is only modified with regard to ships. As the Act will continue to operate as intended with regard to all other forms of personal property, the objects of the legislation are, for the most part, not frustrated.

More worrying is the fact that the integrity of the SRA is to some degree compromised, in that it would no longer provide evidence of all encumbrances registered against a vessel. However, this too is outweighed by the benefits of the continued application of the PPSA.

It is therefore submitted that allowing the continued operation of both registers (with the proviso that the where a ship is registered on Part A, only those PPSA rights and interests that are consistent with the SRA will be enforceable) represents a viable option for reform.

(iv) Dovetail both Acts

The final solution is one advocated by academic and maritime consultant Tetley.[111] He suggests dovetailing the Acts by amending s23(e)(xi) to exclude all ships registered on Part A from the application of the PPSA. The SRA would therefore govern securities over ships registered on Part A, while the PPSA would control securities over all other vessels.[112] This gives effect to the objects of the SRA by allowing Part A to continue to provide evidence of title and all encumbrances registered against that title, while the continued operation of the PPSA ensures creditors have a means of registering securities over those ships not registered on Part A.

It appears that this is what Parliament intended to achieve through the current s23(e)(xi). However, the wording of the section failed to accomplish this due to the use of the "24m in length" distinction. This would be remedied by the proposed reference to Part A rather than ships over 24m.

With regard to foreign registered ships, it is submitted that they should also be excluded from the application of the PPSA, thus encouraging New Zealand creditors to register mortgages at the port of registry. This would allow s70 to operate unimpeded, avoid problems of the type that arose in the *KeyBank* case, and ensure New Zealand mortgagees gain adequate protection by registering their interest in accordance with the flag law of the vessel as opposed to the PPSA.

[111] Above n 56, 707
[112] Above n 56, 707.

This solution appears to present the ideal way of resolving the conflict between the legislation.

7.2 Problems with dovetailing the Acts

In suggesting this solution, Tetley clearly envisaged that the PPSA would operate unconstrained, as opposed to the more limited operation illustrated in (iii), above, whereby PPSA rights and interests may in some cases be extinguished as a consequence of Part A registration. Ideally, under the dovetailing solution, the PPSA should operate as a complete and absolute regime (with regard to securities over those ships not excluded by s23), wholly separate from the SRA. However, a number of difficulties arise, making this impossible. As a result, if the Acts are to dovetail, the PPSA will need to operate in a restricted capacity (as in (iii), above), in the sense that rights and interests arising under the PPSA will be liable to be defeated in some cases.

The first problem occurs where a security is validly registered under the PPSA, prior to the ship being registered on Part A. This situation arises either where an owner elects to register on Part A, as is their right, or where a ship previously under 24m is extended beyond this length, triggering compulsory Part A registration. In order to give effect to PPSR registered securities in respect of such vessels, the SRA would need to be amended to provide for these interests to be automatically transferred to the SRA upon the ship becoming registered on Part A. The interests must retain their original priority date of registration on the PPSR.

A further problem arises in the case of PPSR registered securities which include after acquired property. Here, the underlying security agreement is not one that can be registered as a mortgage under the SRA, as a specific security agreement in respect of the vessel is required. In essence, such creditors will lose the benefit of their registered security in the vessel by virtue of Part A registration.

It is therefore imperative that Part A registration does not operate to avoid the enforcement of PPSA securities, as any securities registration regime must, as a matter of

policy, be immune from such manipulation. A debtor who, having granted a security which applies to after acquired property, becomes the owner of a ship (to which this security attaches) should not be able to register the vessel on Part A in order to invalidate this security. Also in this vein, is the problem that rights available to creditors under the PPSA (such as the notice requirements and enforcement provisions) would be extinguished by Part A registration.

This could be solved by preventing voluntary Part A registration, where a vessel is subject to a PPSA security, without the permission of all secured parties. Where the security is of a type that cannot be transferred to the SRA (such as a security that purports to include after acquired property) the secured party will undoubtedly refuse permission. It would therefore be left to the debtor to discharge the security, or renegotiate the security agreement (for example granting a specific security over a vessel previously subject to a security over after acquired property). Where a debtor seeks to renegotiate rather than discharge securities, it may be necessary to construct subordination agreements between creditors in order to satisfy creditors that the SRA will reflect the current ranking under the PPSA.[113]

With regard to the loss of rights available under the PPSA, the secured party may agree to forfeit these by granting permission to Part A registration, or alternatively, may require that the relevant rights be incorporated into a new security agreement prior to Part A registration.

The situation is slightly more complex where a vessel is extended to over 24m in length, as Part A registration becomes compulsory under s6. This could be avoided if the SRA were to prohibit length extensions without secured party consent, where the extension would result in the application of s6 (where this provision did not previously apply) so as to require compulsory registration. This would allow the extension of vessels to which

[113] For example, under the PPSA a purchase money security interest (PMSI) ranks above earlier registered securities in the same collateral. Therefore, where a debtor plans to grant a specific security over a vessel previously subject to a general security including after acquired property, it may be necessary to subordinate this specific security to any PMSI over the vessel, if the PMSI has a later priority date.

the exceptions in s6 apply (as in the case of pleasure vessels). While this may be argued to unduly restrict rights of use and possession, it should be noted that such length extensions are only likely to occur in a very limited number of cases. Again the onus would remain on the debtor to gain secured party consent or discharge the securities. As this problem is most likely to occur in relation to general security agreements which include a debtor's after acquired property, it would usually be sufficient to enter a specific security agreement in respect of the vessel. It may be necessary to impose penalties on owners who breach this provision, in order to ensure compliance.

In order to put these provisions into practice and preserve the integrity of the Part A register, it would be necessary for the registrar to carry out a search of the PPSR in respect of every application for Part A registration, in order to ensure the proper consents are obtained. This in itself is not problematic and is unlikely to considerably increase the cost of registration.

However, it gives rise to two difficulties. The first arises with regard to leases for more than a year, which under the PPSA are deemed to create a security in favour of the lessor (the owner). As illustrated in (iii), above, the problem arises where an owner fails to register this security interest, thereby subordinating his interest to a security over the vessel registered by the lessee's creditor. In these circumstances, the owner cannot be allowed to effect Part A registration, as the SRA would not recognise the priority of the creditor's security. Again, Part A registration must not provide a means of defeating a creditor's legitimate security.

This problem may be partially solved by requiring secured party consent to registration, as outlined above. In practice, this would require the owner to discharge the security before registration can be effected. However, subsequent purchasers (who, as mentioned above, receive poor title) are unlikely to be aware of leases entered by the prior owner, and therefore will not know that the ship is subject to a security held by the lessee's creditor. While the security is at least discoverable by the owner, should he think to

search the register for securities granted by the lessee, a prospective purchaser is unlikely to be aware of previous lessees and would ordinarily search only the owner's details.

Where an owner has failed to register a lease for more than a year, it would therefore be necessary for the registrar to search the PPSR for securities granted by any lessee of the vessel. However, it is uncertain at what point an owner regains good title, and whether termination or expiry of the lease are sufficient to extinguish the security held by the lessee's creditor. While there is no case law on the issue, it is likely that the creditor's interest continues in the goods until discharged by the lessee.[114] This makes it virtually impossible for the registrar to ascertain whether such a security exists in the vessel as, while the current owner may be able to provide details of leases entered by himself, there is no way of ascertaining all the previous lessees of the vessel under previous owners.

The result is that the registrar can never be sure whether the current owner has good title, or whether the ship is subject to PPSR registered securities. The only way of avoiding this situation is to insert a provision analogous to those in Parts 5 and 6, providing that bona fide purchasers of ships for value are not affected by the previous owner's failure to register a lease for more than a year, and acquire good title. In these circumstances, the lessee's creditor would have rights to the proceeds of sale held by the seller, but would lose any rights of security in the vessel itself.

This conflicts with the objects of the PPSA as it seeks to superimpose traditional notions of title within the PPSA regime, which specifically rejects such concepts of law. Nevertheless, it can perhaps be justified as it is not possible to dovetail the Acts without such a provision. However, this debate is of little import, as the next difficulty casts the final blow to any possibility of dovetailing the Acts in the way Tetley intended.

[114] This is supported by the fact that an owner who fails to register his interest should not be able to circumvent the provisions of the Act (which give primacy to the registered interest of the lessee's creditor) simply by interpreting the lessee's actions as an act of default terminating the lease.

Under the PPSA, security interests continue in collateral sold without the permission of the secured party. While the secured party is required to file a financing change statement reflecting the change of ownership and evidencing the new debtor's details, this requirement is not imposed until the secured party becomes aware of the new owner.[115] In circumstances where the secured party is unaware of the transfer and has not registered a financing change statement, a search of the register using the current owner's details will not disclose the security. Where an application for Part A registration is then made, the registrar would have no reason to decline registration. The creditor would therefore lose his security in the vessel.

The only way of avoiding these problems would be to require ships to be marked with a registration number, allowing the PPSR to be searched by serial number, as in the case of cars and aircraft. At present, only those ships registered on Part A are marked with official numbers[116], and these ships are necessarily excluded from the PPSA under the suggested regime. It is therefore not a viable solution to require vessels to be marked in this way. Both vehicle chassis numbers and aircraft serial numbers provide a reliable form of identification, as there are well established systems recording these details and the numbers cannot be easily altered. As no such system currently exists in respect of ships, individual owners would be left to oversee the marking of serial numbers where they wish to register under the PPSA. This would prove unreliable and easily susceptible to fraud. It is therefore not feasible to treat ships as serial numbered goods under the PPSA.

Consequently, the Acts cannot be made to dovetail in the way originally intended. However, if the approach taken in (iii), above, is applied, whereby creditors bear the risk of PPSA interests becoming unenforceable as a result of Part A registration, this solution may be workable.

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[115] See PPSA ss87-92.

[116] Searching the Register (internet) <www.maritimenz.govt.nz/ship_registration/reg_search.asp> accessed 07/10/07. Ships registered on Part A are marked with an official six digit number, while ships on Part B receive a registration number only.

Where an application is made for Part A registration, the registrar could still perform a PPSR search, as explained above, and refuse registration without secured party consent. However, where the security is not evidenced by a PPSR search, the secured party will be liable to have their interest defeated. Thus creditors bear the onus of protecting themselves, either by refusing finance, or increasing interest rates to reflect this risk.

Arguably, the fact of registration alone need not extinguish the interest. The importance of the integrity of the Part A register stems from the need for third party purchasers or creditors to be able to rely on it as evidence of title and all encumbrances. Provided the ship has not been sold, become subject to a SRA registered mortgage or had a caveat[117] registered against it, the PPSA security could in most cases be enforced without jeopardising the integrity of the Part A register.

However, a potential difficulty arises with regard to third parties who act in reliance on the register but do not acquire a definitive interest in the ship. For example, potential purchasers may spend time and money entering negotiations to purchase a vessel, only to have the holder of a PPSA security assert his interest before a sale and purchase agreement is finalised. To this extent, the Part A register cannot be relied on, and its integrity is compromised as a result.

It is therefore submitted that, in the interests of simplicity, it is better to have Part A registration as the cut off point at which undiscovered PPSA interests become extinguished. In most cases, this will only affect securities in a vessels transferred without permission (where a financing change statement has therefore not been registered) and securities arising out of unregistered leases for more than a year. In all other cases, the security interest will be discoverable on a search of the PPSR, and the registrar will consequently deny Part A registration until secured party consent is recieved. Where an owner intentionally effects Part A registration in order to defeat one of these forms of

[117] A caveat may provide evidence that a third party has acquired an interest in the vessel in reliance on the Part A register.

security, the creditor will have an equitable remedy outside of the legislation, and is therefore not unfairly prejudiced.

This solution, therefore, provides another suitable option for reform. As discussed at (iii), above, the fact that the operation of the PPSA is somewhat restricted and to this extent impedes the objects of the legislation, is outweighed by the benefits of allowing the continued application of the PPSA with regard to small ships for which Part A registration is simply not financially viable. Thus, the question is whether this solution is preferable to the options outlined in (i) and (iii)?

7.3 Which solution should be preferred?

Clearly, having the SRA as the sole means of registering securities in ships of any size, as suggested in (i), is undesirable as securities over ships not registered on Part A would be unregisterable and fall subject to the common law. However, this solution is appealing due to its simplicity, particularly when compared to the other two options which require provision to be made for an array of different contingencies, and are therefore somewhat convoluted responses.

However, the importance of personal property securities regimes to economic development has long been recognised[118], and it is now taken as a given that some form of registration system is vital to any such regime in order to provide a clear statement of parties' rights and an effective range of remedies.[119] Thus, a registration scheme is central to the efficiency of secured transactions and is far superior to relying on the common law alone. Denying small ships access to a registration system is, therefore, not a step that should be taken lightly. As there exist two other solutions that avoid this consequence, one of these should be chosen in preference.

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[118] I Davies "The Reform of English Personal Property Security Law: Functionalism and Article 9 of the Uniform Commercial Code" (2004) 24 Legal Studies 295, 296; R M Goode "Security in Cross-Border Transactions" (1998) 33 Texas ILJ 47.

[119] J Farrar & M O'Regan *Reform of Personal Property Security Law: A Report to the Law Commission* Preliminary Paper No.6 (NZLC, 1988), 11; R M Goode "The modernization of Personal Property Security Law" (1984) 100 LQR 234, 238-239.

In light of the objects of the SRA, it is suggested that dovetailing the Acts, as detailed above, should be preferred to viewing both registers together, as discussed in (iii). As dovetailing the Acts allows the SRA to provide the sole means of registering securities in vessels registered on Part A, this solution better achieves one of the primary objectives of the SRA: to provide a single register evincing title to ships and all encumbrances registered against that title. Where both registers are viewed together, the Part A register cannot fulfill this objective as potential purchasers or financiers are unable to rely on the Part A alone to provide this evidence. To this extent the integrity of the register is compromised. This is particularly troublesome with regard to foreign parties who may assume that the SRA provides the only relevant register, as it would in most other jurisdictions.

As another key aim of the SRA was to align New Zealand law with the law internationally, adopting a system of dual registration schemes that are uncommon to most jurisdictions would seem at odds with this objective. As a general rule, most countries have a single statute governing both ship registration and ship mortgages, and operate a single register which records both details of ownership and registered mortgages. Departing from this international norm would be in conflict with the aims of the SRA, and should therefore be avoided.

Choosing this solution does come with the consequence that securities that are not discovered by the registrar's search of the PPSR prior to permitting Part A registration, will be extinguished. However, creditors should be able to protect themselves adequately against this risk.

Dovetailing the Acts, therefore, presents the best option for reform as it maintains the integrity of the Part A register while providing an alternative registration regime under the PPSA for those ships not registered on Part A.

8. Conclusion

The law as it currently stands in New Zealand is clearly unsatisfactory. The conflict between registration schemes under the PPSA and the SRA has created great uncertainty. As previously mentioned, this problem is unique to New Zealand, and foreign case law and international conventions therefore offer little guidance on the matter.

Legislative reform is clearly necessary. Dovetailing the Acts, as discussed in the final chapter represents the best solution as it allows the SRA to govern where ships are registered on Part A, while continuing the operation of the PPSA in relation to those ships for which Part A registration is not a viable option. This does, to some extent, limit the operation of the PPSA (in relation to vessels subject to PPSA securities that become registered on Part A) and expose creditors with PPSA securities to the risk of having their interests defeated. However, these costs are justified by the benefits of providing a registration system for securities over ships not registered on Part A, and by the fact that creditors can protect themselves against this risk by refusing finance or increasing interest rates.

While this solution may not be ideal, there are few other options for reform. Further, it is desirable that New Zealand law conform with the laws in other jurisdictions, if the disorganised state of maritime securities law internationally is ever to move towards a more cohesive system. While New Zealand could seek to implement a registration system along the lines of the Cape Town Convention, this would be ineffective due to the hostility of the international shipping community towards conventions governing maritime securities. Thus, New Zealand has little choice but to try to align its national maritime securities law with that seen in other jurisdictions. Dovetailing the Acts, as suggested, achieves this by giving due weight to the Part A register, while still adequately providing for smaller ships.

Unfortunately, there are currently few calls for reform with regard to this issue, and legislative amendment in the near future is therefore unlikely. Until Parliament sees fit to

address this issue, the law in New Zealand will remain uncertain and creditors should continue to protect their interests by registration under both Acts.

On an international front, it is hoped that this conflict of dual registration schemes can be avoided in other jurisdictions. As the implementation of PPSA regimes based on Article 9 are becoming increasingly popular, other jurisdictions should be encouraged to learn from the New Zealand example, and avoid similar conflicts between their SRAs and any proposed security regimes.

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Appendix

Survey of New Zealand law firms and marine financiers – July 2006

Participant	*Method of registering securities in ships under 24m (where registered on Part A) prior to KeyBank decision:*	*Aware of Keybank decision?*	*Has method of registering securities in ships under 24m changed as a result of the KeyBank decision?*
Bellgully	Register under both Acts	Yes	No
Simpson Grierson	Register under both Acts	Yes	No
MinterEllisonRuddWatts	Register under both Acts	Yes	No
Kensington Swan	Register under both Acts	Yes	No
Buddle Findlay	Register under both Acts	Yes	No
Chapman Tripp	Register under both Acts	Yes	No
Mayne Wetherell	Register under both Acts	Yes	No
Russell McVeagh	Register under both Acts	Yes	No
Marac Finance Limited	Register under the SRA only	Yes	No
Toyota Marine Finance	Register under both Acts	Yes	No
Marine Finance Limited	Register under both Acts	Yes	No
Finance Direct	Register under both Acts	Yes	No