**Secured Transactions Reform in Jamaica**

**Final Report of Private Sector Development Expert: Paul Holden Under IDB Contract: Dated July 9, 20**

**Introduction**

Analytical work has identified the weak collateral framework in Jamaica as one of the reasons for the severe underdevelopment of its financial markets. Many businesses, particularly SMEs, find it difficult or impossible to obtain loans for investment and business expansion. The analysis showed that the outdated laws governing the pledging of assets as security contributes substantially to the difficulty of obtaining credit.

With the support of the Inter-American Development Bank, Jamaica has embarked on a comprehensive program to reform the business environment and to enhance its competitiveness. As part of its commitments under a third Programmatic Loan, the government of Jamaica has undertaken to reform its framework in terms of which personal property (all property except land and buildings) is pledged as collateral for loans.

**Support for the Reform**

The IDB engaged Paul Holden and Alan Welsh (the consultants) to support Jamaica in implementing this reform. Extensive discussions were held with stakeholders, government departments, and senior officials to ascertain overall support for secure transactions reform in Jamaica and to map the processes necessary to achieve changes in the system in terms of which assets are pledged as security for loans. The consultants identified strong support for this reform from virtually all of private sector stakeholders with whom discussions were held. There was also strong support within parts of government, although a number of government officials expressed reservations regarding the abolition of the Bills of Sale Act and Company Charges. In addition, uncertainties remain regarding both the form and the location of a new Secured Transactions Registry.

**Outputs**

In support of the reform the consultants drafted a number of briefs and discussion papers. A draft paper was prepared to support submission to the Cabinet of a brief that will underlie the issuing of Drafting Instructions in order to have a draft Secured Transactions Bill prepared (Annex A). A background paper was also prepared to brief Cabinet Members on the economic justification for secure transactions reform and to demonstrate the beneficial effects that such a reform has had in other countries (Annex B).

In order to garner stakeholder support a briefing paper was prepared for the Jamaica Bar Association for circulation to its members in order to inform them of the proposed reform (Annex D). In addition, a briefing paper was prepared that highlights the legal issues involved in the reform in Jamaica and outlining the experience of other countries in the legal aspects of the reform, demonstrating the differences in the various reforms that have occurred (Annex C).

This phase of the consultancy is now complete. The team awaits the issuing of a policy statement from the cabinet, which will include instructions to the sponsoring ministry to issue drafting instructions. Drafting instructions may be accompanied by a discussion bill intended to conform to the specifics issued by the cabinet. These instructions will also be copied to the Attorney General and the Chief Parliamentary Counsel.

At this point intense discussions are underway in Jamaica among various stakeholders, particularly those in government. Additional briefings may be necessary by one of the consultants in order to ensure that confusions are eliminated and clarifications made.

**Unresolved Issues**

1. In spite of repeated requests, the team was unable to obtain up-to-date data on the number of bills of sale registrations over the past two years.
2. Similarly, the team was unable to obtain data on revenue generated from bills of sale registrations. Rough estimates indicate that the amount is relatively small so that forgone revenue in the event of the abolition of the Bills of Sale Act should be insignificant, especially in the light of the cost savings from eliminating the existing Bills of Sale Registry.
3. However, until such data are available it is not possible to calculate whether the Secured Transactions Act will replace lost revenue through charging a flat fee for the registration of security interests, or whether alternative sources of revenue will need to be identified.
4. The team had originally envisaged the new Secured Transactions Registry being housed in the offices of the Company Registrar. The technical expertise already embodied in the Companies Office with the corresponding ability to provide maintenance services, as well as backup facilities, made this a logical choice. However, it might be necessary to house the registry under the auspices of the Ministry of Health, where the current Bills of Sale registry resides.

These are important details that can be resolved as the process of reforming the Secured Transactions framework proceeds.

**Next Steps**

A detailed list of the steps necessary to fully implement the secure transactions reform follows. Exactly how these will be implemented must be planned carefully. It is probably best to divide the steps up into a number of phases, which are outlined at the end of the list.

1. Following the issuing of drafting instructions by the Cabinet, the Discussion Bill must be transformed into a working draft. This process will involve consultations with the Chief Parliamentary Counsel, who must be made aware of developments at every stage of the process. In addition, wide ranging and extensive discussions and consultations must take place between the Ministry in charge of the process and both public and private stakeholders. In addition, the Attorney General must be consulted and given the opportunity to provide comments on the working draft.
2. Once comments have been incorporated the Bill will be revised and transmitted by the Chief Parliamentary Counsel to the Attorney General for final review. The Attorney General will referred the bill to the legislative committee of the Cabinet.
3. Once the legislative committee has reviewed the bill and made any changes that it deems to be necessary, the full Cabinet will review the bill again and once it has approved the draft, it will table the bill for consideration by Parliament.
4. As the bill moves through Parliament it might be considered by a Select Committee from both houses. If that is the case, it will hold hearings on the bill and take testimony from all interested parties. At this stage, it might be necessary for experts to be available to answer questions and to ensure that any changes that have been made do not undermine the economic purpose of the secured transactions Bill.
5. At the same time, provision must be made for the repeal of the Bills of Sale Act and the section of the Companies Act that deals with company charges. This can either be done as an integral part of the new secured transactions legislation or they can be repealed separately.
6. Once the bill has been voted on and becomes law, it would then be referred to as the Secured Transactions Act. However, implementation of the Act must await a registry for recording security interests to become operational.
7. Following the passage of the act, it will be necessary to procure the secured transactions registry, from a software vendor. In order to make the process effective, the specifications for the registry, to the extent possible before the legislation is passed, should be laid out in some detail.
8. Once the registry is installed, existing security interests must be re-registered. The period for doing this should be fairly short because all existing security interests that are re-registered will have a priority date that is effective on the date that the Act was passed. Lenders will therefore be cautious about providing loans secured by personal property because they will be unable to ascertain whether a prior registration exists and will not know whether this is the case until after the expiry of the transition stage during which existing security interests are Reregistered.
9. Implementation of the act is an important part of ensuring that it fulfills its potential to improve access to credit in Jamaica. This will involve training users, lenders, lawyers, and the judiciary in the finer details of the act. It would also be advantageous to hold seminars for potential lenders and also to hold a conference to which foreign bankers are invited in order to publicize the new framework for securing personal property as collateral for loans.

These steps can be divided into a number of phases:

1. Tabling the bill to Parliament.
2. Passage of the legislation and the repeal of the Bills of Sale Act and the Company Charges provisions of the Companies Act.
3. Procurement and installation of the registry.
4. Implementation and publicity of the new secured transactions framework.

**ANNEX A**

**DISCUSSION PAPER**

**DRAFT POLICY SUBMISSION PAPER ON SECURED TRANSACTIONS REFORM IN JAMAICA**

**Paul Holden and Allen Welsh**

**Supported under Contract to the Authors by the InterAmerican Development Bank[[1]](#footnote--1)**

**SUMMARY**

1. Sustained economic growth requires access to credit. Private sector credit in Jamaica, as a percentage of GDP, is less than half that of most countries with the same level of income, which has a strong negative effect on growth, especially for smaller businesses.

2. Access to credit in Jamaica is difficult, in part, due to the antiquated laws that apply to the use of personal property as collateral. These laws, such as the Bill of Sale Act of 1867 and 19th century common law devices, must be reformed in order to increase access to credit and improve the functioning of financial markets.

3. A number of countries around the world have reformed their laws with respect to personal property as collateral by implementing a modern “secured transactions law,” which has proven to be effective in improving access to business and consumer credit.

4. A Jamaican Secured Transactions Act will make it easier for borrowers and lenders to use personal property as collateral in four ways:

* Borrowers will be able to pledge their rights in personal property to lenders as security for loans more easily, flexibly, and inexpensively.
* Secured lenders will be more certain of their right to enforce collateral agreements, not only against the borrower, but also against third parties who may lay claim to the collateral.
* A modern public records system will provide information to the public that will identify and prioritise conflicting claims to collateral.
* Enforcement of collateral agreements, including repossession, will be more effective and efficient.

**BACKGROUND**

Sustained economic growth requires access to credit. By any measure, Jamaica’s financial markets are underdeveloped. At the end of 2008, the ratio of private sector credit to GDP, the best measure of access to finance, was equivalent to about 35% of GDP. Ratios of private sector credit to GDP in high-income countries typically exceeded 150%. Low and middle-income countries have ratios greater than 70%.

Why is access to finance in Jamaica so limited? The law is an important factor. Lenders require collateral in the form of real property or personal property. In the United States, where law on personal property as collateral is highly efficient, 70% of private sector credit is secured by personal property. Jamaica cannot achieve such a result under its current laws.

In Jamaica, personal property typically secures credit under the Bill of Sale Act of 1867, 19th century common law rules on company charges, hire-purchase agreements, and a variety of other legal forms rooted in the common law of contracts.

The use of 19th century legal forms is inefficient and unsuitable for modern business practices and results in many anomalies. Some legal forms discriminate by type of borrower. For example, a company may give a fixed charge or a charge on a floating pool of present and future-acquired assets, while an individual may not take advantage of this powerful finance tool. Some forms, such as hire purchase agreements and finance leases require the lender to take or retain legal title to the collateral, while other forms have no such requirement.

Procedures for the enforcement of lenders’ rights differ depending on which legal form is used. Judicial intervention is required under some forms, and not required under others. The rights of lenders against competing creditors are different depending on which legal instrument is used. Some forms protect lenders from the claims of prior and future pledges of the same property given by the debtor to competing creditors while other forms offer limited or no protection.

Some forms require registration to create and prioritize a charge against competing creditors, such as when company charges and registered bills of sale are used. For other forms, there is no registry.

Registering charges is expensive. Many lenders including those using government-sponsored loan schemes, do not register bills of sale, because of the cost, which adds to the risks of providing credit.

In short, the variety of forms, each with its own peculiarities, imposes risk and legal compliance costs on borrowers and lenders. This cost and legal risk reduces access to credit in Jamaica. Depressed credit markets lead to insufficient funding for investment and entrepreneurship. Lending is primarily confined to well-established businesses and those that own real property. The dynamism needed for growth is lacking because key sectors of the economy find it hard to get financing. Small and medium-sized businesses of all kinds report enormous difficulty accessing finance even though many of them are in a position to offer collateral that would be accepted in other countries. Growers of the world famous blue mountain coffee, a product that can be stored, and for which there is excess demand, cannot use their output as collateral to obtain credit, which adversely affects investment and prevents expansion of the sector.

A solution to the lack of access to finance exists. Many countries around the world have reformed, or are in the process of reforming, their laws governing personal property as collateral. The United States was the first to develop an effective collateral framework, starting in the 1960s on a state-by-state basis. Canada followed beginning in the 1970s. A number of countries in Europe and Asia reformed their laws on personal property financing from the late 1980s onwards. Puerto Rico recently adopted American law on secured transactions. New Zealand adopted reform similar to Canadian legislation in 2002 and Australia followed suit last year. Four Pacific Island nations have recently implemented reforms: Federated States of Micronesia (2006), Vanuatu and the Solomon Islands (2009), and the Marshall Islands (2010). Bills are under consideration in many other countries.

Lending risk falls when the law permits effective use of collateral. Lenders react by offering more credit at the same or better terms. More credit on better terms permits higher rates of investment and more capital per worker, resulting in higher incomes. Modern secured lending law is a feature of virtually all countries where access to credit is easier than it is in Jamaica.

**PROPOSAL FOR POLICY REFORM**

Virtually every successful reform that has taken place over the past two decades has used as models, the laws, principles, and rules adopted in the United States and Canada. A Secured Transactions Act that conforms to these models will promote greater access to credit in Jamaica by introducing best practices in the pursuit of four fundamental principles:

***Principle 1 – Ensure that the creation of security in personal property is simple, flexible, and inexpensive and cannot be challenged readily***

The Secured Transactions Act should permit any individual or firm to create security in any personal property of any nature without restrictions. The collateral may be tangible or intangible and may be held by the debtor at the time of the agreement or acquired at any time in the future. The collateral can include equipment, inventory (stock in trade), accounts receivable, consumer goods, securities, letters of credit, warehouse receipts, bills of lading, crops currently growing or that will be grown in the future, livestock including unborn animals, timber to be cut, minerals to be extracted, and fixtures to real property. The only necessary legal formality is that the borrower signs a simple agreement consenting to the use of the property described in the agreement to secure a loan obligation.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Provide definitions of key terms and appropriate rules of statutory construction.
* Define transactions that are subject to the Act, which may be transactions secured by personal property, transactions where property held by the debtor is subject to rights held by other persons, and other circumstances in which property held by the debtor becomes subject to rights held by others, with or without the consent of the debtor.
* Define the nature of security interests in personal property and obligations that are secured by personal property.
* Provide for the effectiveness of security agreements against the debtor.
* Provide for the duties of secured parties (creditors) when the secured party holds collateral.
* Provide for the rights of borrowers to obtain appropriate information from secured parties.
* Provide the conditions upon which security interests will attach to personal property.

***Principle 2 – Clarify the rights of competing creditors***

The Secured Transactions Act should provide the lender with legal certainty as to its rights against competing claims to the same personal property, anticipating all the commercial conflicts that may reasonably be expected to arise. The Act should address the rights of secured creditors against holders of non-consensual claims such as judgment liens, tax liens, and other liens. Potential conflict among creditors should be resolved through legislative rules that are designed to promote commerce.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Define the methods by which a secured party (the lender) may protect its interests against persons other than the debtor.
* Provide for the rights and obligations of persons who buy or lease collateral.
* Provide for the rights of secured creditors in proceeds of collateral (property that is received in exchange for collateral).
* Provide for the rights of secured creditors against lien holders, and others who gain rights in collateral without the consent of the debtor.
* Provide for the rights of secured parties against mortgagees, in the case of security interests in crops, fixtures on real property, timber, and minerals.
* Provide for the rights and obligations of persons who purchase accounts, chattel paper, and instruments that are collateral.
* Provide for the rights and obligations of parties where accounts are sold or assigned.
* Provide for the rights and obligations of parties where collateral consists of deposit accounts or investment property.
* Provide for other circumstances relating to secured creditor rights against third parties who acquire interests in collateral.

***Principle 3: Use modern technology and simple design to share information***

The Secured Transactions Act should provide for the establishment of a modern, electronic registry for filing notices of collateral agreements. Notices will warn prospective creditors and buyers of prior claims to collateral and, with few exceptions, will establish priority among competing creditors by the order of filing. The registry will not receive loan documents, nor will the registrar verify the accuracy of information or determine its compliance with law. Under a notice filing system, the registry simply records the date and time of the notice, assigns a filing number, bills the filer for the filing fee, and stores the notice for public inspection.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Establish a secured transactions filing office to receive, store, and report information on security interests and liens, in accordance with best practices.
* Limit the information collected to the identification of the parties and a description of collateral in accordance with best practices, in order to protect the privacy of agreements and minimize the cost of the registry.
* Provide for the duration of a notice of a security interest, and the method by which the notice may be continued in duration, amended, or terminated.
* Provide for the limited duties of the filing officer.

***Principle 4 – Enforce property rights efficiently***

The Secured Transactions Act should ensure efficient enforcement of obligations, without resort to the courts whenever possible. Upon default, a secured creditor should have the right to possession or control of collateral and the right to dispose of the collateral in a commercially responsible manner.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Provide that the parties to a security agreement may define default.
* Provide for the right of a secured party to take possession or control of collateral upon default.
* Provide rules that facilitate the ability of the secured party to take possession or control of collateral upon default, and to dispose of the collateral.
* Provide rules governing the circumstances under which the secured party may retain the collateral in full or partial satisfaction of the secured debt, and circumstances under which the debtor may redeem the collateral.
* Impose obligations upon the secured party to act in a commercially reasonable manner when exercising its rights upon default.

In addition, the bill should contain appropriate transition rules, and amendments to related legislation to avoid conflict with existing law.

The Secured Transactions Act will provide for the establishment of a filing office that will replace the Bills of Sale Registry and the part of the Companies Registry that deals with company charges. The Secured Transactions Filing Office will be implemented as a publicly accessible electronic service that conforms to internationally recognized standards of practice. The operation of the filing office will sustain itself with user fees and without taxpayer support.

**EXISTING LEGISLATION AND SECURED TRANSACTIONS REFORM**

A Secured Transactions Act will conflict with the Bill of Sale Act of 1867 and the Hire-Purchase Act of 1974. These Acts should be repealed upon the adoption of the Secured Transactions Act. Consumer protection provisions peculiar to these Acts may be re-enacted in the Consumer Protection Act in an appropriate manner to apply generally to consumer transactions.

The company charge is inconsistent with a Secured Transactions Act to the extent the company charge applies to moveable personal property and fixtures. The Companies Act must be amended to limit the effect of the company charge to real fixed property.

Any legislation that establishes tax liens or other claims in favour of government should be amended to authorize filing of notices of the liens in the Secured Transactions Filing Office, with priority against third parties dating from the date of registration.

Stamp duty cannot be effectively collected or enforced under modern secured transactions law, and therefore secured transactions should not be subject to the Stamp Duty Act. The Secured Transactions Filing Office, however, will generate fees that will help to offset lost revenue. Preliminary calculations indicate that any revenue loss will be very small or could even lead to a small revenue gain with the appropriate adjustment of charges.

**Annex B**

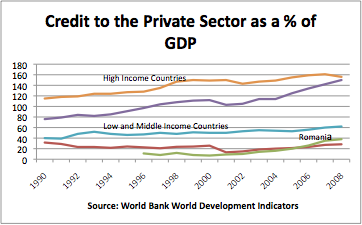
**Reforming Jamaica’s Collateral Framework to Increase Access to Credit: Supplementary Discussion**

## Introduction: Jamaica Has an Underdeveloped Financial System

Although Jamaica has a wide variety of financial institutions, including a stock exchange, finance companies and an insurance sector, its financial system is severely underdeveloped. Domestic credit to the private sector, the best measure of access to finance in developing countries is very low by international standards. The chart shows how Jamaica compares to other groups of countries with respect to the availability of credit. At the end of 2008, the ratio of credit to the private sector to GDP was equivalent to about 35% of GDP. To put this into perspective, ratios of private sector credit to GDP in high-income countries typically exceeded 150% cent. Low and middle-income countries have ratios that are greater than 70%. By any measure, access to credit in Jamaica is limited.

New Zealand

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The result is insufficient funding for investment and entrepreneurship. Lending tends to occur to only well-established businesses and to those persons who own real property. The dynamism that is needed to raise the growth rate of the economy is lacking. In addition key sectors find it hard to get financing. Smaller hotels, growers of the world famous blue mountain coffee, and small and medium sized businesses of all kinds report enormous difficulty accessing finance even though many of them are in a position to offer collateral that would be accepted in other countries.

Jamaica

Limited access to credit extends to other groups as well, particularly women, who are under-represented in formal sector businesses. The reasons for this under-representation are complex. In particular, the current binding association of access to credit for business and the need to pledge property as collateral for business loans has an especially pernicious impact on women entrepreneurs, as will be outlined below.

Yet there are ways of improving the functioning of the financial system that raises the availability of funding. And this does not involve direct government intervention or directed credit, or Development Bank lending, the history of which has been characterized by loan losses and misallocated credit in nearly all countries around the world. Rather it involves modernizing Jamaica’s lending framework in a way that reduces the risk of non-payment of loans. Countries that have done so effectively, have experienced significant increases in credit access for the private sector – the chart illustrates that secured transactions reform in New Zealand that became effective in 2002 and that in Romania that became effective in 2003 have resulted in substantial increases in their private sector to GDP credit ratios.

Modern secured lending systems are a feature of virtually all countries where credit access is much easier than it is in Jamaica. Modernization involves reforming the framework in terms of which collateral is pledged as security for loans, known as the secured transactions framework in terms of which business assets can be pledged as collateral far more easily, with greater reliability and with more certainty of recovery in the event of default than is currently the case in Jamaica. Jamaica needs a well functioning system of secured transactions if access to finance is to improve. This is especially important for women entrepreneurs to enter the formal sector.

In the sections that follow, this paper:

1. Describes the key features of an effective, well functioning system of secured transactions;
2. Analyzes the current system in Jamaica and indentifies the reasons why access to credit is limited, especially for women and others who do not own formal property;
3. Describes some recent reforms in other countries and the impact that they have had;
4. Outlines some of the benefits Jamaica could expect from reform, including how increased access to credit could benefit women and other groups, such as farmers who currently are outside the formal credit system;
5. Makes some suggestions regarding how reform could be implemented.

## Reasons Why Access to Finance is Limited in Jamaica

Why is access to finance in Jamaica so limited? Creditors have no certainty that if a borrower defaults on a loan, repossessing property that was pledged as collateral can be achieved in a reasonable period of time. The reason why banks in Jamaica do not lend is therefore not hard to explain. Lending to all but the wealthiest of borrowers is fraught with risk. As a result, they tend to ask for personal guarantees on bank loans that are backed by real estate. Furthermore, since the process of repossessing and selling real estate assets is costly, the value of the collateral is usually several times the value of the loan, which raises the risk for borrowers. Potential borrowers without titled, registered real estate and other substantial assets cannot find financing. Thus a very large portion of the Jamaican population is cut off from access to financing.

Obtaining information on potential borrowers has also been difficult. To date there has been no credit information bureau at which lenders can check borrowers’ credit histories. However, with the new credit information act about to become law, this will change.

## Why Jamaica Needs Secured Transactions Reform

When the law permits effective use of collateral, the risk from lending falls. Lenders react by offering more credit at the same or better terms. More credit at lower interest rates permits higher rates of investment and more capital per worker, resulting in much higher incomes. Seventy percent of bank loans in the United States are secured by movable assets; at the same time, credit in the United States is about ten times higher relative to GDP than it is in most developing countries.

By increasing access to finance, a legal framework for secured transactions also reduces poverty and reduces wealth disparities, because secured transactions for movable property facilitates greater availability of credit for the poor and for micro and small enterprises.

In Jamaica, commercial banks are unwilling to take as collateral many types of movable assets that are commonly used in countries that have well functioning secured transactions frameworks. In addition, unincorporated entities find it difficult or impossible to obtain loans to finance their businesses. For example, banks rarely lend to sole proprietors, who make up by far the largest category of small businesses in the country. And different types of financing incur different costs, even though the same type of collateral might be used. Equipment financing that occurs through Bills of Sale invokes stamp duty, but under hire purchase agreements, no stamp duty is paid. Each type of security agreement has different legal implications and rules and incurs different costs. Larger financial institutions rarely lend for used equipment, even though smaller businesses might be better off not having to purchase new machinery. This especially harms unincorporated enterprises and women entrepreneurs.

Until the collateral framework is reformed, lack of funding for investment and entrepreneurship will reduce the growth potential of the country and will continue to disadvantage women. When done properly, secured transactions reforms can have significant effects on access to credit.

## Examples of Reform in Other Countries

Some indications of the benefits that Jamaica might expect from a comprehensive secured transactions reform come from examples of best practice reform in other countries. A secured transactions reform in Romania, which occurred in 2003, resulted in filings of security interests rising from less than 10,000 to 600,000 in four years of operation. The number of registered debtors quadrupled, lending rose in both urban and rural areas, and non-bank lending expanded even as a broader range of movable collateral was taken by lenders. Furthermore, the number of lenders registering security interests soared, with many lenders outside the country registering security interests on collateral in Romania. As a result, the ratio of private sector credit to GDP in Romania rose from less than 10% of GDP in 2000 to over 40% in 2008. Over this period, private sector credit, which as a percentage of GDP was 1/3 that of Jamaica before the reform is now higher then Jamaica.

New Zealand, which pre-reform had a collateral framework very similar to that of Jamaica’s, experienced a dramatic expansion of credit available to the private sector following the implementation of what many consider to be the best example of a secured transactions framework within former Commonwealth countries. The New Zealand framework was very similar to that which exists in Jamaica, and also collected stamp duties on registrations of security interests. Following the full installation of the secured transactions system in 2002, the ratio of domestic private sector credit to GDP rose from 70 per cent to over 140 per cent. At the same time, revenue from registrations under the new framework has risen compared to the old system. While many factors obviously affect access to credit, an improved collateral framework undoubtedly made a significant contribution to the increases in both New Zealand and Romania

More recently, Solomon Islands and Vanuatu have implemented secured transactions reform. These have become fully effective only over the past few months. Table 1 shows the effect of the reform in both countries.

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| --- | --- | --- | --- | --- | --- | --- |
| **Table 1: Registrations and Searches of Security Interests Following Reform: Vanuatu and Solomon Islands** | | | | | | |
| **Solomon Islands** | **Sept 09** | **Oct 09** | **Nov 09** | **Dec 09** | **Jan 10** | **Total** |
| Initial Notices | 5283 | 1841 | 18 | 11 | 8 | 7141 |
| Amendments | 41 | 42 |  |  |  | 84 |
| Total | 5204 | 1884 | 19 | 11 | 8 | 7226 |
| Searches | 413 | 867 | 94 | 330 | 274 | 1978 |
| **Vanuatu** | **May – Sept 09** | **Oct 09** | **Nov 09** | **Dec 09** | **Jan 09** | **Total** |
| Initial Notices | 1107 | 43 | 26 | 30 | 32 | 1238 |
| Amendments | 83 | 11 | 1 |  | 1 | 95 |
| Total | 1190 | 54 | 27 | 30 | 33 | 1333 |
| Searches | 1234 | 773 | 202 | 96 | 101 | 2406 |

Data are available for only a few months but they show a substantial number of registrations of security interests *relative to the populations of these countries*.[[2]](#footnote-0) Initially registrations were high because of re-registration of security interests lodged under the old system. The number of searches of the registry is especially encouraging and lawyers report not only that the process is much simpler, but also that many people are doing their own searches obviating the need for legal search fees.

Other secured transactions reforms in the Pacific Islands have also shown promising results. In the Federated States of Micronesia, where a secured transactions reform occurred in 2008, cases of competing priorities among lenders have been resolved without recourse to the courts, whereas in the past such disputes have dragged on for many years. Clarification of the priority of security interests is one of the major benefits of the reform of the collateral framework.

Women have been major beneficiaries of these reforms, which in the case of both Vanuatu and Solomon Islands have been combined with reforms of the Companies Act, which makes it far easier for women to incorporate under a corporate umbrella. Special provisions have been included in this legislation, which will allow women to incorporate easily without the need for expensive legal advice.[[3]](#footnote-1) These are innovative reforms that could have applicability in Jamaica.

## How Jamaican Entrepreneurs, Women and Businesses Can Benefit from Secured Transactions Reform

There are many sectors and groups in Jamaica that could benefit from secured transactions reform. These reforms could have particular benefits for women attempting to enter the formal sector.

The tourism industry is a major sector of the Jamaican economy, which struggles to access credit. However, tourist operators have assets, which can be pledged under a modern secured transactions system. For example, hotels take bookings from operators in the United States and Europe. Typically bookings are made several weeks in advance. While a deposit may be paid, the bulk of the payment occurs after guests have left. Operators expect hotels and other tourist industry service suppliers to give credit terms that range from 15 days to 45 days. Tourism industry representatives indicated that while payment is reliable, it is often late, which puts a substantial strain on the industry’s cash flow. However, these accounts receivable are high quality assets that under the current system are difficult to use. A well functioning collateral framework would allow tourism industry service providers to pledge the receivables and receive advances of between 60 and 80 per cent of the outstanding amounts.

Similarly, equipment dealers that provide machinery and tools to the industrial and agricultural sectors of the Jamaican economy would be able to advance credit more reliably than they can now. The rapid repossession that is possible under a well functioning secured transactions framework would reduce risk of equipment disappearing. While the dealers themselves could take security interests in the equipment, the accounts receivables that extending trade credit provides constitute assets that can be pledged to banks. The result is the lengthening of the credit chain, which increases the number of providers of credit between the source of funds and the ultimate borrower. The longer the credit chain, the greater is the access to finance generally. Furthermore, the closer to the ultimate customer is the company providing the credit, the greater the knowledge of the market being supplied. This knowledge assists in the sale of repossessed assets. It is far easier for a supplier of, say, agricultural machinery, to resell equipment than it is for a bank. Under a well functioning secured transactions framework it would be easier for a bank to finance the dealer and for the dealer to finance customers than at present. Thus as the credit chain lengthens, risk declines, creating a self-reinforcing process for better credit access.

Many sectors that have highly saleable assets will be able to obtain credit, which under the present lending framework is denied to them. Reforming Jamaica’s collateral system will have far-reaching benefits. In the microfinance area, where women currently benefit substantially, increased liquidity could come from microfinance institution pledging their loan portfolios as security in order to increase their loanable funds. This could result in women having greater access to credit than they already do, especially in the areas outside Kingston.

## Features of a Well Functioning Secured Transactions Framework

The description of secured transactions reform outlined in the previous section does not provide any details of what a well functioning collateral system involves. Essentially, a secured transactions framework allows borrowers to pledge movable property as security for a loan in a manner that removes ambiguity regarding exactly what property has been pledged, to whom the property has been pledged, and gives the lender the right to repossess these assets speedily in the event of payment default. To function effectively, the costs involved in utilizing the system should be low, the rights and obligations of all parties to the transaction should be clear, and the procedures to be followed in the event of default should occur rapidly, with a minimum recourse to the courts. Successful secured transactions reform requires that each stage be unambiguous in the law and that transactions costs of using the system are low. Unfortunately, there have been many unsuccessful secured transactions reforms around the world because of the failure to observe each phase.

While every lender will state that the last thing that they want to do is to repossess pledged collateral, the very threat that they can do so provides strong incentives for borrowers to adhere to the terms of loan contracts and to make every effort to repay. The ability of borrowers to pledge property at low cost and for lenders to take collateral and in the event of default, repossess it requires a legal framework that provides for four essential elements.

**Creation.** The law must define the assets that are being pledged, so that a property right is created. It must permit clear and low cost methods for creating this “security interest” on the part of the lender. Secured transactions reform will reduce the uncertainty that lenders have in determining whether assets have already been pledged. In general, people should be free to secure obligations with movable property as they wish, without undue expense and without undue legal restrictions and burdens. A simple agreement, should be all that is necessary to secure an obligation with nearly any form of movable property: tangible and intangible property, present and future-acquired property. The parties may agree that the debtor will remain in possession of the collateral and that the debtor may (or may not) sell, deal in, or otherwise dispose of the collateral with, or without, the knowledge or consent of the creditor. This is important when, say, inventory is used as collateral. Typically the debtor will need to sell the inventory, and purchase new stock, i.e. “rotate his/her stock” during the life of the loan. The agreement needs to allow inventory to be sold and newly purchased goods that move into inventory to become collateral, without the necessity of drawing up a new agreement. This procedure is known as a “floating charge” and applies to any assets that are constantly changing, including debtors or accounts receivable.

**Priority.** The law must set logical and clear priorities among the different claims on pledged assets. It must set a time of registration of security interests, from which a right will prevail against other claimants to the same property. “Secured” lending is less than secure when previous creditors already have rights in, and future creditors could acquire rights in the collateral. The value of collateral is diminished when others may assert claims against it, including judgment holders who obtain writs of execution, tax authorities that can seize collateral based on a tax lien that is unknown to the lender, and bankruptcy trustees.

Further, since the collateral may be sold by the debtor, or otherwise disposed of, there must be rules that determine what rights do the buyers and other transferees acquire in the collateral. The rules should specify whose rights have priority over the rights of others, and under what circumstances. Secured transactions law clarifies these issues in the form of priority rules that specify the rights of borrowers, lenders, and third parties under a variety of commercial situations.

**Publicity.** The law must provide a practical, effective and sustainable system for publicizing rights so that other potential lenders can determine whether an asset has already been pledged to somebody else. Therefore a system is needed that publicizes such pledges. It allows the creditor to file a notice that specifies the parties to the loan agreement and describes the collateral that has been pledged. In well functioning modern systems, the publicity merely indicates, in an easily searchable database, that a security interest exists. Filing, therefore, need not take on any burdensome formalities and need not be subject to the scrutiny of a state agency. The notice establishes a priority right to collateral in the event of a dispute among creditors and other third parties, but the actual status of property rights to collateral are to be found only in the security agreement itself.

The notice serves only two purposes. First, the notice warns prospective creditors and buyers of possible prior security interests in the debtor’s property. Second, the date of the filing of the notice indicates the date by which competing claims to collateral are measured. The first filer has first priority in the event of default. The description of collateral in the notice may be general in nature, but must be sufficient to apprise prospective lenders and buyers of collateral of the possible status of the debtor’s property. With modern technology, notice-filing offices are often operated electronically, which gives speedy internet access to information regarding the filing of security interests and provide fast, efficient, and accurate service to borrowers and lenders. As a result, ambiguities arising from conflicting claims are substantially reduced.

**Enforcement**. The law must set out a workable system for enforcing lenders’ rights, including the repossession and sale of the property in the event of default. The success of secured transactions law depends upon the creditor’s ability to enforce speedily its rights. The creditor must have the right, upon default, to take possession or control of the collateral and to sell or otherwise dispose of the collateral in an economically efficient manner. A sale may be through public or private facilities. Collateral may be disposed of in whole, or in parts. In appropriate circumstances, the collateral may be leased or licensed. Regulation of the creditor’s efforts to obtain value from collateral must be sensitive to the type of collateral and the commercial circumstances in which the creditor must act.

In many circumstances, it should not be necessary to go to court to repossess and sell property in the event of loan default. There is no need for judicial intervention when a secured creditor disposes of collateral that is in the creditor’s possession or control. Creditors often maintain possession of documents of title, warehouse receipts, and negotiable instruments. Upon default, the secured creditor should have statutory authority to sell or lease the collateral. Similarly, upon default, a secured creditor should have statutory authority to collect on accounts receivable that have been pledged as collateral, without judicial permission. Perhaps only in the case of a non-cooperative debtor in possession of tangible collateral is judicial intervention necessary, and then for the purpose of repossessing the property and giving it to the creditor.

If the secured transactions framework does not account for these phases, then both bank and non-bank lenders are reluctant to lend and financial market development is hindered. For private lending to serve borrowers' needs, the legal and institutional framework needs to assure private lenders about one thing: that the borrower will pay. A country's legal framework for debt collection provides that assurance. When the law permits effective use of collateral, the risk from lending falls. Lenders react by offering more credit at the same or better terms. More credit at lower interest rates permits higher rates of investment and more capital per worker, leading to much higher incomes.

## How Does the Collateral System Work in Jamaica?

Jamaica’s collateral framework functions poorly, is costly and uncertain. This is the prime reason why access to credit in the country is limited. What are the reasons for the current inefficient and high cost system? The discussion that follows outlines the problems within the context of the framework outlined in the previous section.

***The Creation of Security Interests in Jamaica is Complex***

A multiplicity of laws governs the creation of security interests in Jamaica. At least five separate legal forms are in common use in Jamaican business practice today. These are:

1. Hire-purchase agreement
2. Finance lease
3. Bill of sale
4. Fixed charge
5. Floating charge

In addition, other ways of pledging property, that arise form common law forms, are used from time to time. These are:

1. Pledge
2. Consignment
3. Assignment

**Some Features of Different Types of Security Interests in Jamaica’s Current System**

*Each form has its own peculiar trappings*. As a result, it is almost always necessary to employ a lawyer to ensure that the particular agreements in terms of which collateral is pledged is watertight, but even so the complexity of the system makes it far from certain that in the event of default, the agreement will stand up in court. The system results in unnecessary expense, whether in the formalities of creating security, the formalities of protecting security interests against third parties, or in the trappings of enforcing security interests against the debtor upon default.

*In Jamaica the type of debtor determines the way that collateral is pledged*. For example, only an incorporated company can give security under a company charge. Individuals may not take advantage of this powerful tool for financing using as collateral existing equipment, inventory, receivables, and other intangible assets. Individuals must resort to devices considered by creditors to be riskier (and therefore more expensive) or less convenient. An individual who tries to finance business receivables, for example, would probably need to resort to the common law assignment, which gives the assignee (the creditor) no protection against a bankruptcy trustee or against prior assignees. The upshot is that the floating charge, which is among the most powerful asset-based lending techniques available, it is out of the reach in Jamaica of all except those who can afford to incorporate and maintain corporate status.

*Currently, the type of collateral determines how it can be pledged:* Under the existing collateral framework in Jamaica, a financial lease, hire purchase arrangements, and bills of sale may only be used to finance new equipment. A floating charge or a consignment may be used for inventory financing. Floating charge and assignment can be used for receivables financing. Fixed charges, bills of sale, and even pledges may be used when existing equipment is to serve as collateral, while a pledge is quite common where negotiable instruments serve as collateral. Thus the system is complex, with no uniformity of treatment of different types of assets being pledged.

***Determining Priority is Difficult***

Lenders, have difficulty determining whether assets have already been pledged as collateral because there is no public notice of the vast majority of secured transactions in Jamaica. The lack of notice constitutes a trap for lenders and for buyers of goods. In Jamaica, the law on secured sales contracts includes no public notice whatsoever, unless the property happens to be a titled property for which a notice of lien is stated on the title document. The common law on assignment and consignment also carries no public notice component. Secured sales contracts, in the form of financial leases, hire purchase agreements, conditional sales contracts, etc., are very common. By comparison, there are only a few hundred registered company charges per year.

***Unpublicized secured debt is the norm in Jamaica*.**

Uncertainty arising from the registration of charges under the Companies Act: There is public notice of a limited number of secured transactions. Though largely governed by common law, company charges are subject to statutory rules on registration under the Companies Act. A company charge registered within 21 days of the charge agreement enjoys priority from the date of agreement. This, however, is a troubling provision that creates the possibility of a lien that may be granted elsewhere during this three-week period. In some cases the situation is even worse because the registry of charges often takes days or weeks to publish notice of the charge, back-dating the date of registration to the date of receipt of the charge document. If a lien is given to somebody else [illegally] during this period, the possibilities for disputing priority are substantial.

Uncertainties arising from the registration of charges under the Bill of Sale Act of 1867: the Office of the General Registrar records the details of bills of sale that can serve as security in a number of transactions.

Users report that the records of the office are not organized in a manner conducive to public search. Searching the records is therefore time consuming and costly and risks of error are high. These costs are passed on to borrowers, raising the costs of credit.

***Problems with Enforcement of Security Interests***

Jamaican secured creditors face their most difficult challenge where tangible collateral is in the possession of a non-cooperative defaulting debtor. In this case, creditors need to use the judicial mechanism to obtain possession of the collateral and legal authority to dispose of the collateral under judicially supervised seizure and sale. Both under the Companies Act and the Bill of Sale Act, the process is time consuming and costly. By the time the assets that have been pledged have been seized and sold, months, or even years can have passed. The value of the assets is therefore limited as collateral and lenders typically heavily discount it.

However, Jamaican law does allow for a number of streamlined enforcement measures that apply to some types of collateral, in particular negotiable securities. Upon default, creditors in possession of instruments may negotiate them, creditors in possession of security certificates may market them, creditors in possession of goods may dispose of them, and creditors may proceed directly against receivables.

Nevertheless, for most classes of movable assets, the bottom line is that the system of enforcement is complex and costly. The table on the previous page summarizes the various ways to repossess assets pledged as collateral. As the diagram shows, complexity and uncertainty in the Jamaican secured transactions system is the norm. The result is higher risk for lenders, higher costs for borrowers and reduced access to credit that impacts in particular smaller businesses and those who do not have titled registered property.

***High Transactions Costs***

Taking collateral under the existing framework incurs high transactions costs that raise the expense of borrowing and reduce competition in the banking system. These costs arise from a number of sources.

Since each loan agreement that involves collateral requires review by a lawyer, legal fees can be substantial. Some security documents necessitate the payment of stamp duty, particularly on the registration of company charges and bills of sale. Stamp duties on assets pledged have a pernicious impact on the cost of access to finance. First, they constitute a tax on borrowing. Second, they increase transactions costs by requiring extensive bureaucratic procedures to be followed. Third, they apply to some types of registration of collateral but not to others. Fourth, they make it costly to switch lenders because new loan documents need to be drawn up and stamp duties paid. Fifth, borrowers indicated that they structured their loans to avoid stamp duty. For example, they use hire purchase arrangements, which are not subject to stamp duty. In addition, practitioners report that stamp duty is frequently not paid until enforcement is against the debtor is sought. In many cases, therefore, it goes unpaid altogether. Another avoidance measure is to use a loophole to minimize or avoid the tax on company charges by subordinating the company charge to a small or token mortgage (the first transaction is taxed, the second is not). Furthermore, stamp duties on the registration of security interests are a small and may not cover the costs of collection. For all these reasons, stamp duties should be abolished.

The existing system needs complete, comprehensive reform through passing a new secured transactions act, the establishment of a registry of security interests and the abrogation of existing legislation governing the creation and enforcement of security interests. Features of the new law should include:

1. Security interests in movable property should be created in a simple agreement that need not use any special terminology and need not be on or in any particular form. Anyone, corporate or individual, should be permitted to give or take security in movables of any nature. In other words, there will be no distinction in the process between companies, sole proprietorships, individuals, producers or consumers. The collateral may exist at the time the agreement is made, or it may be anticipated to arise in the future [in the case of taking liens over future crops, for example]. Collateral may be tangible or intangible and the secured obligation may be monetary or non-monetary. It may be expressed in any currency. It may be contingent or conditional.

**Box 1: The Use of Warehouse Receipts in Financing of Agriculture in Jamaica**

*An important part of financing available to agriculture in developed economies arises from the use of a financial instrument known as a warehouse receipt. Under this system an accredited warehouse takes in agricultural products, vouches for its quality and existence, and issues a receipt to the owner that becomes a negotiable instrument. Under a well functioning system of secured transactions this receipt can then be used as collateral. No such system exists in Jamaica but if it were to be established as part of a secured transactions reform it has the potential to solve a number of problems that exist in the financing of agriculture.*

*Jamaica’s most famous agricultural product is Blue Mountain coffee and is in strong demand worldwide. It can be sold easily and there is an ongoing market. This makes it excellent collateral. Since this coffee can be stored for up to two years without any loss of quality, there is the potential to improve the financing of the sector and perhaps develop a system of self-insurance. If negotiable warehouse receipts could be used as collateral, growers would have the opportunity to store their coffee after it is harvested, obtain financing, and keep back some of their production as a hedge against price fluctuations or even destruction by hurricanes. Since the warehouse would guarantee the existence and quality of coffee, lenders could advance funding knowing that a product that is easily salable on world markets backed it. A reformed secured transactions system would ensure easy repossession and sale in the event of default.*

*Furthermore, since the harvesting season is long, if growers were able to store their coffee in an accredited warehouse and obtain funding as they do so,* *there would be far more funds available to invest back into the industry to ensure continued high standards. In particular, if the warehouse checked quality as the product came in, there would be strong incentives to keep standards high.*

*Once the system was established for the coffee industry it could be extended to other agricultural products that are not immediately perishable.*

1. The new law should establish the clear priority rule that the first to file notice in the Notice Registry has priority over other creditors.
2. Tax liens must be filed in order to obtain priority over other secured creditors. Existing legislation must be reviewed carefully to identify articles that would conflict with new legislation. These should be abrogated in the new law.
3. Concurrently with the new law, an electronic filing archive must be established, in which all security interests will be registered.
4. No stamp duties should be payable on any filing of security interests.

A system of warehouse receipts could go a long way towards providing some industries in Jamaica with finance that is currently unavailable. This reform will contribute towards establishing a system of de facto insurance. [See box on previous page].

**Implementing Secured Transactions Reform in Jamaica**

Discussions with stakeholders have begun. Consultations reveal that the concept of secured transactions reform is not well understood. Users of the existing system have adapted to it and are generally not well informed regarding alternatives.

Another problem is that the constituency that the existing system locks out – smaller businesses, farmers, women and sole proprietors are poorly represented in the higher echelons of Jamaica’s business associations. Nevertheless, once the characteristics and advantages of a reformed system were discussed in detail, those interviewed became enthusiastic regarding the usefulness of a well functioning secured transactions framework.

Furthermore, at the political level there is strong support for this reform. As the process commences in mid-2010, further consultations and discussions will be necessary to broaden awareness of the advantages of a well functioning secured transactions framework. As the process goes forward, the following steps are required.

**Widespread discussions of legislative options must take place.**  This could require further briefing papers prepared for the Minister of Finance, the Bank of Jamaica[[4]](#footnote-2) and other stakeholders by international and Jamaican experts. In countries where successful secured transactions reforms have occurred, the involvement of international lawyers and economists has proved to be important for the development of an effective reform. The subject matter is specialized and complicated and both legal and economic considerations must be taken into account. While the competence of Jamaican lawyers is high, the details of such a reform require expertise based on knowledge of best practices around the world. The experts should be guided by an advisory group made up of Jamaican lawyers, business people, government officials, small business representatives, microfinance representatives, farmers, women’ groups and other stakeholders.

**Abrogation of conflicting laws:** Since there are a number of laws that currently govern the pledging of movable property in Jamaica, the new secured transactions legislation must abrogate the relevant clauses of existing Acts, some of which were identified in preceding sections of this paper, in order to remove potential conflicts with the new legislation. This is essential in order to ensure that there is no confusion at any part of the process for pledging movable property. Part of the task of implementing reform will be the identification and abrogation of possible conflicts.

**Revenue considerations:** Rough calculations seem to indicate that there could be a net revenue gain. The following table shows the number of bills of sale recorded and the number of company charges registered over the 199 – 2007 period.

|  |  |  |  |
| --- | --- | --- | --- |
| REGISTRAR GENERAL'S DEPARTMENT | | | |
| NUMBER OF BILLS OF SALE RECORDED | | | |
| BETWEEN YEARS 2001/2-2007/8 | | | |
| 2001-2002 |  |  | 6,095 |
| 2002-2003 |  |  | 7,678 |
| 2003-2004 |  |  | 6,491 |
| 2004-2005 |  |  | 5,897 |
| 2005-2006 |  |  | 5,897 |
| 2006-2007 |  |  | 9,895 |
| 2007: Jan. - Sept |  |  | 6,016 |
| TOTAL |  |  | 47,970 |

|  |  |
| --- | --- |
| Company Charges Registered | |
| 1999-2000 | 1098 |
| 2000-2001 | 1011 |
| 2001-2002 | 780 |
| 2002-2003 | 634 |
| 2003-2004 | 501 |
| 2004-2005 | 474 |
| 2005-2006 | 563 |
| 2006-2007 | 578 |
| 8 Yr. Total | 5639 |

Stamp duty is 3% of the value of the registered assets. If we assume that the average value of a bill of sale is US $5,000, the total revenue from Bill of Sale registration would be about US $1 million per year. For a US$ 50,000 average company charge over the past 8 years, foregone revenue would be about the same, for total lost revenue of about $2 million per year.

Set against this would be a registration fee of US$10 – US$20 for all security interests registered, including automobiles. Rough calculations suggest that automobile registrations amount to about 25,000 per year alone. Any revenue loss is likely to be minimal and there could even be a revenue gain.

**A plan for the implementation of an electronic filing archive must be prepared.** Planning may begin when there is consensus on the details of the legislative proposal with respect to the operations of the filing archive, although definitive plans for implementing the registry cannot be finalized until the substance of a legislative enactment is known.

We recommend that all existing security agreements be required to register under the new secured transactions framework, with a window of 3 months. During the transition period, lenders with existing security interests can register under the new law. They will have priority that is effective on the date that the law was passed. The longer the transition period, the greater will be the negative impact on granting credit, because lenders making new loans cannot be sure that another lender will not register a prior security interest that has priority.

It must be emphasized that we are proposing a notice archive, not a registry. Documents will not need to be submitted to whoever administers the archive – documentation issues will be the concern of the lender and the borrower and registration in no way warrants that the personal property exists nor that it actually belongs to the borrower. This is an issue for the lender to resolve. The notice archive for Jamaica will only indicate that a lender has taken a security interest in a borrowers movable property. It will provide a broad description of the property and either the company name, or a means of identifying individual borrowers. This could take the form of an identity number. The notice will not specify how much has been borrowed.

**As the legislation approaches becoming law, an implementation plan must be prepared**. Passing legislation is insufficient – training of all the parties involved in the process is necessary in order to make sure that the system operates effectively. In addition, a publicity campaign will be necessary to acquaint potential users of the advantages of the new process and how it may be accessed.

**Conclusion**

Jamaica has experienced low growth for decades. Part of the reason is the lack of availability of finance for investment and growth. In addition to limiting growth, it has also disadvantaged a number of groups, especially women attempting to enter the formal economy. This paper has described in some detail the potential benefits of a secured transactions reform that will increase access to credit. Implementation of the reform without delay will bring substantial benefits.

**ANNEX C**

**AN ANALYSIS OF SECURITY INTERESTS IN PERSONAL PROPERTY: OPPORTUNITIES FOR REFORM IN JAMAICA**

**Discussion Draft**

**Preface**

This discussion paper is intended to add to research and public discussion about Jamaican law on lending secured by personal property. The discussion paper may be useful as Jamaicans discuss proposals for legal reform. The purpose of secured lending legal reform is quite simple: to promote commerce by facilitating the business and consumer credit necessary for economic growth.

The paper reviews existing law and practice, examines reform efforts in other countries that have developed and strived for best practices (large and small, rich and poor), and concludes that substantive reasons to object to Jamaica implementing a secured transactions reform.

While the paper analyses the law of Jamaica, its organization and analytical methodology deliberately follows, in large part, the British Law Commission’s Consultation Paper #64 (2002), Registration of Security Interests: Company Charges and Property Other than Land. The United Kingdom has been involved in similar public discussions for some time, although no reform has as yet been implemented, to a large part as a result of opposition from the legal profession.

Several members of the Commonwealth have moved ahead of the U.K. in adopting comprehensive legal reforms including Canada, New Zealand, Australia, Vanuatu, the Solomon Islands, and others.

The conclusions presented here are not necessarily those of the Inter-American Development Bank or any Ministry, Department, or Agency of the Government of

Jamaica. No attempt is made here to speak for them.

**Introduction**

As in all other countries, credit is of great importance to businesses in Jamaica, whether companies, partnerships or proprietorships. However, access to credit is limited, which is one of the reasons for the low growth of the economy.

Lenders often demand collateral in an attempt to ensure that borrowers pay them before other creditors, and to protect against non-payment. Where personal property (property other than land) serves as collateral, the assets may be pledged, mortgaged or charged, or may be the subject of various other legal transactions that are not currently recognized by the law as creating a security but that serve the same purpose, such as finance leases, hire-purchase agreements and conditional sales. The assets may be equipment, inventory, or accounts receivable or other rights to payment.

The oldest form of security in personal property is the pledge. The lender takes possession of the borrower's property until the debt is discharges. This form of security, however, is rarely suitable in modern business and consumer credit transactions.

Modern commerce requires that lenders find satisfaction in collateral that remains in the possession of the debtor while the obligation is discharged. But non-possessory collateral arrangements pose problems. Collateral in the possession of the debtor may mislead third parties (e.g., prospective creditors and buyers) by creating the impression that the debtor owns the property outright (the impression of "false wealth"). Second, in the event of multiple charges on the same asset, disputes arise over the rights of multiple creditors to satisfy their claims through liquidation of the charged assets. In short, when collateral is held by debtors, creditors need (1) ***notice*** of prior charges and (2) assurance of ***priority*** in the collateral in the event of default.

Problems of notice and priority are addressed to a limited extent where a transaction is subject to the Bills of Sale Act (1867) or the common law on company charge and the company charge registration provisions of the Companies Act. Registered bills of sale and company charges provide information to prospective creditors and provide schemes for priority.

Unfortunately, registered bills of sale and company charges do not cover the entire landscape of transactions secured by personal property, nor do they address many important problems associated with secured transactions.

* Title retention devices such as hire-purchase, finance lease, conditional sale are not subject to bill of sale or company charge registration.
* Transactions where property of buyers or sellers is in the possession or control of another person are not subject to bill of sale or company charge registration. These transactions include lease, consignment, and accounts that are assigned without recourse.
* Fees, taxes, legal compliance costs, and enforcement costs with respect to these transactions are high enough to deter commerce significantly.
* The company charge, which permits the charge of floating pools assets including future-acquired assets, is not available to proprietorships and partnerships.
* Problems associated with buyers of collateral are not adequately addressed by legislation or common law.

**Reforms in Other Countries**

Although several countries, including many not cited here, have undergone significant reform, the bulk of the experience under reformed law has been in the United States, Canada, and New Zealand.

***The United States of America***

Prior to the 1960s, the various states of the U.S. were in a similar position to that faced today in Jamaica. Lenders and borrowers had a number of legal forms to choose from. While registered bills of sale and company charges were not part of the law of the states, legal forms included pledge, chattel mortgage, and title retention devices, trust receipts, factor's lien, field warehousing, and schemes for using intangible property and accounts receivable as security. As in Jamaica, the formal rules for creating security were different from form to form, and enforcement rules varied from form to form. Each form had its own strengths and weaknesses with respect to notice to prospective creditors and priority among competing creditors. Compliance and enforcement costs were high. Economists and legal experts determined that commerce was deterred by the high cost of maintaining the legacy of legal forms designed for commercial needs of past generations.

The Uniform Commercial Code (UCC) was developed in the 1950s and 1960s. Article 9 of the UCC is devoted to secured transactions, transactions where personal property secures obligations. The four principles of reform contained in UCC Article 9 are as follows.

* The various forms of security are replaced with a "unitary" security device. Quite simply, the UCC permits any person (whether an individual or a corporation) may secure an obligation by giving to any other person a "security interest" (or charge) in personal property of any nature, tangible or intangible, and including property that may be acquired by the debtor in the future.
* The UCC recognizes that the interests of third parties may compete with the interest of the secured lender in many circumstances. The debtor may sell the collateral to a buyer. The debtor may give a security interest in the collateral to other creditors. Liens may arise in the collateral in favor of tax authorities or judgment holders, who may try to seize and dispose of the collateral. The UCC anticipates these conflicts and sets forth clear priority rules to resolve the disputes, giving secured lenders certainty that promotes lending.
* A "notice filing system" is introduced to replace the registries that were previously used to create charges. Under the UCC, the security interest is created merely by agreement of the lender and debtor and is enforceable against the debtor without registration. Registration merely provides notice – a warning – to prospective lenders and buyers that the property described in the notice may be subject to a security interest. In the event of competing claims to the same collateral (whether asserted by a buyer, competing creditor, or lien holder), the date of registration may serve as the date of priority in the collateral for the purpose of resolving the dispute. Usually, the first to file a notice has priority over third parties who have not filed a notice or who file notices at a later date.
* Upon default and no matter what the form of transaction, the UCC grants the creditor the right to take possession of collateral. The creditor may take possession of collateral without judicial intervention if it is possible to do so peacefully. The creditor also has the right to dispose of the collateral without judicial intervention. The creditor has a duty to dispose of collateral in a commercially reasonable manner (in general, the creditor must dispose of the collateral in arm's-length transactions with the care that would be exercised if the collateral were owned by the creditor)

With the exception of Louisiana (a civil law jurisdiction that adopted UCC Article 9 in the 1980s) all states of the U.S. adopted the UCC by the end of the 1960s. Amendments were suggested and adopted by most states in 1972, and a revision of Article 9 was completed in 2000. The legislation is widely regarded as highly successful in its purpose to promote commerce.

***Canada***

Nine of ten Canadian Provinces and the three territories have adopted "Personal Property Security Acts" (PPSAs). The PPSAs adopt notice filing systems for secured transactions along the lines of the U.S. Uniform Commercial Code. Canada introduced notable modification to the UCC to accommodate auto finance, which is outside the scope of secured transactions law in the U.S. (Quebec, a civil law jurisdiction, has also adopted reform to its systems for personal property finance, though not as extensive in scope as found in other provinces and the territories.) 16 The PPSAs are based on the Model Personal Property Security Act which was adopted by the Canadian Conference on Personal Property Security Law. The Model PPSA was in turn based upon UCC Article 9. The Saskatchewan Personal Property Security Act 1993 ('SPPSA') is said to be virtually identical to the Model PPSA. Like the UCC, the PPSAs:

* Create a unitary security interest by which any person or company may grant a security interest in any type of personal property to any other person;
* Resolve disputes between secured parties and third parties such as buyers and competing creditors through a comprehensive system of precisely tailored priority rules.
* Establish a simple notice filing system that does not create a charge in property but merely (1) provides notice of the possible existence of prior security interests and (2) establishes a registration date that may be the priority date by which competing claims are measured;
* Introduce more efficient means for the enforcement of security interests. 18 Canadian PPSA registrars were the first to introduce electronic registries by which lenders may register notices themselves and without submitting forms to a physical registrar. Electronic registration is now nearly universal in Canada.

***New Zealand***

The New Zealand Personal Property Securities Act has been in effect since 2002, replacing the company charge registry and other registries relating to personal property. The New Zealand PPSA follows the Saskatchewan and New Brunswick PPSAs in large part, though there are notable differences. The four major principles of the UCC and the Canadian PPSAs are prominent in the New Zealand PPSA. 20 The New Zealand PPSA registry was established from the beginning as an entirely electronic registry, with no paper forms accepted by the registry.

***Australia***

On May 1, 2010, a transition period began leading to full implementation of the Australian Personal Property Securities Act which reforms personal property security law in Australia along the lines of U.S., Canadian, and New Zealand reforms.. The PPSA will be fully in force by May 2011.

The Australian PPSA establishes a notice filing system to replace a variety of antiquated registration systems. The following registries are combined, many of which operated independently in each of the Australian provinces and territories: (1) Registry of Company Charges, (2) Registry of Cooperative Charges, (3) Registry of Encumbered Vehicles, (4) Bills of Sale Register, (5) Register of Liens on Crops, (6) Registry of Ships, and (6) the Fisheries Registry.

***Other systems***

After extensive study, the United Nations Commission on International Trade Law (UNCITRAL) concluded that legal reform promotes secured most effectively when the law achieves general principles of predictability and transparency with regard to the creation, perfection, and enforcement of security rights in personal property, no matter how the agreement is denominated and including the possibility to encumber assets acquired b the debtor after the date of the security agreement. In furtherance of its conclusions, UNCITRAL published on July 10, 2010, its Legislative Guide on Secured Transactions, addressing all the issues that have been central to reform in the U.S., Canada, and subsequent jurisdictions.5 24 In 2001, a conference organized by the International Institute for the Unification of Private Law ('UNIDROIT') and the International Civil Aviation Organization ('ICAO') concluded a Convention on International Interests in Mobile Equipment and a Protocol to the Convention on International Interests in Mobile Equipment.

**Aircraft Equipment**. The convention establishes an international legal order for the creation, registration and enforcement of security and title retention interests (including leasing agreements) in high value, uniquely identifiable mobile equipment. The Convention applies to interests in airframes, aircraft engines, helicopters, railway rolling stock and space assets. These interests will be protected by registration in an international public registry. The registration system, which will be operational 24 hours a day and will be wholly electronic, will allow for the registration of international interests, and assignments and subordinations of such interests, as well as certain other types of interests. Registration will be against the asset, not the debtor. The holder of a registered international interest will have priority over the holder of a subsequently registered interest and over unregistered interests, whether or not registrable.6 Fifty-four nations have signed the convention, including Jamaica.7 Work continues in relation to the establishment of the International Registry. 25 After the fall of the Berlin wall, a number of countries in Eastern Europe reformed law on transactions secured by personal property. The European Bank for Reconstruction and Development, the United States Agency for International Development, and other international aid organizations assisted in evaluating legislation, developing reform proposals, and modernizing registries.8 26 Recently, the Asian Development Bank has sponsored secured transactions reform programs that have led to the enactment of comprehensive legislative reform and the institution of electronic registries in the Federated States of Micronesia, the Republic of the Marshall Islands, Vanuatu and the Solomon Islands.

**Summary of Conclusions**

The current system for registration of company charges and bills of sale has a number of serious weaknesses and reform is needed with respect to (1) the registration process and (2) priority rules as they relate to registration. Jamaica can easily take advantage of a notice-filing system (explored in Part IV) to address the weaknesses of the current registration systems.

***Registry reform*** A notice filing system would make it substantially easier for companies and their creditors to give public notice of security interests. A single and short form, offered via the Internet, would replace the existing and cumbersome manual processes.

Notice filing systems relieve registry staff of the burden to check information in the notice. The register can easily be searched online. Less information would be submitted, but there would be no reduction in the practical value of the register as a source of information on the possibility of existing claims to company assets.

A reformed registration system can provide far more information about a much wider range of transactions than is possible under current law and practice. The current list of registrable charges is far too limited and misleads buyers and lenders. For example, hire purchase and finance lease agreements constitute financed purchases, yet existing registries and priority rules do not cover them. A notice filing system should cover all transactions where the effect is to create security in personal property, and other transactions where a person holds property owned by another under a sales agreement not currently subject to registration.

***Priority reform***

Under current law, priority disputes among competing creditors are determined by distinctions based on legal technicality: is the charge fixed or floating, crystallized or not crystallized, legal or equitable, subject to a statutory lien that enjoys super-priority, and so on. The date of registration is only one factor in determining the priority of a charge. It makes little sense to rely on legal formality to determine priority. A system of priority rules based generally on the date of registration will promote commerce more effectively than current rules. 32 The law can be fairer to borrowers and creditors where a seller or lender has provided a company with credit to purchase new assets. Under current law general creditors may, at times, have superior claims over those who provide financing to procure new equipment. "Purchase-money-interests", if given priority over general creditor claims, will encourage commerce by facilitating finance for business equipment and inventory.

***Individual (non-corporate) debtors***

As ineffective as current law and registries are with respect to company charges, current law is even less efficient with respect to individuals who create security in personal property, whether for business loans or consumer loans. Bills of Sale and hire-purchase agreements are the primary legal forms used by individual borrowers who secure obligations with personal property. The cost of using the Bills of Sale Act is high, deterring many loans and encouraging non-compliance with the law. Moreover, the Bills of Sale Act does not permit non-corporate debtors to create floating charges and for no apparent reason. Specific charges and general charges over existing and future property should be available to proprietors and partnerships as well as to corporate debtors. The advantage of this reform may be particularly advantageous in some forms of agricultural finance

***General provisions for creating and enforcing security in personal property***

As differences between legal forms are extinguished for the purpose of registration and priority, a common set of rules governing the creation, attachment, and enforcement of security interests will lower costs for borrowers and lenders and promote economic activity.

**PART II Security Interests and Company Charge Registration**

**Introduction**

This Section describes types of security that can exist over property other than land, whether the security is created on a consensual basis or arises by operation of law, and then examines the registration of company charges and the role registration plays in the priority of competing charges and other claims over the same asset.

**Security Interests:**

***The purpose of security:*** A creditor who takes security hopes to improve the chances of payment or performance under a contract with the debtor. The threat of enforcement against the collateral may be enough to persuade a defaulting debtor to pay. If the debtor cannot pay, the secured creditor may rely on a claim to assets more favourable than an unsecured creditor enjoys, based on the debtor's prior transfer of property rights to the creditor. The secured creditor may be able to prevent an unsecured creditor from seizing assets, if the secured creditor as collateral has properly taken those assets. Another advantage is, in some cases, the availability of non-judicial remedies. In the event of the company charge, the right to take control over company assets is an advantage.

***Creation, attachment and perfection:*** These concepts are not in common use but they are not new to the common law of personal property. The creation of a security interests refers simply to the debtor's grant of a security interest in a security agreement. The agreement itself is enough to create the interest, without registration or other formality. The security interest is enforceable against the debtor when it attaches to the property, which may occur later, and requires that the debtor obtain rights in the collateral and that the creditor give something of value to the debtor. Perfection occurs when third parties are also bound by the agreement, which usually requires that they have some notice of the agreement (hence the notice filing system), unless the creditor has taken possession of the collateral (e.g. as with the pledge).

***Traditional forms of security:***

***Pledge:*** A pledge is a bailment of an asset for the purpose of security. The object of the pledge may be goods, documents of title, negotiable instruments, and other forms of tangible property. The security interest attaches to the goods and the security interest is perfected against third parties when the creditor takes possession of the pledged property. The pledgor (debtor) continues to own the property, but delivery to the pledgee (secured creditor) transfers the implied power to sell the property on default (or negotiate the instrument) and apply the proceeds to the secured debt. In the meantime, the pledgee holds the property in trust for the pledgor, and has a duty to take reasonable care of the property. 39 There are many inconveniences and inefficiencies associated with the pledge. The pledgee must store and maintain the pledged property. The pledgor forfeits the ability to use the property. In many commercial transactions, the pledge has no useful application.

***Lien:*** A lien is a right to hold property until an obligation is discharged and may arise by the agreement of the debtor or by operation of a statute or common law. Unlike the pledge, the property is not transferred for the purpose of security. Someone who holds the goods until payment is made for the repair service may deliver the goods to a shop for repair. A lien on the goods arises by operation of law and generally lasts until the debt is discharged, provided that the person who holds the lien also holds the property. Also unlike the pledge, there is no implied power to dispose of the property, though a statute, such as statutes creating liens in favour of tax authorities or other government agencies, may grant such a power.

In Jamaica, an unpaid seller holds a lien on goods sold until payment is received under the Sale of Goods Act. Various tax statutes create liens that arise by operation of law.

***Mortgage:*** A mortgage on personal property is a transfer of a property right to the creditor entitling the creditor to foreclose on the right upon default, taking possession of the property with a right to convey title. Upon performance by the debtor, the mortgage right is discharged.

***Equitable charge:*** A charge is a property right entitling a creditor to seize an asset upon a condition (default).

A fixed charge attaches when an agreement has been made, the creditor gives value to the debtor, and the debtor acquires rights in the charged property, whichever occurs last. Under a fixed charge, the debtor may not dispose of the charged asset. Fixed charges, therefore, facilitate equipment finance but are not useful for inventory finance. Fixed charges are not generally associated with intangible property, though in Britain it was held in 1978 that a fixed charge could attach to a company's receivables, a rule that has apparently not spread among the Commonwealth.

A floating charge, which by common law can only be created by a company, may attach to a changing pool of assets, such as inventory of an enterprise, rather than in any particular asset. Under certain circumstances, a floating charge may "crystallize", meaning that it is converted from a floating charge to a fixed charge. Crystallization may occur upon the winding up of the business, upon the occurrence of an event specified in the charge agreement, or upon action by the creditor to enforce the charge in accordance with provisions in the charge agreement (usually involving the appointment of a receiver).

***Company Charge Registration:***  The registration of company charges in Britain dates to the Companies Act of 1900. Originally, registration gave public notice of charges and provided incentives to lenders to register, but did not act to determine priority among competing charges. Priority among competing charges remained largely the province of common law. Instead, the purposes of registration are:

* To disclose encumbrances on property,
* To help prospective corporate borrowers assure prospective lenders that their property is not encumbered,
* To provide some protection in the form of priority as provided by common law, and
* To help receivers determine the validity of a charge.

Extensive documentation is required to register a charge, including a prescribed form, the charge agreement, and details on the amount secured by the charge. Other formalities apply, including time limits for registration (which may only be extended by court order) and proof of payment of stamp duty.

The registrar's certificate of charge is conclusive evidence of compliance with legal formalities; in effect, the act of registration creates the charge.

The priority of the charge is limited to certain third parties such as a liquidator, administrator, or creditor. Buyers and lien holders are examples of potential competing claimants whose interests are not addressed. The company must continue to maintain its own records with respect to the charge. Despite the considerable information required for registration, the effect of the registrar's certificate is that the registered charge is valid as to its original terms, not as to the terms actually appearing on the Charge Register. Those who search registry records must beware if they are seeking accurate information on the charge, which can only be had by examining the charge document. Consequently, the public may not rely on the register to contain accurate information about the details of the charge. The public may only rely on the fact that the certificate will protect the creditor.

**Priority of Floating Charges**

Until crystallization, a company may dispose of charged assets in the ordinary course of its business. Thus, buyers in the ordinary course of business take free title to collateral from the creator of the floating charge. Unfortunately, the crystallization rule creates a loophole in which other creditors may create fixed charges in assets that will have priority over the general creditor (the creditor who holds the floating charge). This is because their charges attach before the floating charge crystallizes. In effect, other creditors may "cherry pick" the assets of the debtor by creating fixed charges, thereby watering down the value of the general creditor's floating charge.

A further limitation on the value of floating charges is the rule that a receiver must pay certain creditors before paying claims secured by the floating charge. Fixed charges are not subject to this limitation. The value of the floating charge is further diluted.

Holders of floating charges frequently attempt to preserve the value of their charges with "negative pledges" by which the company promises not to create fixed charges that would water down the floating charge. But these negative pledges cannot be registered, and therefore cannot be enforced against a creditor who takes a fixed charge in violation of the negative pledge.

**Priority of Fixed Charges:**

Among competing fixed charges, priority depends on the nature of the charge and the type of notice that applies to the collateral. The general rule is that a fixed charge (other than a charge in a receivable) has priority over another fixed charge if the charge was registered within 21 days of its creation (or within any extended period allowed by the court and before the grant of the subsequent fixed charge). The defect in the rule is the 21-day period. If the 21-day period is not observed, the first charge does not have priority over the second even if it was registered before the second charge was created.

Further, the first creditor to register within the 21 day period cannot be sure of priority. If the first charge is an equitable charge and the second is created at law or is a mortgage, the second will probably have priority due to the absence of constructive notice. In short, priority depends not so much on the order of registration but rather on the nature of the legal form used by the borrower and lender.

If the charge is a charge on accounts (receivables), priority depends not on the date of registration but on the date of notice given to the person who owes payment on the account. This imposes a duty on the secured lender to notify every person who owes on a pledged account, a duty that can be quite expensive to perform, if it is possible at all.

**PART III**

**The Need to Reform Company Charge Registration**

This Section considers whether company charge registration needs reform. The conclusion is that reform is necessary, but that weaknesses in the priority scheme, in addition to the registration scheme, are sufficiently profound that wider reform is also required.

The value of a registration scheme is self-evident. At a minimum, the least efficient registration scheme provides some notice of prior charges, and this information is valuable in a number of commercial circumstances. Abolishing the registration scheme is not an option. Reform is required.

What should be the criteria by which reform is measured? More than half a century of experience with reform in other jurisdictions is persuasive. Registration should accomplish two purposes. First, registration must warn people, usually prospective buyers and lenders, of the possibility of prior encumbrances on personal property. Second, the registration date is an objective, verifiable date that lies at the heart of a rational scheme for prioritizing competing claims.

The notice function is satisfied if registration (1) gives the public reasonable notice of the assets or types of assets that may be subject to a charge, and (2) provides information to the public on how to seek more definitive information. Quite simply, registration provides a warning to interested persons that they should seek further information if they intend to deal in property described in the notice.

No registration system can provide positive proof of a charge for a variety of reasons. Registration cannot prove that charged assets still exist, if they ever existed or ever will exist. Registration cannot prove that there is a secured obligation (without which there is no charge), that there ever was, or will be.

Registration is merely a snapshot of conditions at a particular point in time. The amount of the secured debt, therefore, is information disclosed to the registry that, if it is accurate at the time of registration, will likely be inaccurate for all time thereafter.

For these reasons, registration should serve the purpose notice (and priority, as discussed below), but in addition it must be emphasized that the registry serves little purpose to the extent it goes beyond those functions. The attempt prove the existence of a charge by registration adds significant and unnecessary cost and legal formality to each transaction. The collection of unnecessary information such as the amount of secured debt provides no meaningful assurance to serious prospective creditors who will be unsatisfied with a dated snapshot of the company's finances.

The priority function is served if registration provides an objective and verifiable date that the public may easily discover. In most circumstances, the fair result is that the first registered charge has priority over charges that are unregistered or that are registered later. As we have seen, that is not the case today. Priority may be determined by the nature of the charge: fixed or floating, crystallized or not crystallized, legal or equitable.

The registration date lies at the heart of a well-functioning set of priority rules. But a wooden "first to file wins" rule is inadequate in many commercial circumstances. In some cases, buyers should take collateral free of any charge, as when they buy goods from a dealer in the ordinary course of business. In other cases, buyers should take collateral subject to the charge. In cases where a seller or lender advances money for the purchase of specific goods, it makes commercial sense that they enjoy priority in those goods over a prior general creditor. Where a lender has taken possession of goods, documents of title, or negotiable instruments, registration is unnecessary to warn the public of a charge because the debtor cannot offer them for sale or as collateral to others; registration is unnecessary in such cases. For these and other reasons, registry reform is desirable only as part of wider reform of priority rules. Priority rules should be designed to promote commercial activity, rather than exist as mere dependencies on legal formality.

Registration can be efficient and inexpensive when limited to the purposes of notice and priority. The registry need collect only limited information. Electronic means can be used to capture the information, store it, and deliver it to interested persons. In most jurisdictions in Canada, and in New Zealand, registration is accomplished electronically without any human intervention by the registrar. Electronic registration is an option in most U.S. jurisdictions without registrar intervention. Recent reforms in Micronesia, Solomon Islands, Vanuatu, and Honduras have implemented entirely electronic registries for personal property registration.

As discussed above, registration originally sought the goal of public information. Now, registration factors into some priority questions. Even this value is limited under current law, however, because many transactions about which the public would like information are not subject to registration. The scope of the registry is incomplete. As it is set out in the Companies Act, section 93(2)(3), the following charges must be registered: (a) a charge for the purpose of securing any issue of debentures; (b) a charge on uncalled share capital of the company; (c) a charge created or evidenced by an instrument which, if executed by an individual, would require registration as a bill of sale; (d) a charge on land, wherever situated, or any interest therein but not including a charge for any rent or other periodical sum issuing out of land; (e) a charge on book debts of the company; (f) a floating charge on the undertaking or property of the company; (g) a charge on calls made but not paid; (h) a charge on a ship or any share in a ship; (i) a charge on goodwill, on a patent or a license under a patent, on a trade mark or on a copyright or a license under a copyright.

The list of registrable charges is a fixed list. A registered charge over property other than a charge on the list provides public notice but is ineligible even for the imperfect protections of priority established by statute and common law.

Omitted from the list is a wide range of company assets that may be encumbered in one form or another.

* Legal forms which do not technically create charges but which serve the same function – to provide security to a creditor – include every title retention scheme devised by creative lawyers, including conditional sale, hire-purchase, and finance lease. All these, and even true leases, are subject to registration under the reformed acts of Canada, New Zealand, Australia, Solomon Islands, Vanuatu, Federated States of Micronesia, and many other jurisdictions.
* Aircraft are omitted from the list.
* Rights to future payments are omitted, unless they meet the definition of "book debt" though their value may far exceed the value of land or equipment or inventory.
* Computer software, design rights, and perhaps other forms of intellectual property are not on the fixed list.
* Charges on shares are omitted from the list.

Registrable charges do not expressly include charges on business equipment, though they are within the scope of the clause requiring registration of a charge created by an instrument, which, if executed by an individual, would require registration as a bill of sale. In Jamaica, the Bills of Sale Act of 1867 must be considered when lodging a company charge. But the Bills of Sale Act is inconsistent with much of today's commercial practice. Commentators have questioned the wisdom of linking the company charge to such an antiquated statute

***The priority function***

Priority under the company charge scheme does not meet the requirements of modern commerce. The registration date is a rather small factor in determining priority. Many other legal formalities must be considered in order to determine the priority of a charge with respect to competing claims. Failure to register certainly results in loss of priority.

But a host of complicated circumstances must be considered even after registration.

* The 21-day grace period for registration permits a charge to be trumped by another charge, created after the first charge but before it was registered.
* If the first charge is equitable and the second legal, and if the second charge holder had no knowledge of the first charge, the second charge holder may win a priority dispute on the grounds that he is a bona fide purchaser for value and without notice under common law.
* A negative pledge clause in a floating charge agreement need not be registered, and therefore no public notice is created.

As a method of resolving priority issues, company charge registration coupled with an array of statutory and common law rules leaves us with a confusing scheme that deters commerce.

***Registration in advance of a charge agreement***

Jamaican borrowers and lenders are disadvantaged by the fact that the current system does not permit registration in advance of creating a charge. With advance registration (and with reformed priority rules emphasizing the date of registration as the priority date), prospective borrowers and lenders can negotiate while the lender has assurance of priority when credit is actually extended.

Jamaican borrowers and lenders are also disadvantaged by the fact that many loans depend upon a succession of charges. The time and expense of multiple trips to the registry must be factored into many business deals. With the ability to register in advance of a charge (and with reformed priority rules), only one registration will secure multiple charges in a series of transactions between the borrower and lender that may occur over a period of many years.

**Conclusion**

The requirements of notice and priority are not adequately addressed under current law and practice. The registration scheme is complicated, incomplete, restrictive, and in need of reform.

**PART IV**

**Introduction**

This Part describes notice filing as it has been implemented in overseas systems. It concludes that such a filing system would benefit Jamaican businesses and lenders and should be adopted in Jamaica.

**An Outline of Notice Filing**

As noted in Part I, the United States and several Commonwealth countries have adopted comprehensive notice filing systems for security interests in personal property. In these systems a notice is filed in a central registry. In recent years, registries are operated electronically. Limited information is contained in the notice: the identification of the parties (the debtor and the secured party) and a description of the collateral, which may be general in nature. The notice may be filed before or at any time after a security agreement is concluded between the parties. The security agreement is not part of the registry record. A comprehensive set of priority rules, set out in legislation, are largely keyed to the registration date, although there are exceptions, as for example when collateral is in the possession of the secured party.

Invariably, notice systems apply to a wide range of transactions, and are not restricted to company charges.

A notice does not necessarily relate to a specific transaction. The notice is merely a statement that a secured creditor has taken or may take a security interest in assets described therein. Priority rules generally establish priority dating back to the time of notice, even where assets described therein are acquired in the future.

**The Notice**

Under typical legislation, a notice must contain merely the names and addresses of the debtor and secured party and a description of the collateral. The secured party files the notice. In the U.S., the debtor must authorize the filing, although the authorization need not be contained on the notice and is not communicated to the registry. In Canada, the debtor's authorization is not required but the debtor must receive a copy of the notice.

Under typical legislation, collateral may be described specifically or as a class of property such as equipment, inventory, accounts, instruments, documents of title, chattel paper, crops, livestock, etc. Alternatively, the notice may describe collateral as all personal property of the debtor of any nature, and may include property acquired after the notice is filed and after the security agreement is concluded.

By limiting the information contained in the notice, the registry itself can be operated electronically, and with speed and efficiency. The New Zealand system has been entirely electronic from its beginning, as have those in Vanuatu, Solomon Islands, and Micronesia. The U.S. and Canada reformed their law prior to the availability of such technology but have moved substantially to electronic operations.

By limiting the purposes of registration to notice and priority, there is no need for the registrar's certificate.

**The effect of errors in registration**

In the overseas systems, errors and omissions in the notice do not invalidate it unless they cause the notice to be "seriously misleading." A notice that failed to name the debtor would certainly be seriously misleading.

**Should filing be mandatory?** Filing is not mandatory under the overseas systems, nor under others based on them. The penalty for filing is loss of priority under any priority rule that depends on filing. A security interest that has attached to collateral is always enforceable against the debtor without filing, but non-possessory security interests are generally enforceable against third parties only if a notice covering the asset in question has been filed.

**Public character of notice**

Buyers of collateral and prospective lenders (who may be anyone, anywhere) must rely on the registry for notice of possible security interests. It is, therefore, essential that notices be characterized by law as public records, and anyone should have the right to view them through search facilities maintained by the registrar.

**When to file**

Currently, the registry must receive charge registration documents within 21 days of the creation of the charge. This creates, in essence, a "secret lien" for up to 21 days during which a search of registry records may deceive the searcher. In the overseas systems, a notice may be filed at any time, but priority generally dates from the date of filing. There is, therefore, no "secret lien."

**Duration of filing**

In the U.S., a notice has a duration of five years, which can be terminated at any time or renewed for successive five-year periods. This system observes that most credit secured by personal property is short-term credit, and allows the registry a means by which notices are self-purged from the roster of effective notices unless the secured party does something to maintain the effectiveness.

In the Canadian systems, a notice has the duration stated on the notice. The notice can be terminated at any time, and extended if need be. This system observes that a secured creditor may accidentally lose priority by failing to renew a notice at the end of a standard period of time.

**Amendment of notice**

All systems permit the amendment of notices. The names and addresses of the parties may change. The identity of the secured party may change, as when a secured party assigns its interest in collateral to another person. The parties may agree to changes in the collateral. The secured party may discover errors in the initial notice. An amendment procedure permits the secured creditor to keep the notice accurate and up to date.

**Pre-filing**

All systems permit the filing of a notice prior to the creation of a charge, in order to facilitate complex agreements for which extended negotiations may be necessary, and to accommodate transactions comprised of multiple, successive agreements secured by the same collateral.

**Priority**

This section examines the priority of security interests in circumstances in which multiple parties (buyers, other secured creditors, unsecured creditors, and lien holders) assert claims that compete with a secured party that has perfected a security interest by filing a notice (or, perhaps, by taking possession of the collateral).

In the overseas systems, the date of perfection (i.e., registration, or the date of taking possession, or sometimes the date the creditor takes control of collateral) is the date of priority against which competing claims are measured. In general, the first to file a notice or perfect has priority over security interests that are unperfected or are perfected at a later date. A system of priority rules defines the rights of buyers, lessees, and lien holders who assert claims over collateral. Narrow exceptions to the first-in-time rule are set forth to promote equipment, inventory, and livestock finance. Special circumstances are taken into account, such as the commingling of collateral, the creation of accessions and fixtures, and the use of deposit accounts or shares as security.

Unlike the current system in Jamaica and in some other Commonwealth nations, the reformed systems of Commonwealth countries such as Canada, Australia, New Zealand, Vanuatu and the Solomon Islands do not distinguish between legal and equitable claims. The reformed Commonwealth systems do not observe differences between fixed and floating charges, or establish preferences among fixed charges.

**Floating charges in overseas systems**

The UCC and the Canadian PPSAs do not recognize floating charges as they have flourished in the Commonwealth, but they establish a floating security interest that can be much more powerful tool in commercial finance. Security interests may be established in property acquired by the debtor after the date of the security agreement, with priority dating to the date of registration, rather than the date of crystallization. In the meantime, the debtor may deal in the collateral – selling it in the ordinary course of business to customers who take the goods free of the security interest under the priority rules, while preventing other creditors from "cherry-picking" collateral by registering fixed charges.

Secured parties have the right under the reformed systems to agree upon subordination of their interests in collateral. These agreements are effective and enforceable without registration, although the Saskatchewan legislation permits a notice of subordination without requiring it.

**Purchase-money interests**

Purchase money security interests arise when a seller extends credit to a customer for the purchase of goods, or when a lender provides credit for the purchase of specific goods. Purchase money security interests may conflict with prior, general security interests over future-acquired property (i.e., the purchase money goods may constitute future-acquired property). A super-priority rule prevents the general creditor from monopolizing the debtor's credit, and promotes financing for equipment, inventory, and livestock, by granting the purchase money creditor a priority over the general creditor to the extent of the value of the purchase money goods. Upon the discharge of the purchase money security interest, the general creditor resumes its position of priority in the goods.

**Proceeds of collateral**

When the debtor disposes of collateral, the question arises as to the status of property received in exchange for it. In the overseas systems, a security interest in collateral automatically attaches to proceeds, i.e. anything of value given or obtained in exchange or on account of the disposition of collateral. Proceeds may be cash, other property, receivables, insurance payments, and the like. If the security interest in the original property was perfected, then the security interest in the proceeds is also perfected. If the proceeds are of a nature covered by a registered notice, then the security interest in proceeds is perfected for so long as the notice is effective. A security interest attaches to, and is perfected in, proceeds, even if the security agreement is silent as to proceeds.

**Purchasers of charged property**

There is ambiguity in the common law as to the rights of buyers and of charged property. A buyer takes goods free of an unregistered charge, unless the doctrine of good faith purchaser applies. But if the charge is registered, the application of the good faith doctrine is unclear where charged property is bought in the ordinary course of the seller's business. Registration gives the purchaser notice of the charge, but one cannot reasonably expect buyers of stock in trade to search the company registry of charges.

In general, buyers of collateral take charged property free of a security interest only if the buyer gives value for the property before the security interest is perfected. If the property is tangible (e.g., goods) the buyer must also take delivery without knowledge and before perfection. The exception is the buyer in the ordinary course of the seller's business, such as a the typical person who buys goods from the stock-in-trade of a dealer. The buyer in the ordinary course of business takes goods free of a security interest even if the security interest is perfected and even if the buyer has actual knowledge of the security interest.

Similar rules govern the interests taken by lessees of collateral.

**Uniquely identifiable goods**

Some systems modify the rules with respect to certain uniquely identifiable goods, most prominently motor vehicles. In the U.S., for historical reasons, motor vehicle finance is outside the scope of the UCC. In Canada, New Zealand and other reformed jurisdictions, auto finance is within the scope of the PPSAs. Under the PPSAs, a buyer of an auto, other than a buyer from inventory of a dealer, takes the auto free of a security interest unless the auto is described in the registry by its serial number. This rule relieves buyers of the burden to interpret what may be the complicated collateral description filed by a general secured creditor with a blanket security interest in a debtor's present and future personal property. The auto buyer need only search the registry for the serial number of the auto under consideration for purchase. If the serial number is there, whether the buyer searches or not, the buyer takes the auto subject to a security interest. If not, the buyer takes the auto free of any security interest.

**Purchasers of negotiable instruments/documents of title**

All reformed systems grant priority to a purchaser of a negotiable instrument who gives new value for the instrument. Any rule to the contrary would burden the law on negotiable instruments. It is still permissible, however, to take security interests in negotiable instruments, perfect the interests by filing, and enforce them against the debtor and against third parties other than purchasers for value.

**Existing fixed charges** Existing charges must be carefully planned for in transition to a reformed secured transactions legal system.

* New law should not impair contracts that arose under prior law, and disputes among parties to existing security interests should be resolved under the law in effect when they were made.
* There is the possibility, however, that an existing charge may come into conflict with a charge created and perfected under new law.
* Holders of existing charges must be given opportunity to register existing charges in order to preserve rights against holders of new, perfected security interests.
* If existing charges are registered within a reasonable window (in Australia, the window began prior to the effective date of the PPSA for new charges), their priority may relate to the effective date of the new law as against new secured creditors.

**Conclusions**

A notice filing system will give Jamaican borrowers and lenders significant advantages over current registration schemes, when used to warn buyers and creditors of existing claims and when used to drive a more rational and commercially-oriented set of priority rules to governing competing claims.

A notice filing system will be easier to use, in that it will require less information to be registered and can therefore be offered by electronic means to filers and searchers.

Although less information is collected by the registry, the practical value will be greater as priority rules will be clearer, giving more clarity to the status of parties and collateral. The result will be a more favorable climate for business and consumer credit.

A notice filing system will be amenable to registration of a wider range of transactions than are currently subject to registration, greatly increasing its practical value and positive commercial impact.

**PART V**

**Introduction**

This Part examines charges that could be registered under a notice filing system but which are not under the current scheme. The conclusion is that with notice filing and a reformed system of priority rules, a much wider range of charges can be registered to the benefit of Jamaican borrowers and lenders.

**A List of Registrable Charges or a List of Exclusions**

If registration is to be extended to a wider range of transactions, should the scope broadened to a longer list, or should it be all-inclusive except for enumerated exclusions?

In the overseas systems described, registration applies generally to transactions where personal property secures an obligation. The scope of registration and priority rules applies to transactions that are not traditionally considered secured transactions but which have the same appearance to buyers and prospective creditors. Examples are hire-purchase agreements, finance leases, consigned goods, and factored accounts. Except for the U.S., even true leases (sometimes called operational leases) are generally subject to registration and priority rules (though they are not subject to default remedy rules).

Registration for the purposes of notice and priority (but not for the purposes of enforcement) is required of tax liens in the U.S. and Canada, and in many other countries including Commonwealth countries such as the Solomon Islands and Sri Lanka, and other countries including Albania, Cambodia, Federated States of Micronesia, Republic of the Marshall Islands. By subjecting tax liens to notice and priority rules (first to file has priority), lenders have more effective notice of tax liens and more certainty about the status of their claim to collateral, which leads to more lending, more economic activity, and higher tax receipts.

There are many advantages to an inclusive scope of registrable charges, subject only to narrow exceptions.

* The wider the scope, the greater the value of the registry to filers and searchers, borrowers and lenders. The wider the scope, the less uncertainty for creditors as to whether registration is necessary for perfection of their security interests.
* The wider scope, the less opportunity for creative financiers and their lawyers to design transactions exempt from registration, and in a manner that deceives other creditors.
* The wider the scope, the less opportunity for legal challenges in expensive litigation over the question of whether registration was necessary to perfect a security interest.

Provided that registration is simple, fast, and inexpensive, the conclusion is that an inclusive scope for registered charges is preferable to incremental additions to the current list of registrable charges. All charges should be registrable, unless specifically excluded by law.

**Summary of Charges that Would Be Registrable**

To summarize the list of charges and transactions that may be included under a notice filing system of broad application, a list of transactions be as follows.

Any transaction that has the effect of creating a charge on personal property of any nature, whether the property exists at the time the security agreement is concluded or whether the property arises thereafter.

* Transactions in which title retention is used, at least in part for the purpose of securing an obligation to pay the purchase price of goods.
* Consignments of goods and the sale of accounts: Although not secured transactions in a legal sense, people hold property subject to the rights of others and for that reason project an appearance of "false wealth" to buyers and prospective creditors, just as if the property were in fact subject to a charge.
* Charges on fixtures, crops, and in some circumstances, timber and minerals.
* Certain liens arising by operation of law, such as tax liens. 117 Exclusions to registration may include the following.
* Charges on land;
* Charges over property for which there is a special registry, unless special priority rules are devised to resolve any disharmony. An example would be a charge of shares.
* Assignments of accounts made for the purpose of collection only, as part of a business that is sold, or for the general benefit of creditors.

**PART VI**

**Functional Equivalents to Security Interests**

There are many transactions that do not fall within the category of personal property as security, but that perform a similar function. These transactions have been identified above, as transactions that would add commercial value to borrowers and lenders if included in a notice filing registration scheme. This part, then, examines why these transactions would be of benefit to Jamaica. These transactions include title retention (which includes hire-purchase and finance lease) consignment of goods, sale and leaseback or sale and repurchase, and the sale of accounts.

Many of these transactions were created, at least in part, to avoid the expense and legal trappings of creating traditional security. To this extent, none deserves to be exempt from reform under a notice filing system.

Many of these transactions invite competing creditors upon, upon default, to litigate the question of whether they are transactions other than transactions for security, wasting judicial resources and imposing costs on borrowers and lenders.

**Transactions in Goods Title retention**

Title retention devices, such as hire purchase, finance lease, and conditional sale, are examples of transactions created with at least the partial intent to avoid the cost of complying with traditional forms of taking security. Under a reformed system of notice filing that is efficiently operated, there is no justification for their exclusion. To the extent that the forms were created for purposes other than avoiding traditional rules on security, reformed secured transactions law need not (and never has) prevented parties from pursuing those purposes in their contracts. Title retention devices should, therefore, fall within a notice filing system.

**Consignment of goods**

A consignment is a delivery of goods to a dealer. The consignor (the deliverer) retains title to the goods while the consignee (the dealer) is obliged to the consignor for the purchase price, minus a fee. The consignor retains title, in effect, as a form of security. In the meantime, however, consigned goods in the possession of the non-owner consignee present the same appearance of false wealth as if the goods were subject to a security interest or charge. Consignments, therefore, are naturally within the scope of a notice filing system.

"Consignment" is also a term used as a means to finance the purchase of goods by a consignee from a consignor. The financier authorizes the consignee (e.g., dealer) to buy goods from a supplier, taking goods as an agent for the financier. The financier, who takes title to the goods from the supplier, pays the purchase. The dealer sells the goods to customers as an agent for the financier. Again, the separation of ownership from the person who deals in the goods gives an appearance of false wealth to prospective buyers and creditors. It is akin to a title retention device and properly falls within the scope of notice filing.

**Accounts Financing**

Accounts, or the right to receive payment, are among a business's most liquid assets, and in appropriate circumstances, therefore, can be very valuable collateral. A charge on book debt is a registrable under the Companies Act, but accounts finance encompasses assignment of accounts, sale of accounts, and the factoring or discounting of accounts. From a third party's point of view (such as a prospective creditor) these transactions appear the same a charge, yet they are not registrable. There is no apparent reason that they should be treated differently, and therefore they should be included within the scope of a notice filing system.

**PART VII**

**A Functional Approach to Secured Lending Introduction**

Part IV examined notice filing for company charges. Part V examined charges that should be registrable, concluding that many charges that should be registered are not subject to registration. Part VI examined transactions similar to charges that, by their commercial nature, ought also to be subject to registration.

**Criticisms of the Present Law** IV, V, and VI illustrate a problem with current law that has been resolved in the overseas systems. Current law on registration and priority is dependent on legal form, rather than commercial function. All the reformed systems reverse the emphasis: transactions that serve similar commercial function are treated similarly for purposes of registration and priority.

To a buyer or prospective lender, a piece of non-titled equipment such as a tractor or a printing press looks identical, whether the equipment is owned outright or is the subject of a finance lease, a hire-purchase agreement, a mortgage, or a charge. The first two are not registrable; the third and fourth are registrable.

Rights on default also differ from form to form. For example, debtors are entitled to surpluses where assets are mortgaged, not so under hire-purchase agreements.

**Conclusion**

Jamaica will be well served by a transition from a system of secured lending that depends on legal formality to a system of commercial functionality. All charges in personal property should be registrable. All transactions that have the effect of creating security (such as hire-purchase) or which create the appearance of false wealth to third parties (such as consignment and assignment of receivables), should be registrable. To some extent, and for the same reason, even true leases should be registrable for the purposes of notice and priority. A system of priority rules must treat similar property equally for the purpose of resolving disputes among secured creditors and third parties.

The Saskatchewan PPSA applies to (a) to every transaction that in substance creates a security interest, without regard to its form and without regard to the person who has title to the collateral; and (b) without limiting the generality of clause (a), to a chattel mortgage, conditional sale, floating charge, pledge, trust indenture, trust receipt, or to an assignment, consignment, lease, trust or transfer of chattel paper that secures payment or performance of an obligation (b).

The Saskatchewan PPSA defines "Security interest" to mean an interest in personal property that secures payment or performance of an obligation, but also includes certain interests even though they do not secure payment or performance of an obligation.

All forms of receivables should fall within the filing notice system and its related priority rules. There is no commercial justification for differentiating the substantive rights of borrowers and lenders, and no justification for disclosure to or deception of third parties, based on th type of legal form used by the parties to any agreement.

**PART VIII Individual Debtors**

So far, this paper has examined notice filing for corporate debtors, although the introduction to Part I points out that consumers, proprietors, and partnerships also have a need for a rational and efficient legal system governing secured credit.

Although consumer protection principles may justify restrictions on general charges over consumer goods to secure purchase money credit and even general credit, one is hard pressed to imagine other justifications for reserving a system of property rights to a single class of persons (i.e., corporations).

Without exception, in the overseas systems, the rules on which may give a security interest and who may take a security interest are equally applicable to corporate and non corporate debtors and lenders. That is to say, the rules are the same for all with respect to creating, registering, prioritizing, and enforcing security interests in personal property (with limited exceptions as to consumer goods, to prevent lender abuse of those whose bargaining position is weak).

**Security Interests Granted by Individuals Possessory security**

There are no significant differences between the ability of an individual or a company to give a possessory security interest in goods or negotiable instruments. Consequently, this paper will focus on non-possessory forms of security.

**Goods: bills of sale**

The Bills of Sale Act is the primary means by which individuals create security in personal property. The statute is a scheme for protecting lenders under certain transactions from the claims of certain third parties with respect to certain tangible and intangible property. The rules are complicated.

**Registry**

The statute requires a bills sale registrar to keep a register with the name, address, and other particulars of grantors, and has certain other duties. The register is a public record.

Failure to register may not void the bill as to the debtor, but will prevent the creditor from asserting claims against some third parties.

**Scope:**

As with the company charge registry, the scope of the Bills of Sale Act is limited. Title retention schemes and other non-traditional or novel means of taking security are not within the scope of the Act.

**PART IX**

**Individual Debtors & Security Interests: The Need for Reform**

**Introduction**

This Part examines the need to reform law on security interests in personal property given by individuals. The conclusion is that reform is necessary. Many Jamaican businesses do not operate in the corporate form. Many Jamaican businesses may incorporate merely or primarily to gain access to the floating charge, a form that is unavailable to them as individuals but under a reformed system would not require incorporation for them to enjoy. Reformed law on creating, perfecting, prioritizing, and enforcing security interests is, therefore, at least equally important as to individuals as it is to companies, especially considering that the legal forms available to individuals are even more restrictive than for companies.

**Criticisms of Existing Law**

Throughout the Commonwealth, the Bills of Sale Act has been criticized for its dependence on technicality and formality, which creates traps for creditors that may result in loss of priority or even voidance of the bill.

The pitfalls that give worry to creditors can only create a chilling effect on credit for businesses operated by individuals and partnerships, and also for consumers whose lenders would use the Act to protect creditor rights in many circumstances including auto finance.

Title retention devices, some of which were invented at least in part to avoid the Bills of Sale Act, are not registrable and therefore assets subject to the devices create an appearance of false wealth to prospective buyers and lenders.

Commonwealth countries that have reformed secured lending law, including Canada, New Zealand, Vanuatu, Solomon Islands, and quite recently, Australia, have abandoned the Bills of Sale scheme with its registry.

**Conclusion**

The law on security interests given by individuals needs reform. The Bills of Sale Act, on the books for well over a century, is inadequate to support business and consumer credit needed today in Jamaica.

There is no rational basis for distinguishing between individual and corporate borrowers, as evidenced by the success of reformed legislation in the overseas systems that apply the same rules to individuals and companies with respect to creating, perfecting, prioritizing, and enforcing security interests in personal property.

Jamaica should reform its law on security interests in personal property without distinction between individual and corporate borrowers. Concomitantly, the Bills of Sale Act should be repealed.

**PART X**

**Introduction**

This Part examines whether a notice-filing scheme for personal property should set out common minimal rules for the creation of security agreements and the enforcement of security interests.

As it has been noted, current law employs a variety of legal forms in creating and enforcing security interests in personal property. Each legal form has its own rules for creating security interests and enforcing them. Assuming that a functional system replaces the current system based on legal forms, a minimal set of rules for creating and enforcing security interests can further lower costs to borrowers and lenders by reducing the number of legal formalities, such as witnesses, attestations, affidavits, stamp duties, and the like.

This Part, in the next few paragraphs, describes the approach taken in other jurisdictions where a functional approach to security has replaced the system based upon legal forms, namely the U.S., Canada, and New Zealand, but also other Commonwealth countries such as Vanuatu and Solomon Islands and the very new Australia PPSA, as well as other jurisdictions that have followed the U.S./Canadian model such as Cambodia, Federated States of Micronesia, Puerto Rico, the Republic of Marshall Islands, and others.

**The security agreement**

A security agreement is effective according to its terms against the debtor if it is in writing or if the secured party has taken possession of the collateral. A written agreement must be signed by the debtor and must contain a collateral description. There are no other formalities.

**Attachment**

A security interest attaches to collateral and is enforceable against the debtor when (1) a security agreement is effective, (2) the debtor has acquired rights in the collateral, and (3) the secured party has given value to the debtor.

**Rights and remedies on default**

No matter the legal form, upon default the secured party has the right to take possession of collateral without judicial intervention if possible to do so without a breach of the peace. Upon taking possession, the secured party has the right to dispose of the collateral without judicial supervision, but under a duty to dispose of the collateral in a commercially reasonable manner.

Where collateral consists of accounts, the secured party may require the account debtor to pay the secured party rather than the debtor, without judicial intervention.

Upon disposition of collateral, the debtor is entitled to any surplus over the secured debt and the costs of enforcement.

The secured party may retain collateral in full or partial satisfaction of the secured debt by agreement with the debtor.

**Powers and duties of receivers**

Under Saskatchewan law, which is indicative of much of Canadian law, a security agreement may provide for the appointment of a receiver upon default. In New Zealand, the right to appoint a receiver is governed by another statute.

**Minimal Formalities for Giving and Enforcing Security Interests**

With the background set forth above, the question is whether a notice-filing scheme for personal property should set out common minimal rules for the creation of security agreements and the enforcement of security interests.

Title retention credit facilities, such as hire purchase, finance lease, and consignment, make up the bulk of transactions heretofore not considered secured loans, but which are, in effect, secured loans. It seems only reasonable to subject them to the same rules on creating and enforcing security, if they are to be subject to registration and priority rules. To leave them aside would perpetuate a dual regime that would impose unnecessary costs on borrowers and lenders. Second, by bringing title retention devices into the same regime with traditional security arrangements would give to the debtor the advantage of the rules on surplus value, which the debtor is deprived of so long as the pretense is maintained that title retention schemes are not secured transactions.

**Conclusion**

A notice filing system that subjects a wide range of transactions to registration and priority rules will, it seems plain, be more efficient for borrowers and lenders if the transactions are also subject to the same basic rules governing security agreements and enforcement upon default.

Of course, the parties should be, as they are now, quite free to define their own remedies by contract and those remedies should be enforceable to the extent possible under existing law.

**ANNEX D**

**DISCUSSION PAPER**

**DISCUSSION PAPER ON SECURED TRANSACTIONS REFORM FOR THE JAMAICA BAR ASSOCIATION**

**PAUL HOLDEN AND ALLEN WELSH[[5]](#footnote-3)**

**SUMMARY**

1. Sustained economic growth requires access to credit. Private sector credit in Jamaica, as a percentage of GDP, is less than half that of most countries with the same level of income, which has a strong negative effect on growth, especially for smaller businesses.

2. Access to credit in Jamaica is difficult, in part, due to the antiquated laws that apply to the use of personal property as collateral. These laws, such as the Bill of Sale Act of 1867 and 19th century common law devices, must be reformed in order to increase access to credit and improve the functioning of financial markets.

3. A number of countries around the world have reformed their laws with respect to personal property as collateral by implementing a modern “secured transactions law,” which has proven to be effective in improving access to business and consumer credit.

4. A Jamaican Secured Transactions Act will make it easier for borrowers and lenders to use personal property as collateral in four ways:

* Borrowers will be able to pledge their rights in personal property to lenders as security for loans more easily, flexibly, and inexpensively.
* Secured lenders will be more certain of their right to enforce collateral agreements, not only against the borrower, but also against third parties who may lay claim to the collateral.
* A modern public records system will provide information to the public that will identify and prioritise conflicting claims to collateral.
* Enforcement of collateral agreements, including repossession, will be more effective and efficient.

**BACKGROUND**

Sustained economic growth requires access to credit. By any measure, Jamaica’s financial markets are underdeveloped. At the end of 2008, the ratio of private sector credit to GDP, the best measure of access to finance, was equivalent to about 35% of GDP. Ratios of private sector credit to GDP in high-income countries typically exceeded 150%. Low and middle-income countries have ratios greater than 70%.

Why is access to finance in Jamaica so limited? The law is an important factor. Lenders require collateral in the form of real property or personal property. In the United States, where law on personal property as collateral is highly efficient, 70% of private sector credit is secured by personal property. Jamaica cannot achieve such a result under its current laws.

In Jamaica, personal property typically secures credit under the Bill of Sale Act of 1867, 19th century common law rules on company charges, hire-purchase agreements, and a variety of other legal forms rooted in the common law of contracts.

The use of 19th century legal forms is inefficient and unsuitable for modern business practices and results in many anomalies. Some legal forms discriminate by type of borrower. For example, a company may give a fixed charge or a charge on a floating pool of present and future-acquired assets, while an individual may not take advantage of this powerful finance tool. Some forms, such as hire purchase agreements and finance leases require the lender to take or retain legal title to the collateral, while other forms have no such requirement.

Procedures for the enforcement of lenders’ rights differ depending on which legal form is used. Judicial intervention is required under some forms, and not required under others. The rights of lenders against competing creditors are different depending on which legal instrument is used. Some forms protect lenders from the claims of prior and future pledges of the same property given by the debtor to competing creditors while other forms offer limited or no protection.

Some forms require registration to create and prioritize a charge against competing creditors, such as when company charges and registered bills of sale are used. For other forms, there is no registry.

Registering charges is expensive. Many lenders including those using government-sponsored loan schemes, do not register bills of sale, because of the cost, which adds to the risks of providing credit.

In short, the variety of forms, each with its own peculiarities, imposes risk and legal compliance costs on borrowers and lenders. This cost and legal risk reduces access to credit in Jamaica. Depressed credit markets lead to insufficient funding for investment and entrepreneurship. Lending is primarily confined to well-established businesses and those that own real property. The dynamism needed for growth is lacking because key sectors of the economy find it hard to get financing. Small and medium-sized businesses of all kinds report enormous difficulty accessing finance even though many of them are in a position to offer collateral that would be accepted in other countries. Growers of the world famous blue mountain coffee, a product that can be stored, and for which there is excess demand, cannot use their output as collateral to obtain credit, which adversely affects investment and prevents expansion of the sector.

A solution to the lack of access to finance exists. Many countries around the world have reformed, or are in the process of reforming, their laws governing personal property as collateral. The United States was the first to develop an effective collateral framework, starting in the 1960s on a state-by-state basis. Canada followed beginning in the 1970s. A number of countries in Europe and Asia reformed their laws on personal property financing from the late 1980s onwards. Puerto Rico recently adopted American law on secured transactions. New Zealand adopted reform similar to Canadian legislation in 2002 and Australia followed suit last year. Four Pacific Island nations have recently implemented reforms: Federated States of Micronesia (2006), Vanuatu and the Solomon Islands (2009), and the Marshall Islands (2010). Bills are under consideration in many other countries.

Lending risk falls when the law permits effective use of collateral. Lenders react by offering more credit at the same or better terms. More credit on better terms permits higher rates of investment and more capital per worker, resulting in higher incomes. Modern secured lending law is a feature of virtually all countries where access to credit is easier than it is in Jamaica.

**PROPOSAL FOR POLICY REFORM**

Virtually every successful reform that has taken place over the past two decades has used as models, the laws, principles, and rules adopted in the United States and Canada. A Secured Transactions Act that conforms to these models will promote greater access to credit in Jamaica by introducing best practices in the pursuit of four fundamental principles:

***Principle 1 – Ensure that the creation of security in personal property is simple, flexible, and inexpensive and cannot be challenged readily***

The Secured Transactions Act should permit any individual or firm to create security in any personal property of any nature without restrictions. The collateral may be tangible or intangible and may be held by the debtor at the time of the agreement or acquired at any time in the future. The collateral may include equipment, inventory (stock in trade), accounts receivable, consumer goods, securities, letters of credit, warehouse receipts, bills of lading, crops currently growing or that will be grown in the future, livestock including unborn animals, timber to be cut, minerals to be extracted, and fixtures to real property. The only necessary legal formality is that the borrower signs a simple agreement consenting to the use of the property described in the agreement to secure a loan obligation.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Provide definitions of key terms and appropriate rules of statutory construction.
* Define transactions that are subject to the Act, which may be transactions secured by personal property, transactions where property held by the debtor is subject to rights held by other persons, and other circumstances in which property held by the debtor becomes subject to rights held by others, with or without the consent of the debtor.
* Define the nature of security interests in personal property and obligations that are secured by personal property.
* Provide for the effectiveness of security agreements against the debtor.
* Provide for the duties of secured parties (creditors) when the secured party holds collateral.
* Provide for the rights of borrowers to obtain appropriate information from secured parties.
* Provide the conditions upon which security interests will attach to personal property.

***Principle 2 – Clarify the rights of competing creditors***

The Secured Transactions Act should provide the lender with legal certainty as to its rights against competing claims to the same personal property, anticipating all the commercial conflicts that may reasonably be expected to arise. The Act should address the rights of secured creditors against holders of non-consensual claims such as judgment liens, tax liens, and other liens. Potential conflict among creditors should be resolved through legislative rules that are designed to promote commerce.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Define the methods by which a secured party (the lender) may protect its interests against persons other than the debtor.
* Provide for the rights and obligations of persons who buy or lease collateral.
* Provide for the rights of secured creditors in proceeds of collateral (property that is received in exchange for collateral).
* Provide for the rights of secured creditors against lien holders, and others who gain rights in collateral without the consent of the debtor.
* Provide for the rights of secured parties against mortgagees, in the case of security interests in crops, fixtures on real property, timber, and minerals.
* Provide for the rights and obligations of persons who purchase accounts, chattel paper, and instruments that are collateral.
* Provide for the rights and obligations of parties where accounts are sold or assigned.
* Provide for the rights and obligations of parties where collateral consists of deposit accounts or investment property.
* Provide for other circumstances relating to secured creditor rights against third parties who acquire interests in collateral.

***Principle 3: Use modern technology and simple design to share information***

The Secured Transactions Act should provide for the establishment of a modern, electronic registry for filing notices of collateral agreements. Notices will warn prospective creditors and buyers of prior claims to collateral and, with few exceptions, will establish priority among competing creditors by the order of filing. The registry will not receive loan documents, nor will the registrar verify the accuracy of information or determine its compliance with law. Under a notice filing system, the registry simply records the date and time of the notice, assigns a filing number, bills the filer for the filing fee, and stores the notice for public inspection.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Establish a secured transactions filing office to receive, store, and report information on security interests and liens, in accordance with best practices.
* Limit the information collected to the identification of the parties and a description of collateral in accordance with best practices, in order to protect the privacy of agreements and minimize the cost of the registry.
* Provide for the duration of a notice of a security interest, and the method by which the notice may be continued in duration, amended, or terminated.
* Provide for the limited duties of the filing officer.

***Principle 4 – Enforce property rights efficiently***

The Secured Transactions Act should ensure efficient enforcement of obligations, without resort to the courts whenever possible. Upon default, a secured creditor should have the right to possession or control of collateral and the right to dispose of the collateral in a commercially responsible manner.

Accordingly, under this principle, a bill for a Secured Transactions Act should:

* Provide that the parties to a security agreement may define default.
* Provide for the right of a secured party to take possession or control of collateral upon default.
* Provide rules that facilitate the ability of the secured party to take possession or control of collateral upon default, and to dispose of the collateral.
* Provide rules governing the circumstances under which the secured party may retain the collateral in full or partial satisfaction of the secured debt, and circumstances under which the debtor may redeem the collateral.
* Impose obligations upon the secured party to act in a commercially reasonable manner when exercising its rights upon default.

In addition, the bill should contain appropriate transition rules, and amendments to related legislation to avoid conflict with existing law.

The Secured Transactions Act will provide for the establishment of a filing office that will replace the Bills of Sale Registry and the part of the Companies Registry that deals with company charges. The Secured Transactions Filing Office will be implemented as a publicly accessible electronic service that conforms to internationally recognized standards of practice. The operation of the filing office will sustain itself with user fees and without taxpayer support.

**EXISTING LEGISLATION AND SECURED TRANSACTIONS REFORM**

A Secured Transactions Act will conflict with the Bill of Sale Act of 1867 and the Hire-Purchase Act of 1974. These Acts should be repealed upon the adoption of the Secured Transactions Act. Consumer protection provisions peculiar to these Acts may be re-enacted in the Consumer Protection Act in an appropriate manner to apply generally to consumer transactions.

The company charge is inconsistent with a Secured Transactions Act to the extent the company charge applies to moveable personal property and fixtures. The Companies Act must be amended to limit the effect of the company charge to real fixed property.

Any legislation that establishes tax liens or other claims in favour of government should be amended to authorize filing of notices of the liens in the Secured Transactions Filing Office, with priority against third parties dating from the date of registration.

Stamp duty cannot be effectively collected or enforced under modern secured transactions law, and therefore secured transactions should not be subject to the Stamp Duty Act. The Secured Transactions Filing Office, however, will generate fees that will help to offset lost revenue. Preliminary calculations indicate that any revenue loss will be very small or could even lead to a small revenue gain with the appropriate adjustment of charges.

**IMPLICATIONS OF THE NEW LAW FOR LEGAL PRACTICE IN JAMAICA**

Secured transactions legal reform will require change in the practice of commercial law related to the pledging of personal property as collateral for loans. The reform is, in part, an elevation of commercial function over legal form. In a single agreement, any borrower (corporate or individual) may grant to a secured party a security interest in any present and future personal property. The parties may agree to collateral descriptions as they please, but general descriptions are routine. Consequently, many security agreements that previously required individualized loan agreements will be reduced to standard forms, especially for smaller loans.

Many countries where this reform has taken place have seen a sharp increase in the number of security interests recorded. Once the reform is in place, a similar rise can be expected. This implies a change in the nature of legal practice in this area from one of preparing documentation for loan agreements, to one of giving advice on more complicated transactions. It is also likely that external financing secured by personal property will become more common, and the legal profession will need to be acquainted with the details of these types of agreements.

The provisions of the Act will affect any business that provides credit to customers on non-land securities. Financiers will need to review and modify security documents and procedures relating to charges, mortgages over all property other than land, vehicle and equipment leases and hire purchase agreements. Manufacturers & suppliers will need to register their rights in relation to commercial consignments and retention of title arrangements, as they will constitute security interests.

The Act also creates various risks for businesses, which will require advice from the legal profession to make owners and managers aware of the various risks and obligations that they face. For example:

* If another person holds a registered security interest in the assets over which a business or person has an unregistered security interest, the registered interest will take priority over the unregistered interest. The registered party may be able to deal with the assets without reference to the original interest;
* If the counterparty to a contract deals with the assets in the ordinary course of business, such assets could be disposed off and businesses’ interests extinguished, even if it holds title to the asset;

To achieve the highest priority, the secured party must perfect its security interest by control (if the asset is capable of control), by possession (if practicable), or at least by registration.

Lawyers in Jamaica can assist clients by:

* Identifying transactions and affected assets that can be registered;
* Reviewing standard terms of supply, as well as any other arrangements affected;
* Advising on registration of security interests and obligations post registration under the new Secured Transactions Act;
* Redrafting security documents; and
* Preparing new company policies.

In addition many issues will arise during and after the transition to the reformed secured transactions framework on which existing and prospective clients will seek advice. These include:

* How documentation for loan agreements will change?
* How this will impact on existing documentation?
* How will the new law impact priorities and new security interests in the transition period?
* How will auto financing change under the new system?
* Are there any risks to current borrowers during the transition and what will be the impact of the changeover?
* Currently many trade creditors are relying on reservation of title. How will that change under the new system and how can trade creditors protect themselves?

These issues will require that the legal profession dealing with personal property security interests be prepared for the significant change in the legal structure related to the provision of collateral.

1. The views expressed in this paper do not necessarily represent those of the InterAmerican Development Bank [↑](#footnote-ref--1)
2. For Solomon Islands, registrations were 14.5 per 1000 population; for Vanuatu, 5.8 per thousand, and for Romania, 1 per thousand, although the latter amounted to over 500,000 registrations of security interests. [↑](#footnote-ref-0)
3. The new Companies Acts for Solomon Islands and Vanuatu also introduce for the first time in the Pacific the concept of a “community company.” This will allow community groups, including women’s groups, to incorporate for the purposes of promoting a community interest or objective. The use of these community companies should assist women in participating in the economy to a much greater extent than in the past. [↑](#footnote-ref-1)
4. The Bank of Jamaica, as the regulator of banks, has a strong interest in strengthening the banks’ system of collateralization of loans. [↑](#footnote-ref-2)
5. The views expressed in this paper do not necessarily reflect those of the InterAmerican Development Bank [↑](#footnote-ref-3)