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Attorney-General's Department
PPSA Reform Team

By email: PPSAreform@ag.gov.au

Public Consultation on the Government's response to the statutory review of the Personal Property Securities Act 2009

The Australian Financial Markets Association (**AFMA**) is providing comment on the Public Consultation on the Government's response to the statutory review of the Personal Property Securities Act 2009.

AFMA is the leading financial markets industry association promoting efficiency, integrity and professionalism in Australia's financial markets, including the capital, credit, derivatives, foreign exchange, energy, and other specialist markets, including environmental products and sustainability related and linked products. Our membership base is comprised of over 125 of Australia's leading financial market participants, from Australian and international banks, leading brokers, securities companies and state government treasury corporations to fund managers, energy companies and industry service providers.

Generally, AFMA supports the proposed amendments to the law consistent with our previous comments in the reviews and consultation since 2014. AFMA welcomes the Government objectives of providing clearer, more accessible rules for the granting, validity, and enforcement of security interests through the PPS Register and supports streamlining key concepts across the PPS framework. For AFMA members and their clients it is hoped that simplification of the PPSA could improve efficiency and provide greater certainty in terms of the PPSA's application to potential financing arrangements.

AFMA's comments are directed to three points:

- Transition
- Definition of 'account'
- Control

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1. Transition

AFMA supports a transition model from the existing regime as opposed to a grandfathering model. This would ensure that one model is applicable for all security interests posts the transition period. We believe a transition period of at least 24 months should apply.

2. Definition of 'account'

The current broad definition of 'account' may result in certain property inappropriately being characterised as an 'account', where such characterisation is incompatible with the nature and intended commercial use of such property. This is the case for so-called 'stablecoins' issued on blockchain technology. The broad definition of 'account', coupled with the proposed narrowing of the definition of 'negotiable instrument', may result in stablecoins[1] inadvertently and inappropriately being 'accounts' under the PPSA. This issue may also apply to other digital assets that include a 'monetary obligation'.

2.1. Stablecoins as 'accounts"

Because stablecoins typically include a monetary claim against the issuer (for redemption of the stablecoin), they may, unfittingly, fall within the broad definition of 'account', so that a transfer of a stablecoin may give rise to a PPSA security interest (as a 'transfer of an account'). This is inconsistent with the nature of a stablecoin, which is usually designed to be freely transferrable, like a digital form of cash. Treating a transfer of a stablecoin (eg when making a payment) as a security interest (ie as a transfer of an account) is incompatible with a peer-to-peer payment mechanism.

The current definition of account excludes 'a negotiable instrument'. The current broad definition of "negotiable instrument" arguably captures some stablecoins, so that they are excluded from also being 'accounts'. Under the proposed reforms, however, the definition of negotiable instrument is proposed to be narrowed. Stablecoins are unlikely to fall within the proposed narrower definition of negotiable instrument, with the unintended consequence that they may be characterised as 'accounts' if the reforms are implemented.

Treating a stablecoin (ie a medium of exchange) as an account under the PPSA is incompatible with the nature and intended commercial use of such property, and may adversely impact the ongoing innovation in this area. We also consider that the policy reasons for treating a 'transfer of an account' as a security interest do not apply to transactions using stablecoins on blockchain technology.

2.2. Possible solutions

Narrowing the definition of 'account' as recommended in the Whittaker Report should address the concern described above. If the current broad formulation of 'account' is retained, however, we submit that the Government consider an express exclusion to the definition of 'account' for digital assets of the kind described above.

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[1] In June 2023, the Commonwealth Treasury issued a Consultation paper on Payments System Modernisation (Licensing: Defining Payment Functions). The consultation paper proposed to regulate 'payment stablecoins' as 'stored value facilities' and explains that payment stablecoins are '*a bearer instrument that can be transferred on a peer-to-peer basis*", "*with features that make them functionally similar to fiat currency*".

We note that the issue described above is not the only way in which the PPSA impacts digital assets. We also recognise that there is ongoing work on the regulation of digital assets occurring in parallel, including Treasury's consultations on Digital Asset Platforms and Payments Reform. The appropriate characterisation and treatment of digital assets under the PPSA may depend on the outcome of those reforms and should be considered as part of those reforms. One way to address this uncertainty in the interim may be to provide that property can be excluded from relevant definitions by regulation, to allow for flexibility while the regulation of digital assets develops, and to also allow for further innovation in this dynamic area, which may bring new types of digital assets.

3. Control

AFMA supports the proposed reform for a cash account held by intermediaries to be considered as "intermediated securities" and for perfection of this account to be achieved by means of control.

There are technical difficulties with the legislation with respect to control over intermediated securities where the same party is the custodian/secured party, which are long recognised difficulties applying these control tests where the secured party is the intermediary. This is because the tests do not contemplate the intermediary and the secured party being the same party and it is not clear how the intermediary who takes a security interest over the intermediated security will satisfy these controls.

The control tests in section 26(2) of the PPSA are drafted on the assumption that the secured party and the intermediary are different while the control tests in sections 26(3A) and 26(4) may not be practicably achievable. This means that there is at least a risk that an intermediary who takes a security interest in the intermediated security (such as the Prime Broker taking the Security Interest, to the extent it is over intermediated securities) may not be able to satisfy any of the tests for control under section 26 and, as a result of these drafting ambiguities, the only way the Prime Broker can perfect its Security Interest in any intermediated securities is by registration.

The practical result is that if you get the collateral class wrong when completing the PPSA registration, then the registration is not effective and does not perfect the security interest. Similarly, if you register as a PMSI and it is not a PMSI then the entire registration is invalid. This is a common error.

Please contact David Love either on 02 9776 7995 or by email dlove@afma.com.au regarding this letter.

Yours sincerely

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