

The Maiden Civil Case and Other Related Issues

The first significant Australian judgment relating to determining priorities between competing creditors under the *Personal Property Securities Act 2009* (Cth) (PPSA) sends a clear message; what matters is having a “perfected” security interest not “title”.

Introduction

The New South Wales Supreme Court in *In the matter of Maiden Civil (P & E) Pty Ltd; Richard Albarran and Blair Alexander Pleash as receivers and managers of Maiden Civil (P & E) Pty Ltd & Ors v Queensland Excavation Services Pty Ltd* [2013] NSWSC 852 (**Maiden Civil Case**) confirms that if an owner of goods leases them to someone else, then the owner:

“...cannot rely on its title to protect its interest in the goods, instead, the owner must register its interest on the PPS register. Failure to do so may result in the owner losing the goods to other creditors;...”

What does this mean? Simply put, all owners who lease or hire out goods to third parties should take steps to protect their interest in those goods under the PPSA or risk losing them. Mere title over these goods in itself will not necessarily protect an owner’s security interest.

The Maiden Civil Case confirms the (unsurprising) reality of the PPSA and highlights the necessity for lessors and owners who have a registrable security interest to perfect their security interest or risk losing their ownership rights.

One of the stated aims of the PPSA was to preserve the rights of holders of transitional security interests during the transitional period so that they are not disadvantaged. The Maiden Civil Case puts the spotlight on this. The holder of an unregistered charge under the Northern Territory “REVs”¹ regime was not vulnerable in a liquidation scenario because there were no “void against a liquidator” consequences. In contrast, under the PPSA regime, an unregistered security interest vests in the grantor in a liquidation scenario, leaving the security holder worse off.

¹ In this article, I use the term REVs (Register of Encumbered Vehicles) as shorthand for a generic description of the various motor vehicle security registers throughout Australia.

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Whilst not relevant to the decision, the new “taking free” rules under the PPSA also apply during the transitional period and (depending on the relevant REVs jurisdiction) broaden the consequences of failing to register. On the flipside, an operating lease of (say) two months would have been registrable under the old Northern Territory REVs rules (there was no minimum period prescribed for leases) but failing to register would not have mattered once the PPSA came into force.

Maiden Civil Case - the facts in brief

Queensland Excavation Services Pty Ltd (**QES**) purchased certain caterpillar brand wheel loaders and excavators (**Caterpillars**) and leased the Caterpillars to Maiden Civil (P&E) Pty Ltd (**Maiden**) on an informal basis (there was no agreement in writing).

QES did not register its interest on the relevant Northern Territory register that was applicable prior to the PPSA coming into effect (**Relevant NT Register**). Had it done so, that registration would have been “migrated” across to the Personal Property Securities Register (**PPS Register**) and QES would have had a perfected security interest.

In about March 2012, Maiden sought short term finance from Fast Financial Solutions Pty Ltd (**Fast**). Maiden granted security to Fast over all its assets under a General Security Deed (**GSD**), and included the Caterpillars in the list of assets to be charged under the GSD. Fast registered its interest on the PPS Register.

Maiden subsequently went into administration and then liquidation.

Decision

The Court held that the arrangement between QES and Maiden was a “PPS Lease” which gave QES a deemed security interest under the PPSA (s 12(3)).

The Court held that as QES could have registered its interest in the Caterpillars on a transitional register (being the Relevant NT Register), but did not, QES was not afforded temporary perfection (s 322(3) of the PPSA and regulation 9.2 of the *Personal Property Securities Regulations 2010* (Cth)). The same result would have occurred in Western Australia with the corresponding transitional register being the Register of Encumbered Vehicles as established by the *Chattel Securities Act 1987* (WA).

Because QES did not register its security interest, it held an unperfected security interest in the Caterpillars. Fast had registered its security interest and held a perfected security interest in the Caterpillars.



Under the new PPSA law, when there are two competing security interests in the same goods, ownership becomes irrelevant in determining who might be entitled to the goods. Instead priorities are determined based on the statutory rules - in this case, the relevant rule is that a perfected security interest has priority over an unperfected security interest. Fast had a perfected security interest and QES did not and so QES essentially “lost” its ownership rights.

In addition, pursuant to s 267 of the PPSA, QES’s unperfected security interest vested in Maiden upon the company going into administration. The Court confirmed that the practical effect of this section is that QES’s security interest was extinguished and Maiden held the Caterpillars subject only to Fast’s perfected security interest.

Analysis of the nature of the security interest by the Court

As mentioned above, the Court held that the arrangement between QES and Maiden was a PPS Lease. Relevantly, a PPS Lease is a lease or bailment of goods (which does not necessarily secure payment or performance of an obligation):

- a) by a person who is regularly engaged in the business of leasing or bailing; and
- b) for a term of more than one year (90 days or more for serial numbered goods) or capable of extension to one year (or 90 days) by renewals or agreement between the parties (s 13 of the PPSA).

In my view, it is curious that the Court analysed the security interest as being a PPS Lease when the facts presented suggest that the transaction was a finance lease or hire purchase arrangement. It is clear that the Court concluded that it was the intention of the parties that Maiden would own the Caterpillars once it paid the last instalment. Would the better analysis not have been that the transaction was a security interest under s 12(1) of the PPSA, falling under the example of either s 12(2)(e) (hire purchase agreement) or s 12(2)(i) (a lease of goods)?

The introduction of the concept of a PPS Lease was to “deem” lease and bailment transactions to be security interests despite the fact that these types of transactions would not normally be thought of as secured financings. This is in line with the philosophy of the PPSA which is to consider the assumptions that a reasonable financier or buyer would be entitled to make about property in possession of a party other than the owner. For that reason, the length of time of the contract is critical in determining whether or not a PPS Lease exists. In contrast, the length of time of a true financing transaction is (quite rightly) irrelevant.



To qualify as a PPS Lease, the contract for the hire of the Caterpillars would have needed to have a term of at least 90 days. This test was satisfied in the case and so nothing turned on this issue. However, had the lease in question been for a period of two months, based on the reasoning applied in the Maiden Civil Case, the Court would, by contrast, have concluded that QES did not have a PPS Lease. Surely that conclusion would be called into question on the facts.

As an aside (because it is a question I am often asked) lessors of residential real property who lease chattels need not be concerned about having a registrable PPS Lease as there is a specific exclusion under the PPSA where the lease is of consumer property which forms part of a lease of land where the use of the property is incidental to the use and enjoyment of the land (s 13(2)(c) PPSA). This exception does not extend to commercial property.

The ability of a lessee to grant security

Drawing on well established New Zealand and Canadian authority, the Court confirmed that under the PPSA, a lessee under a PPS Lease, upon taking possession of the goods, has a proprietary interest in the goods to the extent that it can satisfy the “attachment” rules (s 19(2) of the PPSA) and can grant security interests to third parties. Fast therefore held a competing perfected security interest in the Caterpillars.

This analysis is critical to the notion that someone other than the owner can be the party granting a security interest over personal property. The Court confirmed that Fast’s perfected security interest took priority over QES’s unperfected security interest under s 55 of the PPSA (even though QES was the true owner).

The Court also rejected the argument that the effect of s 112(1) of the PPSA is to override the impact of the vesting rules by limiting the rights of the holder on enforcement to those held by the grantor (in this case the lessee).

Section 112 of the PPSA provides that “*In exercising rights and remedies provided by this Chapter, a secured party may deal with collateral only to the same extent as the grantor would be entitled to so deal with the collateral.*” The words “this Chapter” is a reference to the enforcement rules in Chapter 4 of the PPSA.

The Court confirmed that s 112 only relates to the construction of provisions in the Chapter 4 enforcement rules *when those rules are being enforced*. This is a helpful analysis to understand that the rights under the underlying contract are not replaced by the Chapter 4 provisions. The two co-exist.



Enforceability against third parties

The Court also commented that QES's security interest was not only vulnerable because it was not perfected by registration, but also because there was no written security agreement between QES and Maiden and the security interest was not enforceable against third parties under s 20 of the PPSA. Relevantly, this means that the secured party must either possess the goods (which will be unlikely) or have a written security agreement which is either signed by the grantor or adopted or accepted by an act of omission of the grantor (s 20(2)(a) of the PPSA).

With respect, although not affecting the outcome of the case, I do not agree with this comment as s 311 of the PPSA provides a specific exception to the requirements under s 20. Under section s 311 of the PPSA, transitional security interests continue to be valid as if the PPSA had never come into effect. As mentioned above, the stated intention of the PPSA was to preserve the rights of holders of transitional security interests during the transitional period so that they are no worse off. There was no equivalent of s 20 of the PPSA under pre PPSA laws therefore an oral contract would not have been fatal.

Accordingly, in the current case, to determine the enforceability of QES's security interest as against third parties, it is the old law that applies and the additional requirements under s 20 of the PPSA do not apply.

The comments concerning s 20 of the PPSA draw attention to the fact that it is important to distinguish between registration and perfection. Where possession or control are not relevant, registration is only part of perfection - under s 21(1)(b)(ii) of the PPSA, for a security interest that is not transitional to be perfected, it must also be enforceable against third parties (and satisfy the attachment rules in s.19 of the PPSA).

Accordingly, without a written security agreement that meets the requirements under s 20 of the PPSA, a lessor's ownership rights will always be vulnerable to third parties.

Regularly engaged in the business of leasing

As mentioned above, the Court held that the arrangement between QES and Maiden was a PPS Lease. To qualify the lessor (in the case of a lease) must be a person who is regularly engaged in the business of leasing.



Although this issue was not in dispute, the Court held that QES was “regularly engaged in the business of leasing” because the income from hiring the Caterpillars was QES’s only income and QES intended to continue to let the Caterpillars for hire on short-term rentals.

This outcome is consistent with Canadian decisions in that it is not the number or frequency of leases entered into by the lessor that determines whether the lessor is regularly engaged in the business of leasing (see *Karkoulas v Farm Credit Canada* (2005) 8 PPSAC (3d) 249 and *David Morris Fine Cars Ltd v North Sky Trading Inc* (1996) 11 PPSAC (2d) 14).

That being said, I query whether or not an argument could have been made that “in the business of” requires an element of the common meaning of the word “business” - being an enterprise rather than just something someone “engages in”. Take for example the WA rare coin business that recently became insolvent. Had a retiree (perhaps establishing a separate legal entity for that purpose) been a bailor of his or her rare coin collection arrangement (the WA business being the bailee) and this was the retiree’s primary source of income, is it the intention of the PPSA that the retiree would be “regularly engaged in the business of bailing”? In debating this with others I have received mixed reactions - perhaps we will hear more from the Courts on this issue in the future.

In the meantime, it is important to be aware that, depending on the circumstances, a one-off lease not commonly thought to constitute a security interest may be caught by the PPSA.

Serial numbered goods - importance of getting it right!

Whilst not relevant to the Maiden Civil Case, it is important to remember that the failure to register QES’s security interest would also have been relevant prior to a liquidation event because the “taking free” rules (and in particular section 45 of the PPSA) apply to motor vehicles during the transitional period. This is yet another example of where the PPSA can in fact alter the rights of the holders of transitional security interests to their detriment.

The important point to note is that having a valid registration under REVs does not of itself protect you from the new PPSA taking free rules. Whilst there is an exemption for transitional REVs interests to comply when it was not possible to register against a serial number under the old regime, you should still check that:

- (a) the relevant VIN or chassis number is the correct one required under the PPSA hierarchy (if there is a VIN then that is the key, if there is no



VIN but a chassis number then that is the information required and so forth);

- (b) the relevant serial number is an exact match - there could have been an error by one digit in the REVs registration which would now be fatal under the new PPSA regime; and
- (c) what does or does not comprise a motor vehicle is likely to be different and so you may need to register something that was not registrable before (for example, a caravan that has a VIN, chassis number or manufacturer's number is now registrable).

To complicate matters, in relation to REVs, the information that has migrated does not include the name of the grantor so you have to search based on the serial number that was used initially under REVs.

Where to from here?

Whilst confirming the PPSA rules on how to determine the priorities of owners and secured parties in a liquidation scenario, the Maiden Civil Case also raises a number of questions. I suspect some of the conclusions will be the subject of debate in the future.

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