

## THE *PPSA*: CONTINUING THE RECONCEPTUALISATION OF RETENTION OF TITLE (*ROMALPA*) SECURITY

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### I INTRODUCTION

With the advent of the *Personal Property Securities Act 2009* (Cth) (*PPSA*), Australia will join the United States, Canada and New Zealand in regulating personal property security with regard to function rather than form. This change will have significant consequences in relation to both the creation and perfection of broadly defined security interests in personal property and the priorities among competing security interests. Although this legislative modification will particularly alter the treatment of interests in circulating assets such as trading stock (inventory) and book debts (accounts receivable), perhaps no change will be as significant as that wrought by the definition of security interests to include retention of title clauses (and similar devices).

Because the new scheme deals with all forms of personal property security as functional equivalents irrespective of their form, the protections afforded creditors through reliance upon concepts of property title will no longer be sufficient. This change to a functionalist approach has been considered by both judges and academics as a paradigm shift, and for good reason. The experiences of the United States, Canada and New Zealand all indicate that acceptance of the new paradigm can cause some difficulty and disquiet. This is particularly so in relation to the modification (or perhaps elimination) of the concept of *nemo dat quod non habet*<sup>1</sup> when the new statutory scheme is applied to security interests broadly defined. The consequences of this change have, unfortunately, caught many (particularly those not conventionally thought of as creditors) unprepared. Those who do not quickly appreciate that their conditional sales, consignment sales, bailments and long term leases are all, like those retaining title to secure indebtedness, potentially considered security interests will find that their title to goods may pass to another as a result of a

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1 No one can give that which he or she does not have. In the context of property, this means that no one can give better title than he or she possesses.

prior perfected security interest. While this paradigm shift does have its limits (in the United States, for example, where certain personal property is subject to certification of title),<sup>2</sup> a review of the experience in Canada and New Zealand indicates that this has caused problems which will, undoubtedly, also be experienced in Australia.

In this article we will review legal principles relevant in Australia to retention of title in sale of goods contracts, and then consider the approach to retention of title under the *PPSA*. In conclusion we explore the impact of the new legislation on contracts subject to retention of title and the extent to which vendors under current contractual arrangements need to adapt to the new legal environment.

## II RETENTION OF TITLE CLAUSES – THE CURRENT POSITION

Retention of title (or ‘Romalpa’) clauses in sale of goods contracts are well-known in commerce and academic writing.<sup>3</sup> The term ‘Romalpa’ derives from

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- 2 In the United States, cars and other such equipment are evidenced by certificate of title which may limit the operation of the general provisions of *Uniform Commercial Code* (‘UCC’) Article 9. Strangely, real property is not subject to certification as in Australia or New Zealand. For a discussion of the consequences of certificate of title legislation in personal property security, see David McCrae and Alvin Harrell, ‘Overview and Update of Vehicle Secured Transactions, Certificates of Title and Related Issues’ (2010) 62 *Consumer Finance Law Quarterly Report* 342.
- 3 See, eg, Berna Collier, *Romalpa Clauses: Reservation of Title in Sale of Goods Transactions* (Lawbook Co, 1989); Gerard McCormack, *Reservation of Title* (Sweet & Maxwell, 2<sup>nd</sup> ed, 1995); Sally Wheeler, *Reservation of Title Clauses: Impact and Implications* (Oxford University Press, 1991); Denis S K Ong, ‘Romalpa Clauses’ (1992) 4 *Bond Law Review* 186; Matthew N Connock, ‘Retention of Title: Divining the Principles, Drafting a Clause’ (1994) 22 *Australian Business Law Review* 37; D I Everett, ‘Romalpa Clauses: The Fundamental Flaw’ (1994) 68 *Australian Law Journal* 404; Anthony Lo Surdo, ‘Effect of Part 5.3A of Corporations Law on Retention of Title Creditors’ (1996) 4 *Insolvency Law Journal* 63; Ray Mansueto, ‘Retention of Title Claims in the Context of Voluntary Administration’ (1996) 14 *Company and Securities Law Journal* 36; A R Brooks, ‘Retention of Title Clauses’ (1997) 5 *Insolvency Law Journal* 9; Berna Collier, ‘Uncertain Rights and Potential Liabilities: The Complex Position of Suppliers with Retention of Title Clauses and Administrators under Part 5.3A of the Corporations Law’ (1998) 9 *Journal of Banking and Finance Law and Practice* 42; John de Lacy, ‘Retention of Title Clauses & Claims Against Processed Goods’ (1998) 16 *Company and Securities Law Journal* 59; D Noakes, ‘Romalpa Clauses: Associated Alloys Pty Ltd v ACN 001 452 106 Pty Ltd’ (2000) 8 *Insolvency Law Journal* 112; Lynden Griggs, ‘The Doctrine of Fixtures: Questionable Origin, Debatable History, and a Future that is Past!’ (2001) 9 *Australian Property Law Journal* 51; Joellen Riley, ‘Trusts Created by Reservation of Title in Trade Supply Contracts’ (2001) 75 *Australian Law Journal* 348; Anthony Duggan ‘Globalisation of Secured Lending Law: Australian Developments’ (2001) 12 *Journal of Banking and Finance Law and Practice* 85; Tyrone M Carlin, ‘Associated Alloys Pty Ltd v ACN 001 452 106 Pty Ltd: A Commentary and Analysis’ (2002) 30 *Australian Business Law Review* 106; D Webb ‘Title-Based Securities and All That ROT’ [2002] *New Zealand Law Review* 199; Daniel Solomons, ‘The Regulation of Romalpa Clauses: The Limitations of Equity’ (2008) 16 *Insolvency Law Journal* 69; L Wolff, ‘Statutory Retention of Title Structures?’ (2009) 14 *Deakin Law Review* 1; Bruce Whittaker, ‘Retention of Title Clauses Under the *Personal Property Securities Act 2009* (Cth)’ (2010) 21 *Journal of Banking and Finance Law and Practice* 273; L Adams, ‘All Aboard the PPS train: The *Personal Property Securities Act 2009* (Cth)’ (2010) 22 *Australian Law Journal* 4; Anthony Duggan, ‘Some Canadian PPSA Cases and their Implications for Australia and New Zealand’ (2010) 38 *Australian Business Law Review* 161.

the seminal case in which a clause of this nature was upheld, *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd*.<sup>4</sup> Since that decision retention of title clauses have been the subject of extensive litigation (and recognition) in Australia.<sup>5</sup>

Traditionally, and in the most basic formulation, by a retention of title clause a vendor of goods seeks to retain property in and title to goods the subject of a contract of sale until the purchaser has paid in full for those goods, or complied with such other condition as the vendor may stipulate. From the perspective of rival creditors of an impecunious purchaser, or a third party sub-purchaser of the goods, the retention of title clause is of a similar nature to an unregistered security over the goods in question, but with a potential of enforceability not necessarily shared by similar contractual devices in the nature of security interests.

As is clear from decisions on point, retention of title clauses take many forms, with correspondingly varying degrees of success in enforcement by vendors. Review of cases in which courts have made determinations in relation to retention of title clauses demonstrates that, while retention of title clauses in respect of goods the subject of the original contract are generally enforceable against the original purchaser, the position is by no means so clear cut where the goods are, for example, resold, combined to become part of other goods, or affixed to land.

While retention of title clauses are creatures of contract, it is interesting to note that they are also recognised by Part 5.3A of the *Corporations Act 2001* (Cth) ('*Corporations Act*') in the context of the powers of administrators to sell goods.<sup>6</sup> Indeed for this purpose section 9 of the *Corporations Act* defines retention of title clauses as follows:

- (a) a contract for the sale of property contains a provision the effect of which is that the seller retains title in the property until the purchase price, or other amount, has been paid in full; and
- (b) the purchase price, or the other amount, as the case may be, has not been paid in full;

the property is subject to a retention of title clause under that contract.

### A The Sale of Goods Act

While retention of title clauses are creatures of contract, by including such clauses in contracts for the sale of goods vendors have traditionally relied on provisions of the (substantially uniform) sale of goods legislation enacted throughout Australia and New Zealand, in particular statutory provisions dealing with transfer of property. More particularly, the Act provides that:

4 [1976] 1 WLR 676 ('*Romalpa*').

5 This includes two decisions of the High Court of Australia: *Associated Alloys Pty Ltd v ACN 001 452 106 Pty Ltd* (2000) 202 CLR 588 ('*Associated Alloys*') and *General Motors Acceptance Corporation Australia v Southbank Traders Pty Ltd* (2007) 227 CLR 305.

6 *Corporations Act 2001* (Cth) s 442CC.

- (1) When there is a contract for the sale of specific or ascertained goods the property in them is transferred to the buyer at such time as the parties to the contract intended it to be transferred,
- (2) For the purpose of ascertaining the intention of the parties regard is to be had to the terms of the contract, the conduct of the parties, and the circumstances of the case.<sup>7</sup>

In the simplest context, a retention of title clause which provides that property in goods will not pass until, for example, payment in full is made to the vendor, operates to prevent property passing in respect of the goods to the purchaser, and further to prevent the purchaser creating a security interest in favour of third parties in respect of those goods. It is effective in cases where the purchaser retains possession of the goods, and does not convert them either by resale or incorporation into other goods or realty.<sup>8</sup>

Beyond that most basic scenario, however, priority questions can arise as between the vendor and third parties in respect of the goods. A common source of contention in proceedings involving retention of title clauses where the original purchaser of the goods was a corporation is whether the clause in fact creates a registrable, but unregistered, charge over property of the *purchaser* under the *Corporations Act*.

In circumstances where the purchaser has in turn purported to create floating or fixed charges over its property (including the goods) in favour of third parties, which charges were registered under the *Corporations Act*, the secured creditor may seek to rely on section 280(1)(b) to defeat the operation of the retention of title clause. Section 280(1)(b) provides:

- (1) A registered charge on property of a company has priority over:
  - ...
  - (b) an unregistered charge on the property created before the creation of the registered charge, unless the chargee in relation to the unregistered charge proves that the chargee in relation to the registered charge had notice of the unregistered charge at the time when the registered charge was created ...

Further, even in the absence of registered secured creditors, in circumstances where the purchaser corporation becomes insolvent, the liquidator or administrator of the purchaser corporation may be entitled to disregard the claims of the vendor of the goods pursuant to section 266 of the *Corporations Act*. Section 266 provides, so far as material, that:

- (1) Where:
  - (a) an order is made, or a resolution is passed, for the winding up of a company; or

<sup>7</sup> See *Sale of Goods Act 1896* (Qld) s 20; *Sale of Goods Act 1923* (NSW) s 22; *Goods Act 1958* (Vic) s 22; *Sale of Goods Act 1895* (SA) s 17; *Sale of Goods Act 1895* (WA) s 17; *Sale of Goods Act 1896* (Tas) s 22; *Sale of Goods 1954* (ACT) s 22; *Sale of Goods Act 1972* (NT) s 22.

<sup>8</sup> See, eg, observations of Staughton J in *Hendy Lennox (Industrial Engines) Ltd v Grahame Puttick Ltd* [1984] 1 WLR 485 in respect of circumstances where diesel engines, which remained identifiable as such, were supplied by a vendor to a purchaser, and the decisions in *John Snow & Co Ltd v DBG Woodcroft & Co Ltd* [1985] BCLC 54.

- (b) an administrator of a company is appointed under section 436A, 436B or 436C; or
  - (ba) a company executes a deed of company arrangement;
- a registrable charge on property of the company is void as a security on that property as against the liquidator, the administrator of the company, or the deed's administrator, as the case may be, unless:
- (c) a notice in respect of the charge was lodged under section 263 or 264, as the case requires:
    - (i) within the relevant period; or
    - (ii) at least 6 months before the critical day ....

Commonly, questions arise as to priority between the vendor of goods subject to a retention of title clause, and third parties who acquire an interest in the goods from the purchaser, where:

1. the purchaser resells the goods to a third party, and there is a dispute between the vendor and the third party;
2. the interest of the vendor falls within the definition of a 'security interest' pursuant to other legislation;
3. the purchaser resells the goods, and both the vendor and a secured creditor of the purchaser claim an interest in the proceeds of resale or book debts arising from the resale;
4. the purchaser affixes the goods to real property, and there is a dispute between the vendor and a third party (for example, the mortgagee of the real property to which the goods are affixed);
5. the purchaser combines the goods with other chattels, and there is a dispute between the vendor and a third party which has an interest in the nature of a security over those combined goods; and
6. the clause purports to retain ownership of the goods in the vendor until all debts owed by the purchaser to the vendor are paid, and there is a dispute between the vendor and a third party who has an interest in the current accounts of the purchaser.

The resolution of each of these matters is not always straightforward, but an understanding of the state of the current law is helpful to an appreciation of the consequences of the *PPSA*. The discussion of these points, below, also helps to inform the apparent objective, in relation to retention of title security, which the *PPSA* intends to achieve.

### **1 *The Purchaser Resells the Goods to a Third Party***

As a general rule, when goods are sold by a person who is not the owner thereof, and who does not sell them under the authority or with the consent of the owner, the buyer acquires no better title to the goods than the seller had, unless the owner of the goods is by the owner's conduct precluded from denying the

seller's authority to sell:<sup>9</sup> *nemo dat quot non habet*. However the situation changes when a third party acquires the goods in good faith from the original purchaser, and without notice of the interest of the vendor subject to a retention of title clause. This is because of the operation of State and Territory sale of goods legislation which provides, so far as material:<sup>10</sup>

Where a person having bought or agreed to buy goods obtains with the consent of the seller possession of the goods or the documents of title to the goods, the delivery or transfer by that person or by a mercantile agent acting for him of the goods or documents of title under any sale pledge or other disposition thereof to any person receiving the same in good faith and without notice of any lien or other right of the original seller in respect of the goods shall have the same effect as if the person making the delivery or transfer were a mercantile agent entrusted as such with the possession of the goods or documents of title.

It is settled law that this section places a buyer in possession of goods with the consent of the owner in the position of a mercantile agent, and validates a sale by the buyer in possession provided the other requirements of the section are met in relation to the good faith and lack of notice of the third party.

An illustration of the effect of this legislation may be seen in *Four Point Garage Ltd v Carter*.<sup>11</sup> In that case a car dealer had originally purchased a vehicle from a vendor, subject to a retention of title clause which provided, so far as material, as follows:

The buyer is advised that title to the goods contained in this invoice remains with the seller until such goods are fully paid.

A third party, in good faith and without notice of the arrangements between the original vendor and the dealer, purchased the vehicle from the dealer. The Court held that the dealer was a buyer in possession with the consent of the owner, and that the third party acquired good title to the vehicle so as to defeat the interest of the original vendor in the goods.

More recently in *GE Commercial Corporation (Aust) Pty Ltd v Mell Associates Pty Ltd*,<sup>12</sup> Palmer J held that the factual circumstances required by the legislation were established in that case by the innocent third party, who had purchased caravans from a dealer in circumstances where the caravans had been subject to a retention of title clause in favour of the original vendor.

For a vendor to protect its property in goods in circumstances where the purchaser has possession, but not ownership, it is necessary for the vendor to ensure that any third party who acquires an interest is made aware, in advance, of the vendor's ownership, so as to prevent the third party acquiring an interest in good faith and without notice. Depending on the nature of the goods, this can

9 *Sale of Goods Act 1896* (Qld) s 24; *Sale of Goods Act 1923* (NSW) s 26; *Goods Act 1958* (Vic) s 27; *Sale of Goods Act 1895* (SA) s 21; *Sale of Goods Act 1895* (WA) s 21; *Sale of Goods Act 1896* (Tas) s 26; *Sale of Goods 1954* (ACT) s 26; *Sale of Goods Act 1972* (NT) s 26.

10 *Sale of Goods Act 1896* (Qld) s 27(2); *Sale of Goods Act 1923* (NSW) s 28(2); *Goods Act 1958* (Vic) s 31; *Sale of Goods Act 1895* (SA) s 25(2); *Sale of Goods Act 1895* (WA) s 25(2); *Sale of Goods Act 1896* (Tas) s 30(2); *Sale of Goods 1954* (ACT) s 29(2); *Sale of Goods Act 1972* (NT) s 28(2).

11 [1985] 3 All ER 12, 14 ('*Four Point Garage*').

12 [2009] NSWSC 787 ('*GE Commercial Corporation*').

present practical difficulties, both because of problems associated with the vendor marking the property as its own pending payment in full by the purchaser, and because of the potential interference with the business activities of the purchaser in imposing such a requirement.

## **2 Vendor's Interest in the Goods is Subject to Other Legislation Regulating Security Interests**

The interest of a vendor in goods sold pursuant to a contract including a retention of title clause is defined, in some States, as being a 'security interest'.

The High Court in *General Motors Acceptance Corporation Australia v Southbank Traders Pty Ltd*<sup>13</sup> held that the interest of such a vendor was a security interest in Victoria within the meaning of the *Chattel Securities Act 1987* (Vic), and that the interest was extinguished for want of registration in accordance with that legislation. In summary, Southbank Traders Pty Ltd (Southbank) was a motor vehicle wholesaler. In 2002 Southbank sold ten motor vehicles to a retailer. The sale agreement contained a retention of title clause, which provided as follows:

- (1) Property in the vehicle(s) to which this invoice relates shall not pass to the purchaser until such time as the vehicle(s) to which this invoice relates, and all other vehicles supplied by the vendor to the purchaser, have been paid in full.
- (2) Until property in the vehicle(s) to which this invoice relates passes to the purchaser, or until the vehicle(s) is or are sold by the purchaser as agent for the vendor hereinafter provided:
  - ...
  - (d) the vendor may at any time recover or resell the vehicle(s) to which this invoice relates and may at any time enter upon the purchaser's premises by its servants or agents for that purpose.
- (3) Until property in the vehicle(s) to which this invoice relates passes to the purchaser, the purchaser shall not sell, encumber or dispose of the vehicle(s) except as hereinafter provided:
  - (a) the purchaser may sell the vehicle(s) in the ordinary course of its business to a bona fide purchaser for value, but only as agent for the vendor;
  - (b) the purchaser shall hold the proceeds of any sale on trust for the vendor and shall keep the proceeds separately and apart from the purchaser's own moneys; and
  - (c) the purchaser shall account to the vendor for the proceeds on demand.

While the purchase price was still unpaid, the purchaser purported to sell the vehicles to General Motors Acceptance Corporation Australia ('GMAC'), and GMAC entered into a floor plan agreement with the purchaser by which it continued possession of the goods as bailee and was able to both display the cars and sell them to members of the public. GMAC then registered a security interest under the *Chattel Securities Act 1987* (Vic) ('*Chattel Securities Act*'). Southbank

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13 (2007) 227 CLR 305 ('GMAC').

subsequently registered a security interest, and brought an action against GMAC for conversion of the relevant vehicles, or alternatively, for detinue.

'Security interest' within the meaning of the *Chattel Securities Act* is defined by section 3(1) as:

an interest in or power over goods (whether arising by or pursuant to an instrument or transaction or arising on the execution of a warrant issued under the Magistrates' Court Act 1989) which secures payment of a debt or other pecuniary obligation or the performance of any other obligation and includes any interest in or power over goods of a lessor, owner or other supplier of goods.

Section 3(3) of that Act provides further that:

For the purposes of this Act, a hirer or lessee of goods or a buyer of goods under a conditional sale is deemed to have an interest in the goods notwithstanding that title or general property in the goods has not passed to the hirer, lessee or buyer.

Priorities in respect of security interests within the meaning of the *Chattel Securities Act* are determined by section 7 (1) which provides:

Subject to section 8, if a secured party has –

- (a) an unregistered security interest (whether or not over registrable goods or interstate registrable goods); or
- (b) a registered inventory security interest –

in goods but is not in possession of the goods and a purchaser purchases or purports to purchase an interest in the goods (otherwise than at a sale in pursuance of a process of execution issued by or on behalf of a judgment creditor) for value in good faith and without notice when the purchase price is paid (or, if the price is not paid at one time, when the first part of the purchase price is paid) of the security interest from a supplier being –

- (c) the debtor; or
- (d) another person who is in possession of the goods in circumstances where the debtor has lost the right to possession of the goods or is estopped from asserting an interest in the goods against the purchaser –

the security interest of the secured party is extinguished.

Significantly, the *Chattel Securities Act* also provides that section 31 of the *Goods Act 1958* (Vic), which in defined circumstances permits a buyer in possession to confer good title on an innocent third party purchaser, has no effect in relation to transfers of 'registrable goods'.<sup>14</sup> Registrable goods include motor vehicles and trailers.<sup>15</sup>

The High Court found that an 'other supplier of goods' for the purposes of section 3(1) of the Act extended to include a vendor of goods under a conditional sale in which title or general property in the goods had not passed to the buyer. The matter was remitted to the Court of Appeal of Victoria, however it followed that as Southbank's interest as owner in the vehicles was a registrable security interest under the Act, it had been extinguished by the purchase of the vehicles by GMAC.

<sup>14</sup> *Chattel Securities Act 1987* (Vic) s 7(6).

<sup>15</sup> *Chattel Securities Act 1987* (Vic) s 13.



It is interesting to compare this case with the decisions in *Four Point Garage* and *GE Commercial Corporation*. While the outcome was effectively the same – the interest of the original vendor was extinguished – in Victoria in the *GMAC* case this occurred because the vehicles were in fact ‘registrable goods’ the vendor could – and, it appears, should – have protected its interest by registration, that avenue was not available under the sale of goods legislation. The principles articulated by the High Court in *GMAC* are equally applicable in Western Australia because of the operation of the *Chattel Securities Act 1987* (WA), which is, so far as is material, identical to the Victorian statute.

The position in respect of comparable legislation elsewhere in Australia is less clear-cut. In New South Wales and the Northern Territory, for example, ‘security interest’ means an interest or power

- (a) reserved in or over an interest in the goods, or
- (b) created or otherwise arising in or over an interest in the goods under a bill of sale, mortgage, charge, trust or power,

by way of security for the payment of a debt or other pecuniary obligation or the performance of any other obligation but does not include an interest or a power reserved or created, or otherwise arising, under a lease or hire-purchase agreement or an agreement excluded from this definition by the regulations.<sup>16</sup>

While not as broad as the definition under the *Chattel Securities Act 1987* (Vic), potentially this definition could extend to the interest of a vendor under a retention of title clause, although the reference to an interest being reserved by way of security, and the absence of reference to ‘any other supplier of goods’ which was of importance in the *GMAC* case, may militate against such an inference being drawn. A similar result appears to follow from consideration of the definition of ‘security interest’ in section 3 of the *Security Interests in Goods Act 2005* (NSW), which replicates the definition in the *Registration of Interests in Goods Act 1986* (NSW) but specifically excludes an interest or a power reserved or created, or otherwise arising, by or under any of the following:

- a letting of goods with an option to purchase the goods,
- an agreement for the purchase of goods by instalments (whether described as rent or hire or otherwise) not being an agreement by which the property in the goods being purchased passes at the time of the agreement or on, or at any time before, delivery of the goods,
- any other contract for the hiring of goods, or
- any other agreement, arrangement, instrument or circumstance of a kind prescribed by the regulations.

In Queensland, South Australia, Tasmania and the Northern Territory the definition of ‘security interest’ is even more specific than that in New South

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<sup>16</sup> *Registration of Interests in Goods Act 1986* (NSW) s 3(1); *Registration of Interests in Motor Vehicles and Other Goods Act 1989* (NT) s 3(1) (emphasis added).

Wales and, in light of the limitations in the definition, appears not to include the interest of a vendor under a retention of title clause.<sup>17</sup>

### **3 *The Purchaser Resells the Goods, and Both the Vendor and a Secured Creditor of the Purchaser Claim an Interest in the Proceeds of Resale or Book Debts Arising from the Resale***

Prior to the decision of the High Court of Australia in *Associated Alloys*,<sup>18</sup> it was uncertain whether a clause purporting to 'retain' ownership of proceeds of resale was effective. This issue had been the subject of dispute since the original *Romalpa* case where the Court held that the proceeds of resale in the hands of the purchaser were traceable by the original vendor.

A key issue of discussion in cases after *Romalpa* was whether it was necessary to establish a fiduciary relationship between the original vendor and the purchaser before a tracing remedy could exist in respect of proceeds of resale of the original goods supplied. The debate had substantially concentrated upon whether the retention of title clause allowed the tracing and recovery by the supplier of the proceeds of sub-sale, and whether it actually created the necessary fiduciary relationship in the first place. Interestingly, the trend of authorities supported the proposition that, because the source of the supplier's right to trace these proceeds of sale was the contractual agreement between the parties rather than equitable principles which might have applied in the absence of such agreement, and because the interest of the supplier in the proceeds was defeasible upon payment by the purchaser of the amount outstanding in respect of the goods, any interest of the supplier in the proceeds of sub-sale was by way of unregistered charge.<sup>19</sup>

In *Associated Alloys* the vendor sold steel to the buyer over a number of years subject to a retention of title clause. The only part of the clause in dispute was sub-clause 5, which read as follows:

In the event that the Buyer uses the goods/product in some manufacturing or construction process of its own or some third party, then the [Buyer] shall hold such part of the proceeds of such manufacturing or construction process as relates

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17 For example, section 2 of the *Motor Vehicles and Boats Securities Act 1986* (Qld) defines security interest as meaning 'an interest in a motor vehicle, boat or outboard motor by way of security for or in respect of a liability, whether present, contingent or future created or otherwise arising in or under or in connection with a bill of sale, mortgage, charge, lien, hire-purchase agreement, lease or instrument having a like effect to any of them' and includes the interest of an owner within the meaning of the *Hire Purchase Act 1959* (Qld) and that of a lessor. Cf *Goods Securities Act 1986* (SA) s 3(1); *Motor Vehicles Securities Act 1984* (Tas) s 3; *Sale of Motor Vehicles Act 1977* (ACT) s 32A. Further, in these jurisdictions the operation of the legislation is currently confined to motor vehicles and other defined chattels.

18 (2000) 202 CLR 588.

19 See, eg, *Tatung (UK) Ltd v Galex Telesure Ltd* (1989) 5 BCC 325; *Chattis Nominees Pty Ltd v Norman Ross Homeworks Pty Ltd (Receiver Appointed) (in liq)* (1992) 28 NSWLR 338; *Modelboard Ltd v Outer Box Ltd (in liq)* (1993) BCLC 623; *Compaq Computer Ltd v The Abercorn Group Ltd* [1993] BCLC 602. Cf *Peerless Carpets Ltd v Moorhouse Carpet Market Ltd (rec apptd)* (1992) 4 NZBLC 99-266, where the Court observed that that the proceeds were to be held on trust for the vendor pending payment in full, and held that the clause should be interpreted as it read.

to the goods/products in trust for the [Seller]. Such part shall be deemed to equal in dollar terms the amount owing by the [Buyer] to the [Seller] at the time of the receipt of such proceeds.

The High Court considered that the proper construction of the phrase ‘the proceeds’ included reference to moneys received by the buyer, and not debts in the buyer’s books. A term was, of necessity, implied into the contract between the parties providing for the discharge of the debt when a trust was constituted under sub-clause (5) ‘equal in dollar terms [to] the amount owing by the [Buyer] to the [Seller] at the time of the receipt of such proceeds.’ The sub-clause was an agreement to constitute a trust of future-acquired property, and therefore was not a ‘charge’ requiring registration under the corporations legislation.

In light of this decision it is important that the retention of title clause is not drafted in a way that extends the rights of the vendor beyond an interest in the original property sold. So, for example, a clause which attempted to allow the vendor to require the buyer to assign its claims against sub-purchasers to the vendor without specific limitation regarding the amounts owed by the buyer to the original vendor has been struck down as an unregistered charge.<sup>20</sup> As is clear from *Associated Alloys*, the trust implied in respect of the proceeds of resale is referable to the goods the subject of the original sale, and no more.

Further, it appears that it is necessary for the clause to refer specifically to the proceeds of sale to support the existence of a trust as found in *Associated Alloys*. In the absence of specific reference to a continuing interest of the original vendor in the proceeds of sale, the Court may be reluctant to imply such an interest.<sup>21</sup>

#### 4 *The Purchaser Affixes the Goods to Real Property*

Where goods the subject of a retention of title clause are attached to land, it is important to ascertain whether they have become fixtures. If they have become fixtures, the legal title of the supplier in the goods will cease notwithstanding the existence of the clause: *Whenuapai Joinery (1988) Ltd v Trust Bank Central Ltd*.<sup>22</sup> In circumstances however, where the clause gave the supplier the right to enter on to the land and take possession of the goods notwithstanding that the goods have become fixtures, there is authority that the supplier will have an equitable interest in the land to enter and recover the goods: *Perron Investments Pty Ltd v Tim Davies Landscaping Pty Ltd*.<sup>23</sup> A retention of title clause which is silent in relation to the issue of entry on to the land and recovery of goods which become fixtures does not operate to create an enforceable interest in the relevant

20 *E Pfeiffer Weinkellerei-Weineinkauf GmbH & Co v Arbuthnot Factors Ltd* [1988] 1 WLR 150. In that case the clause included the following provision: ‘All claims that he gets from the sale ... regarding our goods, with all rights including his profit amounting to his obligations towards us, will be passed on to us.’

21 As was the case in *Toveill Pty Ltd v Australian Quality Plus Pty Ltd* [2010] NSWSC 1003 (7 September 2010).

22 [1994] 1 NZLR 406, 410–1.

23 [2009] WASCA 171 (7 October 2009) [13].

land in the supplier of the goods: *Hardie Finance Corporation Pty Ltd v Ahern [No 3]*.<sup>24</sup>

Where a third party has an interest in that land – for example, a mortgagee or a charge-holder - then depending on the nature of the third party's interest (for example, whether it is legal or equitable) the supplier may be unable to enforce the interest in land created by the Romalpa clause so as to recover the goods: *Trust Bank Central Ltd v Southdown Properties Ltd & Ors*.<sup>25</sup>

### 5 *The Purchaser Combines the Goods with Other Chattels*

Where goods supplied subject to a retention of title clause are mixed irretrievably with other goods of the purchaser in a manufacturing process, a clause asserting ownership over the supplied goods only will be ineffective for the reason that the supplied goods themselves have ceased to exist: *Borden (UK) Ltd v Scottish Timber Products Ltd*.<sup>26</sup> Similarly, where the goods the subject of the clause are attached to other goods with the result that the separation would result in damage to the product as a whole, the Romalpa clause cannot be enforced so as to repossess the goods.<sup>27</sup>

On the other hand, if the goods can be separated without damage, the clause is effective and the vendor may seek to recover them in the event of non-payment: *Hendy Lennox (Industrial Engines) Ltd v Grahame Puttick Ltd*.<sup>28</sup> Where the material supplied by the vendor is altered by the purchaser but without changing its substance, the courts have been more ambivalent. So, in *Pongakawa Sawmill Ltd v New Zealand Forest Products Ltd*<sup>29</sup> the Court of Appeal of New Zealand held that a retention of title clause in respect of tree logs continued to be effective in respect of sawn timber from those logs, whereas in *Chaigley Farms Ltd v Crawford, Kaye & Grayshire Ltd (t/a Leylands)*<sup>30</sup> the Court held that a retention of title clause in respect of live animals supplied for slaughter did not extend to the carcasses of the animals after slaughter.

In any event, as was clear from the decision of the High Court in *Associated Alloys*, in circumstances where the clause specifically *contemplates* a manufacturing process involving the goods and provides that such part of the proceeds of such manufacturing or construction process as relates to the goods shall be in held in trust for the vendor, effectively the clause operates to create a continuing interest in the goods notwithstanding that they have ceased to exist in the form in which they were sold.

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24 [2010] WASC 403 (22 December 2010) [328].

25 (1992) ANZ Conv R 247, 251.

26 [1981] Ch 25, 44–5. In this case the subject of the retention of title clause was resin, which was mixed by the purchaser with other substances to make chipboard. The Court held that the retention of title clause in relation to the resin did not extend to the chipboard, notwithstanding that the Court accepted that a percentage of the chipboard was constituted by the resin.

27 *Rendell v Associated Finance Pty Ltd* [1957] VR 604, 609.

28 [1984] 1 WLR 485, 497–9. In this case diesel engines were held severable from the generators to which they had been connected by the purchaser.

29 [1992] 3 NZLR 304.

30 [1996] BCC 957.

### **6 The Clause Purports to Retain Ownership of the Goods in the Vendor until All Debts Owed by the Purchaser to the Vendor are Paid**

The courts have upheld the use of retention of title clauses which claim to vest ownership in the vendor of goods supplied not only until the goods themselves have been paid for, but until *all* goods supplied by the vendor to the purchaser have been paid for. This type of clause is known as an ‘all-debts’ or ‘current account’ clause: *Puma Australia Pty Ltd v Sportsman’s Australia Ltd*,<sup>31</sup> *Chattis Nominees Pty Ltd v Norman Ross Homeworks Pty Ltd (rec apptd) (in liq)*<sup>32</sup> and *Geal Investments Ltd v Ivil Hotels Ltd (rec apptd)*.<sup>33</sup>

The benefits to a supplier of using an all debts clause are illustrated by the facts in *Geal Investments*. In that case Supplier (1) sold goods to the purchaser with an all debts retention of title clause, whereas the retention of title clause in the contract between Supplier (2) and the purchaser merely allowed Supplier (2) to retain ownership of the goods specifically supplied until those specific goods had been paid for. When the purchaser became insolvent it was possible to identify certain goods as having been supplied by Supplier (1) and others by Supplier (2), however it was not possible to ascertain which goods of either supplier had been paid for. In the circumstances, Supplier (1) was able to point to its all debts retention of title clause and recover possession of goods in the possession of the purchaser which it had supplied. Supplier (2) however could not identify unpaid goods, and was unable to recover possession of any goods in the possession of the purchaser.

## **III THE PPSA AND RETENTION OF TITLE**

### **A Background**

Like many law reform developments, the revision of personal property security law concepts which has now arrived in Australia proceeded on a geographically circuitous route, originating in the United States with its *UCC* Article 9, proceeding next to the Canadian Provinces’ personal property security legislations, and thence to the *Personal Property Securities Act 1999* (NZ) (‘*NZPPSA*’). While each of these developments may have been motivated by unique deficiencies within each country’s pre-reform circumstance, all now accept the importance of public registration of security interests based upon a consideration of the function rather than the form of the transaction. While these changes were not primarily intended to alter retention of title, the conceptual consequences on retention of title is somewhat revolutionary.

In the United States, it was long accepted that possession was the oldest and most trustworthy way to provide security over a chattel. Originally, this meant that to create a valid security interest in property required transfer of possession

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31 (1994) 2 Qd R 149.

32 (1992) 28 NSWLR 338.

33 (1992) 4 NZBLC 99-280 (‘*Geal Investments*’).

to the creditor or secured party. Non-possessory security interests were originally considered fraudulent and invalid against third parties, based upon the likelihood that creditors would rely upon the debtor's apparent ownership of assets within his possession.<sup>34</sup> One major deficiency of the law as it stood in the United States at the turn of the twentieth century was the inability of debtors to provide security over a circulating group of assets (such as inventory or accounts receivables).<sup>35</sup> Debtors and creditors exercised their ingenuity to accommodate non-possessory security interests in personal property; however, the various methods adopted from state to state left the law of personal property security somewhat in disarray, being described as a 'labyrinthine melange.'

Article 9 brought this 'labyrinthine'<sup>36</sup> melange of personal property security law under one roof. It legitimized the status of non-possessory interests and provided a workable mechanism – filing in a public office – for satisfying the requirement that potential creditors be put on notice that certain assets of the debtor might be subject to claims by others.<sup>37</sup>

In addition to allowing the equivalent of the English 'floating charge',<sup>38</sup> Article 9 introduced the concept of a public registry of personal property security interests based upon function rather than form. As a matter of law reform, the changes brought about in relation to personal property security (predominantly found in Article 9) were certainly some of the most significant of the *UCC* developments. As part of this concept alteration, retention of title was dealt with simply:

The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer ... is limited in effect to a reservation of a 'security interest'.<sup>39</sup>

While Canadians did not suffer from the inability to secure assets of circulating capital,<sup>40</sup> the comprehensive approach of Article 9 to the numerous

34 For a discussion of these points, see Kenneth C Kettering, 'Securitization and Its Discontents: The Dynamics of Financial Product Development' (2008) 29 *Cardozo Law Review* 1553, 1593–6.

35 Known respectively in the English common law world as trading stock and book debts. United States law never developed the equitable floating charge. William James Gough, *Company Charges* (Butterworths, 2<sup>nd</sup> ed, 1996) 437–8. See, eg, *Benedict v Ratner*, 268 US 353 (1925).

36 As described by James Angell MacLachlan, *Handbook of the Law of Bankruptcy* (St Paul, West Pub Co, 1956) 257.

37 Peter J Coogan, 'Article 9: An Agenda for the Next Decade' (1978) 87 *Yale Law Journal* 1012, 1015–6, citing Grant Gilmore, *Security Interests in Personal Property* (Little, Brown & Co, 1965) 283–316 and 462–3.

38 Grant Gilmore, *Security Interests in Personal Property* (Little, Brown & Co, 1965) 357; Peter J Coogan summarises in 'Article 9: An Agenda for the Next Decade' (1978) 87 *Yale Law Journal* 1012, 1016 that: Article 9 rejected *in toto* the old notion that non-possessory interests in after-acquired property are suspect. It dramatically expanded the parties' freedom to create security interests in all kinds of after-acquired collateral, regardless of the ultimate nature of the collateral. The best-known example, and perhaps the most widely used financing device under Article 9, is the security interest in present and future inventory and accounts receivable.

39 *UCC* § 1-201(35).

40 See Ronald C C Cumming, 'Article 9 North of 49°: The Canadian PPS Acts and the Quebec Civil Code' (1996) 29 *Loyola of Los Angeles Law Review* 971, 972:

personal property security devices (the Canadian position being described as 'Byzantine'<sup>41</sup>) made its systematic approach evermore attractive as technology improved the use of the public register of charges. After Ontario initially enacted a Personal Property Security Act in 1986, each of the common law provinces of Canada followed.<sup>42</sup> Each of these enactments, though not identical, traced their common intellectual origins to the *UCC* Article 9, and all moved to a functional approach to security interests which meant that retention of title clauses to secure future performance were included within that concept.

It is not surprising that a systematised and comprehensive model for registration of functionally defined security interests, enacted in the various United States in the 1960s would find a favourable reception in Canada, an immediate neighbour and major trading partner. The merits of such a system in the antipodes, however, would necessarily be based upon the inherent benefits judged without concern as to any perceived value arising from harmonisation of the laws of close trading partners. In 1989 the New Zealand Law Commission presented its Report No 8, *A Personal Property Securities Act for New Zealand* which strongly endorsed the enactment of an Article 9 type regime.<sup>43</sup> The chaotic nature of personal property security law in New Zealand was described emotively as a quagmire<sup>44</sup> rather than as merely labyrinthine or Byzantine, the descriptors used in North America. Although the benefits had been clearly identified, the New Zealand legislation was enacted only in 1999. With the new paradigm of personal property security being adopted in New Zealand, the benefits of such a system re-energized attempts to bring similar legislation to

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Canadian provinces did not place legislative shackles on the equitable mortgages of after-acquired property as was done in England, with the result that this form of mortgage was used, from an early period, for agricultural and business financing. Under the principle established by the House of Lords in the pivotal decisions in *Holroyd v Marshall* and *Tailby v Official Receiver*, secured financing on the security of existing and future accounts of businesses was frequently used in all common-law provinces prior to enactment of the PPSAs.

41 'By the 1960s, personal property security law [in Canada] had become almost Byzantine in its complexity and lack of consistency': Cuming, above n 40, 973.

42 *Personal Property Security Act*, RSO 1990, c P-10 ('*OPPSA*'); *Personal Property Security Act*, RSM 1993, c P-35 ('*Manitoba PPSA*'); *Personal Property Security Act*, SS 1993, c P-6.2 ('*Sask PPSA*'); *Personal Property Security Act*, RSY 1986, c 130 ('*Yukon Territory PPSA*'); *Personal Property Security Act*, SA 1988, c P-4.05 ('*Alberta PPSA*'); *Personal Property Security Act*, RSBC 1996, c-359 ('*BCPPSA*'); *Personal Property Security Act*, SNB 1993, c P-7.1 ('*New Brunswick PPSA*'); *Property Security Act*, SNS 1995-96, c 13 ('*Nova Scotia PPSA*'); *Personal Property Security Act*, SPEI 1997, c 33 ('*Prince Edward Island PPSA*'); *Personal Property Security Act*, SNWT 1994, c 8 ('*Northwest Territories PPSA*'); *Personal Property Security Act*, SNWT (Nu) 1994 c 8 ('*Nunavut PPSA*'); *Personal Property Security Act*, SNL 1998, c P-7.1 ('*Newfoundland and Labrador PPSA*'). Even the Quebec Civil Code has adopted a number of the features of central registration of the civil law equivalent of security interests: see Cuming, above n 40.

43 This followed on from New Zealand Law Commission, *Reform of Personal Property Security Law*, Preliminary Paper No 6 (1988).

44 Stefan A Reisenfeld, *The Quagmire of Chattels Security in New Zealand* (Legal Research Foundation, School of Law, University of Auckland, 1970), cited by Anthony Duggan and Michael Gedye, 'Personal Property Security Law Reform in Australia and New Zealand: The Impetus for Change' (2009) 27 *Penn State International Law Review* 655, 659.

Australia.<sup>45</sup> Likewise, the close contact between New Zealand and Australia made both the benefits of the New Zealand system more obvious to Australians, while presenting clear detriments to continuing with the pre-existing position.<sup>46</sup>

Despite the fact that comparable jurisdictions have had personal property securities regimes in place for many years, Australia has been among the last to begin the process of legislative reform.<sup>47</sup> In comparison with laws relating to real property, laws dealing with security over personal property in Australia had developed in a haphazard fashion, perhaps typified by what has been described as ‘that famous body of ill-drafted legislation known as the Bills of Sale Acts’.<sup>48</sup> The first serious step on the way to reform occurred on 11 April 2006 when the Standing Committee of Attorneys-General released an Options Paper entitled ‘Review of the law on Personal Property Securities’. The Options Paper identified three fundamental problems in the existing law, namely:

1. the problematic nature of taking security over personal property;
2. the plethora of types, registration systems, and administrative bodies involving personal property security in Australia at both federal and State levels; and
3. the potential for gaps, overlaps and conflicts to exist between differing systems.

Significantly for the purposes of this paper, in 2007 the then Federal Attorney-General, Philip Ruddock, declared that a fundamental objective of personal property law reform was to ensure that lenders and purchasers entering into transactions involving personal property would be able to check cheaply and easily on the internet whether there was an encumbrance in the property.<sup>49</sup>

As the Explanatory Memorandum to the *PPSA* states, the *PPSA* relies on the Commonwealth’s own constitutional power and power referred to it by the States

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45 The continuous instigation for this reform by Professor David Allan, a colleague and friend of many who have contributed to this Thematic Issue 34(2), is certainly acknowledged and appreciated:

Professor Allan almost single-handedly managed to keep the issue alive, by convening stakeholder workshops at Bond University in 1995 and 2002, [see (2002) 14 *Bond Law Review*] by exploiting his connections with the Banking Law Association and, generally, by taking every available opportunity to prod reluctant governments into action.

Duggan and Gedye, above n 44, 657.

46 The difficulties with differing characterisation of retention of title is addressed in Juliet Taylor, ‘Retention of Title and the Trans-Tasman Supply of Goods’ (2006) 12 *New Zealand Business Law Quarterly* 71.

47 Earlier papers on this topic came from the Molomby Committee, an ad hoc committee of the Law Council of Australia produced for the Attorney-General of Victoria, in 1972, the Victorian Law Reform Commission and the Queensland Law Reform Commission in 1992, the New South Wales Law Reform Commission and the Australian Law Reform Commission, and the Business Law Division of the Commonwealth Attorney-General’s Department.

48 Edward I Sykes and Sally Walker, *The Law of Securities* (Lawbook, 5<sup>th</sup> ed, 1993) 530–1. A number of these Acts remain in operation: see *Bills of Sale and Other Instruments Act 1955* (Qld); *Bills of Sale Act 1886* (SA); *Bills of Sale Act 1900* (Tas); *Bills of Sale Act 1899* (WA). The complexity of the pre-*PPSA* position can be seen from the fact that the *PPSA* amends or replaces provisions in over seventy Australian State, Territory and Commonwealth Acts.

49 Attorney-General’s Department (Cth), ‘Personal Property Securities Reform’ (Media Release, 8 May 2007).



under section 51(xxxvii) of the Constitution.<sup>50</sup> The legislation is also modelled on the New Zealand, Canadian and US legislation, drawing on work by the United Nations Commission on International Trade Law (UNCITRAL) and the International Institute for the Unification of Private Law (UNIDROIT).

The Personal Property Securities Bill was introduced into the House of Representatives on 24 June 2009 and received Royal Assent on 14 December 2009. It commenced on 15 December 2009, however in light of extensive transitional provisions the regime is not expected to take effect until early 2012.

The Explanatory Memorandum identified the following key features of the legislation:

- the Bill would establish a single national law governing security interests in personal property;
- the concept of ‘security interest’, which attaches to personal property when the grantor has rights in the collateral and value is given or the grantor does an act which creates the security interest;
- the establishment of a public Register of Personal Property Securities (‘the PPS Register’) which would contain details of registered security interests in personal property;
- the concept of ‘perfection of a security interest’, which occurs when a security interest attaches to personal property and the secured party takes possession and/or control of the property, or registers it on the PPS Register;
- definition of circumstances when personal property would be able to be acquired free of a security interest; and
- definition of default rules for determining priority between competing security interest in the same property, including special priority rules for specific transactions including purchase money security interests, accessions and commingled goods.

The *PPSA* has been amended by:

- *Personal Property Securities (Consequential Amendments) Act 2009* (Cth),<sup>51</sup> and
- *Personal Property Securities (Corporations and Other Amendments) Act 2010* (Cth).

The Personal Property Securities (Corporations and Other Amendments) Bill 2011 contains the final set of amendments to the *PPSA*, and consequential amendments to other Commonwealth legislation prior to the *PPSA* coming into effect later in early 2012.

<sup>50</sup> Explanatory Memorandum, Personal Property Securities Bill 2009 (Cth) 10.

<sup>51</sup> This also amends 25 statutes relating to fisheries, intellectual property, maritime and other legislation to enable the creation, registration, priority, extinguishment or enforcement of interests in personal property.

In considering the impact of the *PPSA* on current principles relating to retention of title, it is important to first note the following concepts under the legislation.

### B 'Security'

In the first instance, a security interest in respect of personal property is required in order to register under the *PPSA*.<sup>52</sup> 'Security interest' in personal property is defined as including '... conditional sale agreement (including an agreement to sell subject to retention of title).'<sup>53</sup> The traditional distinction between continuing *ownership* of goods by the vendor pursuant to a retention of title clause, and a security interest which can only be created by a person who actually owns the goods, is rejected in the *PPSA* which adopts a functional definition of security interest by reference to the effect of the transaction. Accordingly, it follows that the interest of a seller in goods subject to a retention of title clause is a 'security interest' for the purposes of the *PPSA*.

### C 'Perfection' of Security Interests

In order to register this interest, the security holder must 'perfect' the security interest in particular 'collateral'. Section 21 (1) of the *PPSA* provides that this occurs if:

- (a) the security interest is temporarily perfected, or otherwise perfected, by force of this Act; or
- (b) all of the following apply:
  - (i) the security interest is attached to the collateral;
  - (ii) the security interest is enforceable against a third party;
  - (iii) subsection (2) applies.

Section 21 (2) provides, so far as material, that it applies if:

- (a) for any collateral, a registration is effective with respect to the collateral; or
- (b) for any collateral, the secured party has possession of the collateral (other than possession as a result of seizure or repossession).

In the *PPSA*, 'collateral' primarily means personal property to which a security interest is attached. In respect to registration of a security interest the *PPSA* provides that 'collateral' includes personal property described by the registration.<sup>54</sup>

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<sup>52</sup> *PPSA* s 12(1).

<sup>53</sup> *PPSA* s 12(2)(d).

<sup>54</sup> *PPSA* s 10.

### D 'Purchase Money Security Interest'

The *PPSA* also creates a security interest called a 'Purchase Money Security Interest'<sup>55</sup> ('PMSI') which, subject to some exceptions,<sup>56</sup> is defined as any of the following:<sup>57</sup>

- (a) a security interest taken in collateral, to the extent that it secures all or part of its purchase price;
- (b) a security interest taken in collateral by a person who gives value for the purpose of enabling the grantor to acquire rights in the collateral, to the extent that the value is applied to acquire those rights;
- (c) the interest of a lessor or bailor of goods under a PPS lease;
- (d) the interest of a consignor who delivers goods to a consignee under a commercial consignment.

A PMSI offers a form of 'super priority' over other security interests, but only to the extent of personal property<sup>58</sup> that is the subject of a specific sale agreement including, for these purposes, a retention of title clause. A perfected PMSI has priority over other perfected security interests when the PMSI concerns 'inventory' or its proceeds.<sup>59</sup> <sup>60</sup> A PMSI is perfected in the same way as other security interests.<sup>61</sup> In this case, 'inventory' includes goods that are held by a person as raw materials or as work in progress, or held, used or consumed by a person, as materials.<sup>62</sup>

### E Priority

Under the *PPSA*, as a general rule:

- (a) perfected interests have priority over unperfected interests; and
- (b) priority between perfected interests amongst themselves, and unperfected interests amongst themselves, is determined on a first-in-time basis.<sup>63</sup>

### F Third Parties

Similarly, a buyer or lessee of personal property, for value, takes the personal property free of an unperfected security interest in the property.<sup>64</sup> This is not the

55 For an early discussion on PMSI, see Australian Law Reform Commission, *Personal Property Securities*, Report No 64 (1993) [7.2]–[7.6]. In the UK, see Law Commission, *Registration of Security Interests: Company Charges and Property other than Land*, Consultation Paper No 164 (2002) [7.71]–[7.73].

56 *PPSA* s 14(2).

57 *PPSA* s 14(1).

58 But not personal property of low value or which is intended for use predominantly for personal, domestic or household purposes and in certain other cases: *PPSA* s 14(2).

59 *PPSA* s 62(2)(a).

60 *PPSA* s 10: Definitions of 'proceeds'.

61 *PPSA* s 21.

62 *PPSA* s 10(c), (d): Definitions of 'inventory'.

63 Pt 2.6. Default priority rules are set out in *PPSA* s 55.

64 *PPSA* s 43(1).

case if the unperfected security interest was created or provided for by a transaction to which the buyer or lessee is a party.<sup>65</sup>

### G The Register

The Personal Property Securities Register will be electronic and computer-based, updated in real time, and publicly accessible around the clock.<sup>66</sup> A number of existing State and Territory registers will be migrated to the register.<sup>67</sup>

#### H Specific Scenarios Relating to Retention of Title

The ‘super priority’ effect of the Purchase Money Security Interest (PMSI), mentioned earlier, must be considered in each of the following scenarios because, to the extent of the ‘super priority’ accorded to personal property within its scope, it modifies and prevails over most, if not all, the other security interests discussed in these scenarios. It is important to note that a purchase money security may be created notwithstanding the existence of other pre-existing security interests in after-acquired property. To this extent, it is the provision in the *PPSA* that most closely replicates a ‘simple’ Romalpa clause under the former law.<sup>68</sup>

The following example in the Explanatory Memorandum to the *PPSA* demonstrates its effect:

#### Example

Grant A is a wholesaler of car radios. Grant A purchases car radios from Manufacturer A, financed by Bank B. Bank B has a security interest in Grant A’s all present and after acquired property but does not have a purchase money

65 *PPSA* s 43(2).

66 See Personal Property Securities Register <[www.ppsr.gov.au](http://www.ppsr.gov.au)>; David Bergman, ‘PPS Essentials: How will the Reforms Affect Insolvency Practitioners?’ (2011) 23(1) *Australian Insolvency Journal* 44.

67 *Commonwealth*: Australian Register of Ships (mortgages only), ASIC - Register of Company Charges (including provisional charges), Fisheries Register.  
*New South Wales*: Register of Encumbered Vehicles (REVS NSW), Security Interest of Goods Register: stock mortgages originally registered under the *Liens on Crops and Wool and Stock Mortgages Act 1989* (NSW), Bills of Sale from 1 January 2000, current crop mortgages and all other interests registered under the *Security Interests in Goods Act 2005* (NSW), Register of Co-operative Charges.  
*Queensland*: Register of Encumbered Vehicles (REVS Qld), Bills of Sale Register (including Register of Liens on Crops of Sugar Cane), Register of Co-operative Charges.  
*South Australia*: Vehicle Securities Register, Bills of Sale Register, Stock Mortgages and Wool Liens Register, Liens on Fruit Register, Register of Co-operative Charges.  
*Tasmania*: Register of Vehicle Security Interests, Register of Bills of Sale, Stock, Wool and Crop Mortgages and Co-operative Charges.  
*Victoria*: Vehicle Securities Register, Register of Liens on Wool and Stock Mortgages (stock mortgages only), Register of Co-operative Charges.  
*Western Australia*: Register of Encumbered Vehicles (REVS WA), Bills of Sale Register.  
*Australian Capital Territory*: Register of Encumbered Vehicles (REVS ACT - from REVS NSW), General Register of Deeds and Instruments, Register of Co-operative Charges.

68 Amanda Bull Thynne, ‘Purchase Money Security Interests and the Default PPSA Priority Rules: An Overview’ (2011) 26(10) *Australian Banking and Finance Law Bulletin* 167, 169; Aidan Drinkwater, ‘The Rise and Fall of Purchase Money Security Interests at General Law and under Article 9 Regimes’ (2010) 21 *Journal of Banking and Finance Law and Practice* 5, 13–4.

security interest. Grant A decides to take up Manufacturer A's offer to supply the car radios on a deferred payment basis. Manufacturer A would have a purchase money security interest in the car radios supplied after this time.<sup>69</sup>

Taking account of this, and the general principles discussed above, it is useful to determine how the *PPSA* will now apply to the common questions of priority involving retention of title clauses discussed earlier before turning to a more general analysis of potential impacts of the legislation on commercial arrangements where vendors seek to retain an interest in goods.

### 1 *Retention of Title and the PPSA – the Purchaser Resells the Goods to a Third Party*

As explained earlier, the current rule applying to this circumstance is *nemo dat quot non habet*, except when a third party acquired the goods in good faith without notice of the interest of the vendor from the original buyer in possession of the goods. The *PPSA* is not intended to exclude or limit the operation of any other law if that other law is capable of operating concurrently with the *PPSA*.<sup>70</sup> Accordingly, the *PPSA* does not displace laws otherwise dealing with ownership of goods. However this general approach is subject to precedence being given to the rules in the *PPSA* with respect to creation and perfection of security interests, and priority.

The general rule now becomes: in circumstances where the vendor of goods subject to a retention of title clause registers its security interest in the goods, the security interest of the vendor is perfected and enforceable against third parties: section 20.

However where the vendor of goods subject to a retention of title clause does not perfect its security interest by, for example, registration, and the buyer sells the goods on to a third party, section 43 *PPSA* applies. Section 43 provides:

Main rule

- (1) A buyer or lessee of personal property, for value, takes the personal property free of an unperfected security interest in the property.

Exception

- (2) Subsection (1) does not apply if the unperfected security interest was created or provided for by a transaction to which the buyer or lessee is a party, unless the personal property concerned is of a kind prescribed by the regulations for the purposes of this subsection.

Accordingly, the interest of the third party prevails over the original vendor notwithstanding the retention of title clause, provided the third party provided new value and was not a party to the transaction which provided for the security interest. The following simple example is given in the Explanatory Memorandum to the *PPSA*:

#### **Example**

Grant A obtains secured finance from Bank A to purchase a forklift. Bank A does not register the forklift on the PPS Register or perfect it using the other perfection

<sup>69</sup> Explanatory Memorandum, Personal Property Securities Bill 2009 (Cth) [2.134].

<sup>70</sup> *PPSA* s 254.

methods. Grant A sells the forklift to Buy A. Buy A would acquire her interest in the forklift free of Bank A's security interest.<sup>71</sup>

Perhaps presciently, the Explanatory Memorandum notes that these arrangements provide an incentive for secured parties to perfect their security.<sup>72</sup>

Interestingly, unlike the *Sale of Goods Act* provisions whereby a third party can acquire good title from a buyer in possession, section 43 of the *PPSA* does not require that the third party acted either in good faith or without notice of the security interest arising from the retention of title clause. It is enough that the third party provided value, and was not a party to the original transaction.

The *PPSA* also provides specific rules in Part 2.5 for third parties to take free of security interests in defined circumstances. So, for example, section 44 anticipates regulations which will provide that personal property of specific kinds may, or must, be described by serial number in a registration of a security interest under the *PPSA*.<sup>73</sup> In such circumstances a buyer or lessee of personal property takes the personal property free of a security interest in the property if searching the register, immediately before the time of the sale or lease, by reference only to the serial number of the property, would not disclose a registration that perfected the security interest.<sup>74</sup>

## **2 Retention of Title and the PPSA: Vendor's Interest in the Goods is Subject to Other Legislation Regulating Security Interests**

To the extent that the interest of a vendor pursuant to a retention of title clause is a 'security interest' for the purpose of State legislation, this position will be superseded by the *PPSA* and the clear incorporation of such interests into the definition of 'security interest' within the meaning of the *PPSA*.

## **3 Retention of Title and the PPSA: The Purchaser Resells the Goods, and Both the Vendor and a Secured Creditor of the Purchaser Claim an Interest in the Proceeds of Resale or Book Debts Arising from the Resale**

The position under the *PPSA* in relation to traceability of proceeds of sale is addressed under Part 2.4 Division 2 of the Act. In particular, 'proceeds' of collateral are defined by section 31(1) which provides, so far as material:

*proceeds* of collateral to which a security interest is (or is to be) attached means identifiable or traceable personal property of the following types, subject to subsections (2) and (3):

- (a) personal property that is derived directly or indirectly from a dealing with the collateral (or proceeds of the collateral)

In circumstances where, for example, there is a dealing in the collateral giving rise to the proceeds, the security interest attaches to the proceeds, unless

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71 Explanatory Memorandum, Personal Property Securities Bill 2009 (Cth) [2.72].

72 Explanatory Memorandum, Personal Property Securities Bill 2009 (Cth) [2.73].

73 Paragraph 2.74 of the Explanatory Memorandum anticipates such property including motor vehicles, watercraft and aircraft. Regulations have only been promulgated in respect of section 45 of Part 2.5, and then only in respect of motor vehicles: *PPSR* regs 2.1, 2.2.

74 *PPSA* s 44.

the security interest provides otherwise (section 32(1)(b)). Significantly, the security interest also continues in the collateral unless:

- (i) the secured party expressly or impliedly authorised a disposal giving rise to the proceeds; or
- (ii) the secured party expressly or impliedly agreed that a dealing giving rise to the proceeds would extinguish the security interest.<sup>75</sup>

Unlike under the current law as explained in *Associated Alloys*,<sup>76</sup> the substitution of a trust relationship between the original vendor and purchaser is not required for the continuation of the interest in the proceeds. Section 31(2) provides:

Proceeds are traceable whether or not there is a fiduciary relationship between the person who has a security interest in the proceeds, as provided in section 32, and the person who has rights in or has dealt with the proceeds.

Where the security interest attaches to the proceeds, section 32(5) provides, in substance, that the security interest in the proceeds has the same default priority as the security interest in the original collateral. The amount secured by the security interest in the collateral and proceeds is limited to the market value of the collateral immediately before the collateral gave rise to the proceeds: section 32(2).

While the security interest in the original goods will also attach to the proceeds in the circumstances contemplated by section 31, the security interest in those proceeds will only be *perfected* if the registration of the security interest, as section 33(1) provides:

- (a) describes the proceeds, if the description complies with any regulations made for the purposes of paragraph (d) of item 4 of the table in section 153 (financing statements with respect to security interests); or
- (b) covers the original collateral, if the proceeds are of a kind that are within the description of the original collateral;
- (c) covers the original collateral, if the proceeds consist of currency, cheques or an ADI account, or a right to an insurance payment or any other payment as indemnity or compensation for loss or damage to the collateral or proceeds.

These provisions demonstrate that, provided a vendor of goods registers a security interest, its position is improved compared with that under retention of title. This is because:

- under the *PPSA* if the security interest actually describes the collateral as extending to proceeds, the vendor could perfect the security interest pursuant to section 33; and
- even if the security interest did not describe the collateral as extending to proceeds, the security interest nonetheless attaches to the proceeds. The vendor, however, would potentially lose priority against a competing creditor in the event of a dispute as to the proceeds.

<sup>75</sup> *PPSA* s 32(1)(a).

<sup>76</sup> (2000) 202 CLR 588.

To that extent, it would benefit a vendor not only to register the security interest in relevant goods, but to ensure that the contract describes the collateral broadly to extend to proceeds. Although the positions in other jurisdictions to the concept of property and security interest need to be approached with some caution because of different statutory provisions, it is useful to note that in Canadian provinces with equivalent personal property securities legislation it appears common for a security interest in respect of chattels to be defined to include ‘all ... present and after acquired personal property including ... Intangibles ... and in all proceeds and renewals thereof’. The enforceability of such provisions in respect of proceeds of sale does not appear to be in doubt.<sup>77</sup>

Further, it is interesting to note that the position under *PPSA* is in other ways comparable with the position under the current law, as exemplified in such cases as *Toveill Pty Ltd v Australian Quality Plus Pty Ltd* [2010] NSWSC 1003 (where the Court was not prepared to imply an interest in proceeds of sale in a vendor in the absence of specific provision in the contract), and *E Pfeiffer Weinkellerei-Weineinkauf GmbH & Co v Arbuthnot Factors Ltd* [1988] 1 WLR 50 (where the Court held a clause purporting to assign all claims in respect of the goods to the vendor, irrespective of the original sale price, was unenforceable).

#### **4 Retention of Title and the PPSA: the Purchaser Affixes the Goods to Real Property**

As a general proposition, the *PPSA* does not apply to interests in fixtures: section 8(1)(j).

In light of this approach, it can be speculated that the current law described earlier continues to apply in respect of goods which become fixtures.<sup>78</sup>

#### **5 Retention of Title and the PPSA: the Purchaser Combines the Goods with Other Chattels**

The *PPSA* deals extensively with goods which are the subject of security interests and which are affixed to, or become commingled with, other goods. Parts 3.3 and 3.4 of the *PPSA* respectively provide for accessions, and processed or commingled goods.

In relation to goods which become constituent of other goods, a security interest in goods that become an accession to other goods continues in the accession: section 88. Rules as to priority of security interests are summarised in section 87, which so far as material, provides:

A security interest arising in an accession before it is affixed to goods has priority over a security interest in the goods as a whole. However, there are exceptions relating to interests in the whole created after the accession is affixed and before the security interest in the accession is perfected.

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<sup>77</sup> See comments in *Saulnier v Royal Bank of Canada* [2008] 3 SCR 166, [16]–[21].

<sup>78</sup> Fixtures are defined in *PPSA* s 10 as meaning goods, other than crops, that are affixed to land.



A security interest arising in an accession after it is affixed will ordinarily be subordinate to an existing interest in the other goods (unless, for example, the holder of the existing interest agrees otherwise) and to a later interest in the other goods that arises before the interest in the accession is perfected.<sup>79</sup>

The *PPSA* also makes provision for removal goods which have become affixed to other chattels: sections 92–95.

In relation to goods which are processed or become commingled with other goods, the common law principle that any interest in goods was extinguished once the goods were incorporated into a process of manufacturing as reflected in such cases as *Borden (UK) v Scottish Timber Products Ltd* is not maintained.<sup>80</sup> Section 99 of the *PPSA* specifically provides:

- (1) A security interest in goods that subsequently become part of a product or mass continues in the product or mass if the goods are so manufactured, processed, assembled or commingled that their identity is lost in the product or mass.

Note: A person might take an interest in the product or mass free of the security interest because of the operation of another provision of this Act.

- (2) Without limiting subsection (1), the identity of goods that are manufactured, processed, assembled or commingled is lost in a product or mass if it is not commercially practical to restore the goods to their original state.

Further, perfection of a security interest in goods that subsequently become part of a product or mass is to be treated as perfection of the security interest in the product or the mass: section 100.

To this extent, the *PPSA* substantially simplifies the position and priority rules as between competing creditors, compared with the existing position under the general law relevant to retention of title.

## **6 *Retention of Title and the PPSA: the Clause Purports to Retain Ownership of the Goods in the Vendor until All Debts Owed by the Purchaser to the Vendor are Paid***

Such a contractual provision invariably gives rise to a security interest under the *PPSA*. A key question is the approach the courts will take to the application of the *PPSA* to such a provision.

As the contractual arrangement between the vendor and purchaser in such circumstances invariably contemplates that the goods will be on sold by the purchaser to third parties, and replaced by new goods supplied on account by the vendor, the goods may be ‘inventory’ for the purposes of *PPSA* Part 9.5. Interestingly while the definition of ‘circulating asset’ in section 340 specifically excludes ‘goods’ (section 340(3)), it specifically *includes* inventory (section 340(5)(e)), which in turn is defined by section 341 to be inventory according to its ordinary meaning (section 341(1B)(a)). The ordinary meaning of inventory includes:

<sup>79</sup> See *PPSA* ss 89 and 90.

<sup>80</sup> [1981] Ch 25.

A list of articles, property or goods, enumerated in reasonable detail. The list may be used in a variety of situations, for example a record of stock held, an account of goods sold, or in relation to bills of sale or to the goods and chattels of a deceased estate. Also the amount or value of a company's current assets that consist of plant and equipment, raw materials, work in progress, stock and finished goods, or such goods individually.<sup>81</sup>

The concept of a security interest over circulating assets including inventory is akin to the current floating charge, although the *PPSA* defines the arrangement in question as personal property rather than by reference to a specific type of security interest. This again excludes any further relevance of the current law principles relevant to retention of title.

Alternatively, if such an arrangement under the *PPSA* contemplates new property being subsequently subjected to the security interest, it may be that section 18(2) *PPSA* applies. This section states that a security agreement may provide for security interests in *after-acquired property*. 'After-acquired property' means personal property acquired by the grantor after a security agreement is made (section 10). The *PPSA* permits a security interest in after-acquired property to attach without specific appropriation by the grantor (section 18(3)); further security agreements may provide for future advances (section 18(4)).

Relevantly, the *PPSA* contemplates that a creditor may register a financing statement which describes the collateral as 'all present and after-acquired property of the grantor' (sections 151(1) and 275(8)). Again, this is somewhat akin to a floating charge under the current law, and is also similar to the arrangement contemplated by retention of title clauses where goods are sold by a vendor to a purchaser in anticipation that the purchaser will sell them on, but the clause is enforceable against any goods in the possession of the purchaser at any stage whilst debts remain outstanding. In light of the provisions of the *PPSA*, again there appears no room remaining for retention of title clauses of this nature – security interests including after-acquired property appear to cover the field.

While *PPSA* would appear to provide a rational framework for the resolution of the matters discussed above, the consequences of applying the new statutory scheme may not be without difficulties. The simple setting of priorities among conflicting security interests (broadly defined) means that the old notions of security based upon title must be rethought. This may not be so different from the position under Australian legislation as it currently stands; however, acceptance that the *PPSA* may have unintended consequences upon personal property title in commercial arrangements which fall within its operation has caused some disquiet when such legislation was implemented overseas.

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81 Peter E Nugh and Peter Butt (eds), *Butterworths Australian Legal Dictionary* (Butterworths, 1997).

#### IV THE IMPACT OF THE *PPSA* ON PERSONAL PROPERTY TITLE IN COMMERCIAL ARRANGEMENTS

In Canada and New Zealand, the personal property securities legislations' abandonment of conventional property concepts to resolve priority conflicts initially caused some difficulty. Because retention of title clauses and other devices provided for by a transaction that, in substance, secured payment or performance of an obligation usually involved parties, such as finance providers, with an appreciation of the personal property securities, failure to perfect such interests has not resulted in many examples of the type of anomalous results which often follow such significant legislative changes. The theoretical difficulties faced by the transition away from standard property concepts, however, have been quite apparent in the treatment of leases of more than one year. Unlike other devices which, to be considered a security interest, necessitate that they be provided for in order to secure payment or performance of an obligation,<sup>82</sup> leases which fall within the definition of a 'PPS Lease' in section 13 of the *PPSA* come within the Act without the requirement that they secure a payment or a performance of an obligation (as is the case with Canadian and New Zealand legislation).<sup>83</sup> For this reason, it is not surprising that many of the most noteworthy cases dealing with the theoretical issues presented by the transition to the personal property security legislations in Canada and New Zealand involve owners of personal property leased for more than one year who failed to perfect their security interest.<sup>84</sup>

Judicial consideration of the consequences of the personal property securities regime in Canada highlights some of the confusion faced as a result of the transition. In *Sprung Instant Structures Ltd v Caswan Environmental Services Inc*,<sup>85</sup> the issue was addressed by the Alberta Courts. In the case, Sprung Instant Structures had leased two portable tents to Caswan Environmental Services for a period in excess of one year. Sprung had not perfected its security interest through registration, and the Royal Bank of Canada had advanced funds under the terms of a general security agreement. The bank had registered its rights under that agreement. At first instance, Forsyth J held that the general security agreement executed between the bank and Caswan granted the bank a security

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82 *PPSA* s 12(1).

83 There are specific exceptions for certain non-financing leases. These are discussed in Nicholas Mirzai, 'The Personal Property Securities Act and Commercial Leases Arrangements: A Practitioner's Guide' (2011) 22 *Journal of Banking and Finance Law and Practice* 3.

84 The transitional problems faced elsewhere will hopefully cause fewer problems in Australia. At the commencement of the *PPSA*, a retention of title clause, for example, gives rise to a transitional security interest (*PPSA* ss 307 and 308) and will be enforceable against third parties as if the law applying before the *PPSA* came into existence still applied (*PPSA* s 311). It is deemed to attach to the collateral immediately before the commencement of the *PPSA*, irrespective of whether the security interest arose before, at or after the registration commencement time (*PPSA* s 321) and it is deemed perfected from immediately before the registration commencement time (*PPSA* s 322(1)), but ceases to be deemed as perfected upon the happening of a number of events (*PPSA* s 322(2)), including the passing of 24 months (*PPSA* s 322(2)(f)). Priorities in the transition are dealt with in *PPSA* s 320.

85 [1998] 6 *WWR* 535.

interest in the structures.<sup>86</sup> The Alberta Court of Appeal, however, reverted to general property law concepts in determining that the leasehold had terminated and that, in any event, the bank's security interest could not alter the property rights of Sprung:

Even if the General Security Agreement somehow does cover the lessee's interest in the lease or somehow covers the leased goods, that lessee's interest is worthless and was terminated. That lessee's interest is not what the bank seeks here. The bank seeks the reversion.<sup>87</sup>

A similar analysis was used by the British Columbia Courts in the case of *Re Giffen*.<sup>88</sup> In that case, a car was leased to Giffen for a period of more than one year, which meant that it was a security interest (as it would be under the Australian *Personal Property Securities Act*). Because the security interest in the car (the lease) was not perfected, the trustee in bankruptcy claimed that the car should be available as part of the estate. The British Columbia Court of Appeal resolved the matter by reference to conventional property concepts, finding that the car was not 'property of the bankrupt.'<sup>89</sup> On appeal, however, the Supreme Court of Canada reversed the British Columbia Court of Appeal's conclusions based upon the extended consequences of the *Personal Property Security Act 1989* of British Columbia. According to the Supreme Court, the British Columbia Court had misinterpreted the task:

The Court of Appeal in the present appeal did not look past the traditional concepts of title and ownership. But this dispute cannot be resolved through the determination of who has title to the car because the dispute is one of priority to the car and not ownership in it.<sup>90</sup>

In the view of the Canadian Supreme Court, the property rights of persons subject to provincial personal property security legislation are determined by the legislature. While the legislative scheme may incorporate common law concepts in whole or in part, the provincial legislatures may redefine or revise those concepts to meet the objectives of the legislation. The Canadian Supreme Court accepted that the personal property securities legislation introduced a new conceptual approach to the definition and assertion of personal property rights and that the property rights of the debtor in this case were to be determined by reference to the legislation.<sup>91</sup>

Accepting the views of the Saskatchewan Court of Appeal,<sup>92</sup> and relying upon academic commentary about the consequences of the legislation,<sup>93</sup> the Canadian Supreme Court concluded that:

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86 [1997] 5 WWR 280.

87 [1998] 6 WWR 535, [4] (Cote JA for the entire court).

88 [1998] 1 SCR 91.

89 [1996] 5 WWR 111, [56] (Finch JA).

90 [1998] 1 SCR 91, [28].

91 Particularly the *Personal Property Security Act*, RSBC 1996, c-359, s 12.

92 *International Harvester Credit Corp of Canada v Bell's Dairy Ltd* [1986] 6 WWR 161.

93 T M Buckwood and Ronald C C Cuming, 'The Personal Property Security Act and the Bankruptcy and Insolvency Act, Two Solitudes or Complementary Systems?' (1997) 12 *Banking and Finance Law Review* 467.

[A] lessee obtains a proprietary interest in leased goods. Section 12(2) states explicitly that ‘a debtor has *rights in goods* leased to the debtor . . . when he obtains possession of them in accordance with the lease’. Thus, [section] 12 operates to ‘deem or recognize that a lessee has a proprietary interest’ ...

‘a trustee in bankruptcy, upon whom there devolves a chattel in the possession of the bankrupt under a commercial lease for a term exceeding a year, *succeeds to the contractual or “possessory” interest of the bankrupt* in that chattel, as well as *the bankrupt’s statutory or “proprietary” interest therein as conferred upon the debtor by s 12 of the Act*’.<sup>94</sup>

Based upon this understanding of the *Personal Property Security Act* and its interaction with the *Banking and Insolvency Act*, the Supreme Court concluded that ‘the bankrupt, as lessee, can be described as having a proprietary interest in the car.’<sup>95</sup>

More recently and closer to home, the New Zealand courts have also faced similar problems reconciling the new personal property security system with fundamental property concepts.

In *Graham v Portacom New Zealand Ltd*,<sup>96</sup> the New Zealand Courts addressed the impact of the *NZPPSA* upon personal property title for the first time. In that case, Portacom New Zealand Ltd, leased portable buildings to NDG Pine Ltd with the lease period being in excess of one year. Despite the fact that such leases were deemed to be security interests under the *NZPPSA*, Portacom had not perfected its interest by registration. The Hongkong and Shanghai Banking Corporation Ltd held a debenture over NDG’s assets which had been perfected by registration. When the bank appointed receivers and managers of NDG’s assets, the receivers claimed the right to sell the buildings. Portacom as lessor of the buildings, asserted that its property rights in the reversionary interest should not be defeated by the perfected security interest of the bank.

In determining that the receiver had priority over the Portacom interest and could sell the buildings, Rodney Hanson J indicated that all leases in excess of one year unless specifically excepted were, under *NZPPSA* section 16, deemed to be a security interest whether they were intended to secure an advance or not.<sup>97</sup> As a result of the priorities outlined in the legislation, Portacom’s unperfected security interest was defeated by the registered security interest of the bank. In resolving the conflict, the theoretical shift brought about by the *UCC* and the Canadian personal property security legislations – as described in the academic literature<sup>98</sup> – was referred to in the following way:

The internal logic of the Article 9 and *PPSA* priority regime is premised on a rejection of derivative title theory in favour of registration as the principal mechanism for ranking priority both among secured creditors and as between the

94 [1998] 1 SCR 91, [37] (emphasis in original). For an analysis of the importance of this decision, see Anthony Duggan and Jacob Ziegel, ‘Justice Iacobucci and the Canadian Law of Deemed Trusts and Chattel Security’ (2007) 57 *University of Toronto Law Journal* 227, 229.

95 [1998] 1 SCR 91, [37].

96 [2004] 2 NZLR 528.

97 See Mirzai, above n 83.

98 Michael G Bridge et al, ‘Formalism, Functionalism and Understanding the Law of Secured Transactions’ (1999) 44 *McGill Law Journal* 567.

secured creditor and the debtor's general creditors including the trustee in bankruptcy. To give effect to this intent, 'rights in the collateral' must be understood as requiring a mere bare right to possession or a power to convey a greater interest than has the debtor, a point confirmed in *PPSA* jurisprudence and expressly stated in some of the more recent *PPSAs*. On this interpretation, ostensible ownership – in the radical sense of bare possession or control of the collateral – has effectively replaced derivative title for the purposes of determining the scope of the secured debtor's estate at the priority level. Thus, by the very act of deeming a true lease to be a *PPSA* security interest, ownership in the leased assets is effectively vested in the lessee as against the lessee's secured creditors and trustee in bankruptcy.<sup>99</sup>

This reasoning was accepted by Rodney Hanson J as applying with equal force to the *NZPPSA*, since its provisions are not distinguishable in any relevant particular from North American law.<sup>100</sup> He thus concluded that both the leasehold and proprietary interests of NDG in the buildings were subject to the prior perfected security interest of the bank, and the receivers appointed by the bank had the power to sell the buildings.<sup>101</sup>

A similar result occurred in *Waller v New Zealand Bloodstock Ltd*.<sup>102</sup> In that case, a breeder entered into a lease purchase agreement with New Zealand Bloodstock and a related financing entity for the lease and ultimate acquisition of a horse. The agreement occurred on 31 August 2001, before the *NZPPSA* commenced on 1 May 2002. Prior to the lease purchase agreement, the breeder had also given a fixed and floating charge over its assets to S H Lock (New Zealand) Ltd. At the commencement of the *NZPPSA*, S H Lock (New Zealand) Ltd had perfected its security interest through registration of a financing statement. New Zealand Bloodstock took no steps to perfect its security interest. On 6 July 2004, New Zealand Bloodstock terminated the lease for non-payment and took possession of the horse. On 23 July 2004, S H Lock (New Zealand) Ltd exercised its rights under its security interest, claiming the horse as part of the breeder's assets. The rights of the financier to the full property in the leased horse was supported in the following terms:

Accordingly, for the limited purpose of priority of securities, the contractual language of cl 4(f) of the agreement to lease (providing that title to the stallion would remain with New Zealand Bloodstock ...) was overridden by statute: because its lease was for a term of more than one year, New Zealand Bloodstock was deemed by s 17 to have a statutory 'security interest'. That being the case, instead of enjoying its previous inviolable title to the stallion, New Zealand Bloodstock's interest, now a 'security interest', was liable to be overridden by a competing security interest.<sup>103</sup>

In *Rabobank New Zealand Ltd v McAnulty and Ors*,<sup>104</sup> the reasoning in *Bloodstock* was applied equally to a horse held on bailment for more than one year (also potentially a security interest under the *NZPPSA*). Although accepting

99 [2004] 2 NZLR 528, [28] citing with approval Bridge et al, *ibid* 602–3.

100 [2004] 2 NZLR 528, [28].

101 *Ibid* [38].

102 [2006] 3 NZLR 629 (William Young, Robertson, Baragwanath JJ, Court of Appeal) ('*Bloodstock*').

103 *Ibid* 643. Section references are to the *NZPPSA*.

104 [2010] NZHC 1534 (23 August 2010) (Gendall J).

that the property rights in bailed goods could be acquired by the holder of a perfected security interest if the bailment as a security interest was not perfected, Gendall J did not grant summary judgment in the case due to the fact that it was not entirely clear that, on the facts, the bailment was a security interest as defined by the legislation. This necessitated further consideration of that issue.

Although the above cases might be taken to indicate that conventional personal property rights are no longer relevant to determining personal property rights under the priorities established by the *PPSA*, this conclusion would be overly broad. Within the legislation itself, there are limitations to the way in which security interests can be created. For example, the consequences of theft in the application of the *PPSA* have been identified in the academic literature as requiring resort to conventional property concepts.<sup>105</sup>

The residual importance of conventional property concepts can also be seen from the case of *J S Brooksbank & Co (Australasia) Ltd v Exftx Ltd (rec apptd in liq)*.<sup>106</sup> This case concerned a claim in conversion by the suppliers of wool to a carpet manufacturer which went into receivership and liquidation. The wool had been supplied under an agreement whereby the carpet manufacturer (Exftx) would obtain neither possession of, nor title to, any wool until after the supplier (Brooksbank) had received payment by way of cleared funds (title passing before actual delivery – upon payment). A shipment of wool was released mistakenly to the carpet manufacturer by brokers despite a lack of payment. Upon discovery of this error, the wool mistakenly released was segregated. ANZ Bank (the financier) claimed priority through its perfected security interest in all of the assets of Exftx.

Because the supplier had acted through its agents to deliver the wool voluntarily (though mistakenly) and because there was no unconscionable conduct by the manufacturer, there was neither conversion nor facts warranting the imposition of a constructive trust. For purposes of the *NZPPSA*, the interest in the wool following its delivery was characterised by the Court at first instance as being a simple conditional sale with retention of title and thus capable of being characterised as a security interest. Had that been the case, the perfected security interest of the financier in the wool would have had priority over the unperfected interest of the supplier under the provisions of the *NZPPSA*. Fortunately for the wool supplier, the retention of title was not intended to secure payment or performance of an obligation since no delivery was contemplated prior to

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105 Struan Scott, 'The PPSA: The Continued Relevance of Conventional Legal Principles in Determining the Existence of a Security Interest' [2009] 15 *New Zealand Business Law Quarterly* 203.

106 [2009] NZCA 122 (21 November 2007).

payment. In consequence, the wool supplier's title to the goods was not subject to a better claim by the financier.<sup>107</sup>

## V CONCLUSION

The *PPSA* does not appear to effect major changes to the position of a vendor attempting to protect its interest in personal property providing the vendor follows the rules prescribed in the *PPSA*, particularly the need to perfect the vendor's security interest in the subject personal property.

If a vendor follows the rules it is unlikely to suffer any derogation of its rights compared with the previous regime and, in fact, may well have an improved position in the following principal respects when a contest among security interests arises:

- if a perfected security interest has been registered as a PMSI, a vendor has a position little different from that which prevailed under a 'simple' Romalpa clause;
- a purchaser for value without notice of another interest normally will not take against the perfected security interest of a vendor;
- a vendor gains rights in the proceeds of a sale to a third party whether or not the security interest so provides;
- a vendor may claim all debts owed in a security interest and be permitted to trace the proceeds of sale without a trust being created; and
- a vendor gains a security interest in goods that become accessions, or are processed or commingled with the original goods, the subject of a security interest.

While the scheme introduced by the *PPSA* does add both clarity and certainty, it is also clear that the *PPSA* will advance a new paradigm for personal property title as well as priorities over security interests as defined within that legislation. Vendors using retention of title clauses will need to be aware of the requirement to perfect their interests through registration or possession because a failure to do so may have serious financial consequences. Those consequences have been seen elsewhere in relation to leaseholds, conditional sales and consignments sales. Because the *PPSA* alters the priorities of such a broad range

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<sup>107</sup> In the vast majority of circumstances involving retention of title, title is retained to secure performance of a sales contract under the *PPSA*. When such is the case, the rights of secured parties in the property, including the rights of the vendor retaining title, will be merely a security interest (s 12(2)(d)), and the various security interests in the property will be prioritised according to the *PPSA* (s 55). As *J S Brooksbank & Co (Australasia) Ltd v Exftx Ltd (rec apptd in liq)* indicates, however, the competing rights of parties in property which do not come within the *PPSA* (because, for example, it was delivered by mistake or is not otherwise intended to act as security) will be determined by general law concepts and resort to remedies related thereto, such as conversion. In this regard see also Scott, above n 105. In relation to pre-*PPSA* priorities in unregistered charges, see *General Motors Acceptance Corporation Australia v Southbank Traders Pty Ltd* (2007) 227 CLR 305.



of transactions when they come within its ambit, conventional property rights are no longer the only matter of relevance in personal property disputes. That this has caused some difficulty in Canada and New Zealand to financiers, practitioners and the judiciary is clear. It is hoped that Australians will adapt with less difficulty than experienced in those countries.