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Receivables Financing - Enforcement and Priority Issues

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1 Introduction

This is a companion piece to a paper to be presented by Rebecca Hope covering, in a broad sense, some of the "front end" aspects of receivables financing. This paper deals with some enforcement and priority issues associated with receivables financing arrangements (hence the catchy title). Therefore, although capable of standing alone, it may make sense for it to be read alongside or immediately after Rebecca's paper.

I want to start with a few overarching comments and caveats:

- "Receivables" is a very wide expression. For the purposes of this paper, I am going to narrow the term somewhat and deal mainly with traditional accounts receivable, for example those generated every day in a manufacturing or service business when it supplies goods or services on credit to customers. I'm not going to cover, except in passing, "financial" receivables such as loans, mortgages, credit cards, leases, hire purchase arrangements, etc that are generated in the finance sector. I am dealing mainly with "accounts"[1] and not "chattel paper" [2] for the purposes of the Personal Property Securities Act 2009 (Cth) (**PPSA**).

- "Receivables financing" covers a wide spectrum of finance arrangements, from factoring to invoice discounting (disclosed or undisclosed) to receivables purchase arrangements (with or without recourse) to securitisation. The common element is the provision of finance effectively secured against pools of receivables to which the financier expects to have first priority recourse in a default scenario.[3] I'm not proposing to stray into securitisation, but my commentary is as applicable to enforcing against a pool of securitised receivables as it is to enforcing a factoring arrangement.

- The PPSA has been in force for over 2 years now. It has changed the ground rules and overturned some technical conventional legal wisdom that was very relevant to pre-PPSA receivables financing. Rebecca has covered this in her paper. However, to date, the PPSA remains largely untested by Australian courts (certainly insofar as it relates to receivables financing), so in interpreting some of the trickier concepts our expert commentators are forced to draw from New Zealand and Canadian authorities.

- There is a PPSA statutory review currently underway and we can be hopeful that some clarifications will be made to some of the more problematic sections of the PPSA that are relevant to receivables financiers, such as section 64, although this not necessarily guaranteed, since the terms of reference for the review centre principally on the application of the PPSA to small businesses.

- The views expressed in this paper (and any errors or omissions) are the author's alone.

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[1] i.e. *"a monetary obligation …. that arises from disposing of property … or providing services"*: s 10 PPSA.
[2] S 10 PPSA.
[3] For PPSA purposes, the form of the security is largely irrelevant, as is the legal nature of the financing (e.g. secured loan, receivables sale, etc). Almost invariably, an "in substance" security interest for the purposes of s 12(1) PPSA, or a "deemed" security interest for the purposes of s 12(3) PPSA, will be created. However, the distinction between the 2 types of security interest may be relevant in determining applicable enforcement rules. See later in this paper.

This paper will cover:

- Threshold key enforcement considerations, such as control of collections and dealing with account debtors.
- General enforcement approaches for receivables, such as collecting out and portfolio sale.
- Formal rules of enforcement and Chapter 4 of the PPSA (which often applies in the receivables financing context but only where the financing creates an "in substance" security interest).
- Relevant priority rules for proceeds of enforcement, and
- Receivables as "circulating assets".

2 Threshold key enforcement considerations – collections and debtors

Receivables are the lifeblood of any business as they represent the return which has been earned from its business endeavours. By their nature, account receivables are usually short-term assets that can be turned into cash or liquidated easily. This is both a blessing and a curse in the enforcement context.

- On the one hand, a good, quick recovery should be possible **if** the financier has the right security package and receivables data, provided the underlying receivables themselves are collectible.
- On the other hand, if a financier doesn't have the right security package or enough receivables data to move quickly, then they can expect their security to evaporate and will achieve a poor recovery.

For this reason receivables financiers and their legal advisers must be focused on the following to ensure they are well placed to enforce in need:

- having live and accurate data on the receivables themselves, which will require the right covenant package from the customer and a good IT platform, and
- obtaining effective and clean control over collections, which again will require the right security package and a good IT platform.

These requirements were paramount pre-PPSA and remain paramount today.

2.1 Obtaining receivables data

Typically, a covenant package will include obligations on the customer to provide:

- electronic copies of all relevant invoices, credit and adjustment notes, and
- an electronic feed of basic receivables data sufficient to allow the financier to immediately enforce the receivable if required.

In a high volume receivables-generating business, these obligations will typically be discharged by means of a live two-way IT platform between customer and financier.

2.2 Controlling the collections

In an old-school factoring arrangement, the financier will assume effective control of the accounts receivable function for the customer. Account debtors will be notified of the financing (be it by way of receivables assignment or secured loan) and required to pay the receivable into a locked bank account, usually in the name of the financier. From a legal and security perspective, this is a robust arrangement.

However, it is likely to be much less commercially attractive for the financier's customer. The customer may not want to let its debtors (ie. its good customers) know that it has factored their accounts. It might also not be administratively convenient to ask the debtors to redirect payments into a dedicated account with the financier, particularly if those payments are made electronically or under existing direct debit arrangements.

So more common in a larger scale receivables financing arrangement is something that is less robust. Typically account debtors will not be notified of the receivables financing. Absent that notice, not enough will have been done to transfer the legal title to the receivable to the financier.[4]

In these circumstances, arrangements will be put in place between the financier and the customer to ensure that receivable collections either:

- come into a dedicated locked bank account controlled by, if not necessarily in the name of, the financier, or
- are promptly swept from a general bank account in the name of the customer, after reconciliation and identification, into the financier's own account.

Collections paid into a bank account in the name of the customer will likely be regarded as "proceeds" (as that term is defined in the PPSA) provided they are identifiable or traceable.[5] On this basis, any security interest in the receivables themselves will generally continue into their proceeds once they have been paid into the customer's bank account.[6] I will discuss this important feature in more detail later. However, generally the financier will still want to ensure that it has proper security, not only over the collections, but also if possible over any bank account of the customer into which those collections are paid.

A common approach in these circumstances is for the customer to be required to declare a trust in favour of the financier over any bank account into which collections are paid. Whilst I understand there is an argument that a declaration of trust of this kind does not give rise to a separate security interest requiring registration, in practice I am more inclined to play it safe and assume that it does and specifically register a financing statement on behalf of the financier against the bank account as well.[7]

If the financier is an authorised deposit-taking institution (**ADI**) itself, in practice the preference would be for the bank account to be opened in the name of the customer with

[4] s 12 Conveyancing Act 1919 (NSW) and its equivalents in other Australian jurisdictions require, among other things, for notice of the assignment to be given to the account debtor in order to achieve a legal assignment.

[5] s 31(1)(c)(ii) PPSA.

[6] s 32(1) PPSA.

[7] On the one hand, a declaration of trust might not be a "transfer" for the purposes of the "deemed" security interest provisions in s 12(3)(a) PPSA On the other hand, the declaration of trust might be argued to itself be an "in substance" security interest as it secures the obligation to account for collections. It would be unfortunate for a financier if a court were persuaded that an registered (and therefore unperfected) declaration of trust stood alone and was subsequently defeated by another perfected security interest. Best practice is to avoid the argument and register anyway. Belts and braces are OK in these circumstances.

the financier. The financier would then be able to exercise rights such as set off or combination of bank accounts to sweep the account of moneys owed to it relating to the collections and perfect any security interest in respect of the bank account by control, as well as by registration.

However, if the financier is not an ADI or for any other reason the bank account cannot be held with the financier, then it will be important to ensure that there is an bank account agreement in place between the financier and the ADI which ensures that the financier has control and priority in respect of the collections in the account. Under this arrangement, the ADI promises, in favour of the financier, not to exercise any rights of combination of account or set-off and accepts the financier's sole right to control and operate the bank account. In my experience, it is this latter point that is particularly fertile ground for trouble in insolvency or near insolvency scenarios. If full control of the collection account isn't established up front with the relevant ADI, then there is a risk that proceeds in the account will either evaporate or become subject to competing claims of other creditors or insolvency practitioners.

2.3 Notifying the account debtors

A receivables financier might avoid contacting or dealing with debtors at all if the receivables are highly liquid and it has the right security package in place over the customer's collections account. However, this won't always be the case. Even if no notice of the receivables financing has been given to the account debtor up front, it may still be important for the financier to be in a position to give that notice quickly in an enforcement scenario.

Giving notice to the debtor will complete the formalities for legal assignment of the accounts receivable[8] and it will permit the financier to collect the receivable free of any future equities or defences arising in favour of the account debtor.[9]

It will generally be preferable for any notice to come from the customer/assignor.[10] However, in an enforcement, the customer/assignor may be unable or unwilling to give the notice. It is therefore common instead for a "title perfection" power of attorney to be granted up front in favour of the financier to allow it to give the notice on the customer's behalf.

3 General enforcement approaches

Before I move to the technical rules and considerations applying to enforcement of receivables financing arrangements, I want to provide an overview of the general enforcement approaches available. These usually boil down to just 2: collect out and portfolio sale. The more "current" (i.e. shorter dated) and liquid the receivable assets are, the more likely that a collect out will be the better option.

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[8] s 12 Conveyancing Act 1919 (NSW) and its equivalents in other Australian jurisdictions. The notice must also properly identify the property, identify the assignee and actually notify of the assignment. For an up to date in-depth analysis of "The impact of the PPSA on assignments of account", please see John Stumbles' paper of that name: Melbourne University Law Review 2013 [Vol 37:415].

[9] s 80(1)(b) PPSA.

[10] Mainly because, if it doesn't, the account debtor can call for proof of the assignment before being required to pay the financier instead: S 80(7)(1)(b) PPSA and, until such proof is given, the debtor is entitled to continue to account to the assignor creditor. Note also the "garnishee" process provided for in s 120 PPSA, which may be a better option.

3.1 Collect out

A collect out could be conducted by the financier, by the customer under close supervision, or by an agent for the financier (such as a mercantile agent or insolvency practitioner). I am using “agent” in the commercial sense when I refer to insolvency practitioners. If the practitioner is formally appointed as a receiver of the customer, then the usual rule applies that the receiver is the agent of the customer. A formal appointment is unusual unless:

- the receivables are longer dated and a portfolio sale is therefore under consideration;
- the receivables are otherwise in jeopardy or their collection will be prejudiced; or
- there have been other insolvency practitioner' appointments and the company’s business assets are being dismembered.

3.2 Portfolio sale

This approach is generally only used if the receivables are longer dated. It is more common if the receivables are a liquid pool of financial assets (e.g. mortgages, leases, etc.). The financier will likely owe a duty to conduct any sale in such a way as obtain the market value for the portfolio. For this reason, it would be common for a financier to appoint a receiver to conduct a portfolio sale instead. This appointment largely shifts the duty to the receiver and ensures an expert carries out the sales process.[11]

4 Formal rules of enforcement

4.1 “Deemed” v “in substance” – why the distinction might be important

Chapter 4 of the PPSA sets out some rules governing enforcement of security interests, but it doesn’t apply to "deemed" security interests that are provided for by the transfer of an account that does not secure payment or performance of an obligation.[12] Therefore we may need to establish, first, whether a receivables financing arrangement creates an “in substance” security interest for the purpose of s 12(1)[13] or a “deemed” security interest for the purpose of s 12(3)[14] of the PPSA and, secondly, whether or not that arrangement secures payment or performance of an obligation, before we can identify what (if any) enforcement rules apply.

This isn’t always straightforward.

If the financing doesn’t involve any purported transfer or assignment of account receivables, then we can quickly move on. We are dealing with an “in substance” security interest and Chapter 4 applies.

However, if the financing is documented as a receivables assignment then we need to keep analysing. A financier under a receivables purchase structure will clearly hold a "deemed"

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[11] s 420A Corporations Act 2001 imposes an essentially identical duty on a receiver as is placed on the financier under s 131 PPSA.

[12] s 109(1)(a) and (b) PPSA.

[13] s 12(1) PPSA: *“A security interest means an interest in personal property provided for by a transaction that, in substance, secures payment or performance of an obligation (without regard to the form of the transaction or the identity of the person who has title to the property).”*

[14] s 12(3) PPSA: “*A security interest also includes the following interests, whether or not the transaction concerned, in substance, secures payment or performance of an obligation: … (a) the interest of a transferee under a transfer of an account or chattel paper; “*

security interest under s 12(3)(a) of the PPSA, but, in the overall context of the transaction, are any obligations effectively secured?

Often the answer to that question will be "yes". In receivables purchase arrangements there will often be obligations effectively secured. For example:

- Is there recourse to the customer if an account debtor fails to pay?

  I'm not just thinking here of a straightforward payment obligation on the customer if the account debtor defaults. Recourse can be subtler than that. For example, the arrangement may be that, if the account debtor fails to pay, then the lending facility automatically reduces, potentially creating recourse through the back door.

- Does the customer have any repurchase obligations?

- Does the customer have any top-up payment obligations if there is part-payment by the account debtor (for example, because a set-off has been exercised or an allegation made that the customer has not performed its obligations to the account debtor)?

If the answer to any of the above questions is "yes" then, in addition to a "deemed" security interest under s 12(3)(a), the financier also has an "in substance" security interest which engages Chapter 4 and the rules in that Chapter must be followed.

Although I don't intend to otherwise cover this point in this paper, the analysis that I have just gone through is also relevant to the application of the vesting rules in Part 8.2 of the PPSA. These rules operate to render unperfected security interests ineffective, with the result that the secured property vests in the customer if a liquidator or administrator is appointed to it or a deed of company arrangement is executed in respect of it.[15] However, the vesting rules do not apply to "deemed" security interests created under a receivables sale structure if no payment or performance obligations are secured. Even if they are unperfected at the onset of the customer's insolvency, they remain effective security for the financier.

4.2 Chapter 4 general rights and obligations

Chapter 4 of the PPSA provides general enforcement rules dealing with seizure, disposal or retention of collateral, and prescribes certain steps that must be taken after a security interest in collateral has been enforced. We have established that Chapter 4 can technically apply to the enforcement of many receivables financing arrangements, but so what?

Concepts of seizure, disposal and retention seem on their face inapplicable to highly liquid assets, such as receivables, unless the enforcement approach is by way of a portfolio sale.

However, Chapter 4 does impose:

- a general standard of honesty, and

- a requirement for commercial reasonableness in relation to enforcement actions.

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[15] s 267(1) PPSA operates to vest the unperfected security interest. However section 268(1)(a) provides that does not apply to *".. a security interest provided for by any of the following transactions, if the interest does not secure the payment or performance of an obligation … (i) a transfer of an account ….."*

It also contains special rules for the enforcement of security interests in certain liquid assets (accounts, chattel paper and negotiable instruments). These provisions, which are set out in s 120 PPSA, are particularly relevant in the receivables financing context where receivables are the relevant collateral not used predominantly for personal, domestic or household purposes.[16] Also, the enforcement provisions do not apply where a receiver or receiver and manager has been appointed to deal with the relevant property.[17]

The financier may dispose of the collateral by exercising a power of sale.[18] Before the sale the financier undertaking enforcement must give a notice of the intended disposal to the grantor/customer and other secured parties with a higher priority security interest.[19] The notice must include particulars of the collateral, the enforcing financier and the manner of sale.

A financier exercising a power of sale has a duty to obtain market value for the collateral or otherwise obtain the best price that is reasonably obtainable.[20] Any purchaser then takes the collateral free of all security interests.[21] The proceeds of the sale must be distributed among secured parties in order of priority with any residual proceeds given to the grantor/customer.

Accounts are the relevant collateral in the receivables financing context. A receivables financier can also use an effective garnishee process under section 120 of the PPSA as an alternative to seizing proceeds.[22] By serving a garnishee notice on the account debtor, the account debtor will be required to pay the financier instead.

Interestingly, these garnishee rights apply to all types of "in substance" security interests. Therefore, the legal form of the receivables financing (i.e. secured debt, receivables assignment (equitable or otherwise)) becomes less relevant in a PPSA world. The PPSA effectively allows direct enforcement by way of garnishee by the financier of a receivable, even if the receivable has not been properly assigned to it at law.

If, ultimately, a financier receives any amounts from the garnishee procedure, then:

- if the receipt is in the form of currency, the amount must be distributed in accordance with the general priority rules that I will discuss later, and[23]

- if the receipt isn't in the form of currency, then the financier must apply the amount against the secured obligation.[24]

The rationale for this distinction isn't clear. On its face, it would appear to make it possible for a receivables financier to effectively queue-jump and ignore higher-ranking priorities, according to the nature of the payment received. However, the financier is also required to give a notice to other secured parties with a higher-priority security interest.[25] If those parties do not object to the action, then the financier can go ahead and do it. If the higher-ranking financier snoozes, they might lose; there is no consent requirement as such. This

[16] s.115 PPSA
[17] s.116(1) PPSA
[18] s.128(1) PPSA
[19] s.130 PPSA
[20] s.131 PPSA
[21] s.133 PPSA
[22] s 120 PPSA.
[23] s 120(5) PPSA.
[24] s 120(4) PPSA.
[25] s 121 PPSA.

underscores the importance of higher-ranking security interest holders always insisting on a priority agreement, not just relying on their statutory priority under the PPSA scheme.

4.3 Contracting out of Chapter 4 obligations

As mentioned, it is possible for parties to a security agreement to contract out of a number of rules in Chapter 4 where the relevant collateral is not used predominantly for personal, domestic or household purposes.[26] In any well-drafted security agreement, there will be provision which excludes some or all of the provisions referred to in the contracting out provisions in s 115 of the PPSA.

This contracting out would not, however, typically include the garnishee procedure in s 120.

The financier would, in any event, want to ensure that it is placed in a position where "it need not comply with" Chapter 4, rather than "it has excluded" Chapter 4. This approach addresses the risk that contracting out of an obligation to comply with a procedural requirement may lead to an argument that the financer cannot rely on the remedy at all. By stating that that the financier may, but need not, comply with any relevant Chapter 4 provisions, this ensures that if the financier wishes to exercise a Chapter 4 remedy which has related procedural requirements that must be complied with, the financier has the freedom to elect to exercise the right, power or remedy and comply with the necessary procedural requirements.

By way of a final comment, Chapter 4 itself makes it clear that it is not intended to be a comprehensive code of enforcement. So the financier will still want to ensure that the receivables financing arrangement contains the appropriate contractual and proprietary enforcement rights that apply outside the PPSA scheme. This includes the ability to appoint a receiver or receiver and manager to achieve a sale of the receivables asset. The Chapter 4 enforcement rules do not apply to this type of enforcement method.[27]

5 Relevant priority rules for proceeds of enforcement

5.1 Basic rules

Whether or not a security interest is enforced under Chapter 4 or by one of the more traditional pre-PPSA methods, such as receivership, the PPSA prescribes the order in which a secured party must apply all amounts and proceeds realised from the enforcement.[28]

There are two qualifications to that position. The prescribed order does not apply to "deemed" security interests that do not secure performance or payment of an obligation. Also, when I use the word "proceeds" here, both I and the PPSA mean "proceeds" within its ordinary meaning.[29] The PPSA also gives that term a very specific meaning that is relevant to the breadth of security interests and discussed elsewhere in this paper, but it does not apply to the statutory order of application of proceeds, which is as follows:

1. first, to discharge obligations to persons holding interests other than security interests at higher priority[30]; then

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[26] s 115 PPSA.
[27] s 116(1) PPSA.
[28] s 140(2) PPSA.
[29] s 140(1) PPSA.
[30] This includes such things as liens and charges arising by operation of general law, rights of set-off and transfers of account made solely to facilitate collection or as part of a sale of business.

2. to meet reasonable expenses incurred in relation to the enforcement to the extent secured; then

3. to discharge obligations to persons holding higher-priority security interests; then

4. to discharge obligations to the secured party secured by the security interest; then

5. to discharge obligations to persons holding lower-ranking security interests in the collateral; and then,

6. finally, to the grantor.

This statutory waterfall begs the question about which security interests have the higher priority.

As mentioned earlier, a typical receivables financing will usually create security interests in at least accounts (i.e. the receivables) and a general intangible (i.e. the bank account for the collections). To gain priority, these security interests need to be perfected. Perfection by registration is generally the only avenue open to receivables financiers[31] as it is not possible to possess or control accounts for the purposes of the PPSA.[32]

Relevantly, the priority rules are as follows:

- Priority between unperfected security interests in the same account is to be determined by the order of attachment of the security interests.[33]

- A perfected security interest in an account has priority over an unperfected security interest in the same account.[34]

- Priority between two or more security interests in the same account that are both perfected is determined by the order in which the "priority time" for each security interest occurs.[35] It is of course common for secured parties both holding perfected security interests to agree by way of priority agreement that, amongst themselves, a different order of priority will apply.

5.2 "Proceeds"

Now I turn again to "proceeds" as that term is specifically defined for the purposes of the PPSA and the implications of that definition for the enforcement of security interests by a receivables financier.

In nutshell, the PPSA definition of "proceeds" allows secured parties who have a security interest in a particular item of personal property to continue to have the benefit of that security interest when that personal property converts into another form.

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[31] s 55(5) PPSA.

[32] "Possession" isn't conceptually applicable to a chose in action like an account (although it might be in relation to negotiable instruments and chattel paper) and "control" only applies to certain classes of collateral not including accounts: s 21(2)(c) PPSA.

[33] s 55(2) PPSA: attachment will usually occur when the security agreement is signed or a document is executed giving effect to the sale of the receivable to the financier. For these purposes, the time at which notice is given to the underlying debtor becomes irrelevant.

[34] s 55(3) PPSA.

[35] s.55(4) PPSA: For accounts, the priority time will be determined by first-in-time registration because it is not possible to possess or control accounts for the purposes of the PPSA.

Let's use a simple example: a box of widgets is owned by a manufacturer and subject to a security interest in favour of an inventory financier. Other things being equal, the inventory financier's security interest in the widgets automatically continues in the account receivable created when the manufacturer sells the widgets to its end customer. It also continues in any cash proceeds paid by that customer when it pays the relevant invoice.[36]

You can see here that there is fertile ground for conflict between:

- financiers who claim a security interest in inventory
- retention of title suppliers
- general financiers who hold general security interests in the assets of a customer
- ADIs who are holding the bank account into which the cash proceeds are paid, and
- the humble receivables financier who only claims an interest in the accounts receivable and the proceeds.

The PPSA endeavours to provide a set of priority rules to resolve these various conflicts.

5.3 PMSIs and the 'super priority' rule

In receivables financing, one of the most important set of priority rules relate to purchase money security interests (or PMSIs) which, in the context of this paper, essentially refer to retention of title or other conditional sale arrangements relating to goods.

The PPSA gives the holder of a registered PMSI (for example, the supplier of goods to the customer) a form of 'super-priority'[37] that can trump the interests of all other secured parties. This includes a receivables financier with a security interest in the accounts receivable that represents the sale proceeds of the goods which are the subject matter of the PMSI and sold by the customer in the ordinary course of its business.

It is worth pausing here to recognise that this 'super priority' is really not all that different in substance to the pre-PPSA priority position.

A pre-PPSA receivables financier was never in a position to get "good" security over an accounts receivable representing the proceeds of the sale of inventory purchased from a supplier under a properly drafted retention of title arrangement. Because the customer never owned the inventory, the retention of title arrangement ensured that the supplier owned the sale proceeds as well. They could not therefore be reached by a financier who purported to take security over the customer's title to the proceeds.

Now we are in a PPSA environment, the 'super priority' afforded to a supplier with a registered PMSI functions in largely the same way as the supplier's title functioned under the pre-PPSA law.

5.4 PMSIs and s 64 notices

However, there is a special procedure which allows the receivables financier to assert a higher priority over the PMSI holder.

[36] s 32(1) PPSA.
[37] s 62 PPSA.

This procedure, which is set out in s 64 PPSA, allows the receivables financier to give a notice to the PMSI holder of the receivables financing arrangement within the time limits specified by that section.

The effect of this notice, if correctly given, is to elevate the priority of the receivables financier's security interest above that of the PMSI holder.

As a practical matter, however, it is difficult for a s 64 notice to be effectively given because it must be provided to the PMSI holder at least 15 business days before the receivables financier's security interest attaches to the account, which would usually be when the related security agreement is signed.

The difficulties with the timing of the s 64 notice have not gone unnoticed. As part of the PPSA statutory review process currently being underway, there have been a number of submissions, both from legal advisers and from trade associations and other bodies, concerning the need to fix the drafting in s 64 to make the process simpler. In particular, it has been suggested that the notice required to be given to the PMSI holder under s.64(1)(b) should be able to be given before or after the accounts financier has registered in relation to accounts. The financier's priority could then apply to accounts for which it has provided new value at any time from the later of 15 business days after the notice has been given to the PMSI holder or when the accounts financier's registration is made in respect of accounts.

Having mentioned, however, the potential simplification of the s 64 procedure, it also has to be said that it is often the case that great angst is created when a receivables financier flags its intention to give a s 64 notice to, for example, a key supplier of the customer. The danger is always that the service of the notice may have the effect of changing the customer/supplier relationship in a way which, from the supplier's perspective, is detrimental to it.

6 Receivables as circulating assets

The last subject I'd like to touch on is Part 9.5 of the PPSA, which explains how the pre-PPSA concepts of a fixed charge and a floating charge operate under the PPSA.

As you will no doubt know, much of the common law regarding the distinction between fixed and floating charges and the degree of control which a charge has to achieve in order to create a fixed charge has developed in the receivables financing context.[38]

The reason for this is a priority issue which still applies under the PPSA and it arises out of s.562(1) Corporations Act 2001 which gives employees statutory priority for their claims out of floating charge property. As a result of this priority rule, it has always been practically very important to establish whether a particular asset of a company is properly comprised in or subject to a floating charge (to use pre-PPSA language) or subject to a circulating security interest (to use PPSA language).

For the receivables financier, it is important to note that if a security interest is provided for by way of transfer of an account or chattel paper, then the account or chattel paper is not a

[38] See for example Siebe Gorman & Co. Ltd v Barclays Bank Ltd [1979] 2 Lloyd's Rep 142, Re New Bullas Trading Ltd (1994) 12 ACLC 3203 and Re Spectrum Plus Ltd [2005] 4 All ER 209. This line of cases developed and supported the mechanics adopted by many receivables financiers to ensure appropriate control of receivable proceeds.

circulating asset for the purposes of the PPSA[39] or the Corporations Act and is not therefore at risk of being applied to meet employee entitlements.

However, for receivables financiers who construct their financing arrangements by way of a secured loan, it will be important to ensure that the security package provides:

- for proceeds from the receivables to be paid into a specified bank account;
- for the financier to have effective control over that account; and
- that payments into the account do not automatically give rise to a drawing right in favour of the customer.[40]

In addition, where appropriate, registrations claiming control over what would otherwise be circulating assets (for example, the receivables and the bank account into which the proceeds are paid) will need to be made by the financier to secure its priority over employee entitlements.

7 Concluding remarks

The title of the seminar at which this paper is presented is “Receivables Financing – a fresh look”. I hope that you have got something fresh out of it. If there is a particular takeaway from my part, then I think it is probably along the lines that the introduction of the PPSA hasn’t in practice changed anything radically for the receivables financier in the enforcement scenario. Sure, there are different registration requirements up-front which need to be followed and possibly a few more tools in the toolkit, such as the garnishee rights under section 120. However it remains the case that having the right receivables data and, most importantly, proper control over collections are the real keys to a successful enforcement outcome when you are dealing with rapidly liquidating assets.

[39] s.341 (4A) PPSA
[40] s.341 (3) PPSA