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PPSA – what will the courts make of it all?

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Introduction

1 The given title refers to the *Personal Property Securities Act 2009* (Cth) (PPSA (Cth)) and therefore to the courts of Australia.

2 It will be well known to those attending this Conference that the PPSA (Cth) introduces terms and concepts that are foreign to the general law relating to personal property securities. The terms "collateral", "attachment", "security agreement", "security interest", "financing statement", "PPS lease" and "perfection" spring to mind. (Generally, speaking, I will not discuss the meaning of the novel terms used.) Importantly, the new régime is an integrated one that treats personal property securities in the same functional way, irrespective of the different legal forms they may take.

3 What will the courts make of it all? I predict that they will accept that the new legislation is a harmonious whole and that it is to be construed as such, free of any pre-disposition in favour of the former legal categories.

4 On the whole, Canadian and New Zealand judges seem to have had no difficulty in interpreting and applying the Personal Property Security regimes of the Canadian common law Provinces and that of New Zealand in that way.

5 As a separate matter, I predict that Australian courts will find the Canadian and New Zealand cases generally persuasive, but will need to take into account differences, not only between the respective PPSAs, but also between the background law against which they were enacted.

6 I will, in due course, consider three of those decisions and inquire what they may hold for Australian courts.

The significance of security

7 A security secures a payment or performance of an obligation. It has these aspects:

(1) it gives the creditor a right as against the grantor of the security, to enforce the security against the collateral in case of default by the debtor;

(2) it gives or may give the creditor a right, to the extent of the value of the collateral, to priority of payment over unsecured creditors if the debtor should become a bankrupt or be ordered to be wound up;

(3) it gives the creditor the right to follow the collateral by asserting the security against a third party who has taken title to it.

8 The position of non-parties to the granting of the security calls for consideration in (2) and (3). It is in those cases, in particular, that the courts will be called upon to jettison "old learning" in favour of "new learning".

Some warnings

9 Professor James O'Donovan has said of the PPSA (Cth):

> "the best advice that can be offered to an interested party approaching the PPSA 2009 for the first time is to avoid transposing pre-existing concepts and principles into the analysis of PPSA 2009 and embrace the new concepts it introduces. It will also be important to focus on the words of the relevant sections of PPSA 2009 and the official commentaries to discern their meaning. If this does not provide clarity, examine the stated objectives of the new legislation for guidance."

(*Personal Property Securities Law in Australia,* Thomson Reuters, Loose-leaf 2012, at [1.110] p1-11)

10 In the same vein, Professor Sheelagh McCracken has said in relation to the PPSA (Cth):

> "Both New Zealand and Canadian courts have emphasised the need for "old learning" to be set aside and for new approaches to be adopted. With a considerable body of international jurisprudence to

> draw upon, a fascinating question is the extent to which Australian courts will adopt others' learning on these new concepts."

"Conceptualising the Rights of a Lessee under the Personal Property Securities Regime: the Challenge of "New learning" for Australian Lawyers" ((2011) 34(2) *NSWLJ* 547 at 549 – footnote reference omitted)

11 As we shall see in the cases examined below, it is not only academic commentators who have warned against preconceptions based on the old law: so have Canadian and New Zealand judges.

Nemo dat quod non habet

12 In two ways the new régime contradicts the general law principle that a person cannot give that which he or she does not already have. I suggest that this rule is based on notions of "property" as known to the general law. For my purposes, both ways in which that general law rule is contradicted arise in the context of leases or bailments.

13 The first way is exemplified by s 19(5) of PPSA (Cth) (which is comparable to s 40(3) of *Personal Property Securities Act 1999* (NZ) (PPSA (NZ)), and to s 12(2) of the *Personal Property Securities Act 1993 (Saskatchewan)* (PPSA (Sas)). (As will be well known to this audience, the PPSA (Cth) is based on the PPSA (NZ) which was in turn based generally on the PPSA (Sas) which, in turn, finds its genesis in Article 9 of the *Uniform Commercial Code* of the United States (UCC).)

The first way relates to enforcement between the immediate parties. Section 19 (1) provides that a "security interest" (defined in s 12) is enforceable against a "grantor" in respect of particular collateral only if the security interest has "attached" to the collateral. The expression "security interest" is defined in s 12(1) to mean:

> "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)"

Section 19 (2) provides that attachment occurs in certain circumstances. One of these is that "the grantor has **rights in the collateral**, or the power to transfer **rights in the collateral** to the secured party": s 19(2)(a) (my emphasis). Taken at face value, this provision would, comfortingly, seem to reflect the *nemo dat* rule. This is

because we are inclined to equate the statutory "rights in the collateral" with the general law's "property in the collateral".

But subs (5) of s 19 provides as follows:

> "For the purposes of paragraph (2)(a) a grantor has **rights in goods** that are leased or bailed to the grantor under a PPS lease, consigned to the grantor, or sold to the grantor under a conditional sale agreement (including an agreement to sell subject to retention of title) when the grantor retains possession of the goods." (my emphasis)

This provision leads us to expect that at least for the purpose of the attachment of a security interest, the *nemo* dat rule is to be contradicted.

14 Consistently with this expectation, a "PPS lease" is defined in s 13 to mean, among other things, a lease or bailment of goods for a term of more than one year (cf s 16 of PPSA (NZ), s 2(1)(y) of PPSA (Sas)) and under the general law a lessee or bailee would not be able to grant to a creditor a propriety interest in the goods because the lessee or bailee has none to grant. Yet the effect of ss 13 and 19(5) of the PPSA (Cth) is that in the case of a lessee or bailee under a PPS lease a "security interest" attaches to the goods.

15 The provisions create as it were a parallel universe. Things are not as they seem. Section 19(2) might have provided, but it does not provide, that for attachment to occur the grantor must have **property** in the collateral or the power to transfer **property** in the collateral. Likewise, subs (5) might have provided, but it does not provide, that under the transactions described in that subsection the grantor is **deemed to have property** in the collateral for the purpose of s 19 (2). But the old concepts and terms are discarded entirely.

16 I will set out the definition of "grantor" later (see [62]), but it is worth noting here that the grantor who is the lessee or bailee under a PPS lease has not, as the word might have suggested, granted, given or transferred anything. It is true that the lessee or bailee is a party to an agreement (a "security interest" must be provided for by a "transaction" – s12 (1)), but not one under which that party parts with any right or interest in the goods in favour of the lessor. On the contrary, the lessor parts with the right to possession and the lessee promises to pay and gives other promises. I digress to note among the exclusions from the scope of the PPS Act (Cth) provided

for in s 8 are interests in personal property created, arising or provided for by the operation of the general law (such as a lien or charge: s 8 (1)(c)).

17 In summary, and unfamiliarly, the PPSA (Cth) confers on the lessee or bailee under a PPS lease special statutory rights in the goods (for want of a better term a special form of "statutory property") and turns the lease or bailment on its head so that the lessee or bailee grants a security interest in the goods to the lessor or bailor.

18 The second and more significant way in which the *nemo dat* rule is contradicted by the PPSA (Cth) concerns the manifestation of the rule that a trustee in bankruptcy can take no greater property than that which the bankrupt had. It is "the property of the bankrupt", defined as the property divisible amongst the bankrupt's creditors, that vests in the trustee: *Bankruptcy Act 1966* (Cth) ss 5 ("property" and "the property of the bankrupt"), 58, 116. There must be "property" as defined and the trustee takes subject to equities, the trustee's title being no better than that of the bankrupt.

19 A company's title to its personal property does not change upon the making of a winding up order: its property remains vested in the same legal entity, although the powers of the directors are suspended in favour of the powers of the liquidator (*Corporations Act 2001* (Cth), s 471A). It is the "property" of the company that the liquidator must realise and distribute.

20 If the individual or company had been a lessee or bailee of goods no proprietary interest would vest in the trustee in the one case or be available in the winding up in the other case.

21 Against the above background, I will consider this second contradiction of the *nemo dat* rule as that contradiction is illustrated in one Canadian and two New Zealand cases and ask what lessons they may hold for Australian courts called on to interpret the PPSA (Cth). The cases are: *Re Giffen* [1998] 1 SCR 91; 155 DLR (4th) 332 (*Giffen*); *Graham v Portacom New Zealand Ltd* [2004] 2NZLR 528 (*Portacom*) and *Waller v New Zealand Bloodstock Ltd* [2005] 3 NZLR 629 (*Waller*).

Giffen

22 Telecom (the Lessor) leased a car to the British Columbia Telephone Company (Employer) which leased it out to its employee, Giffen, for more than twelve months

with an option for Giffen to buy it from Telecom. Although Telecom was not a party to the sublease, it was in various ways heavily involved in the arrangement which was part of a broader "plan" of the Employer for the benefit of its employees (the "Employee Agreement Personal Vehicle Lease Program/Flex Lease Program").

23 Giffen made an assignment in bankruptcy. The Lessor did not register a financing statement under the Personal Property Security Act of British Columbia (SBC 1989, c 36) (PPSA (BC)). This meant that the Lessor's security interest in the car was not perfected.

24 With the consent of the trustee in bankruptcy, the Lessor sold the car.

25 As under the PPSA (Cth), under ss 2 and 3 of the PPSA (BC) a lease of goods for a term of more than one year gave rise to a "security interest" in the lessor, even though it did not secure payment or performance of an obligation.

26 The trustee claimed the proceeds of sale. The trustee relied on s 20 (b) (i) of the PPSA (BC). That provision was to the effect that a security interest in collateral was not effective against a trustee in bankruptcy if the security interest was not perfected at the date of the bankruptcy.

27 The Lessor relied on the fact that Giffen had never owned the car and proposition that the trustee could not have a better title than Giffen had had – a manifestation of the *nemo dat* rule.

28 The primary Judge (Hood J of the Supreme Court of British Columbia) upheld the trustee's argument; the Court of Appeal for British Columbia upheld the Lessor's; and the Supreme Court of Canada upheld the trustee's.

29 The primary Judge followed a decision of the Saskatchewan Court of Appeal in *International Harvester Credit Corporation of Canada Ltd* v *Bell's Dairy Ltd (Trustee of)* (1986) 61 CBR (NS) 193. Hood J noted (a) that s 20 (b)(i) was even more favourable to the trustee than its Saskatchewan equivalent; and (b) that the Saskatchewan equivalent had been held to be constitutionally valid in *Paccar Financial Services Ltd* v *Sinco Trucking Ltd (Trustee of)* [1989] 3 WWR 481 (Sas CA).

30 In the British Columbia Court of Appeal ((1996) 16 BCLR (3rd) 29), Finch JA, with whom Macfarlane and Wood JJ A concurred, protested (at 40) that to allow the trustee's claim would be to "overlook fundamental concepts of bankruptcy law" as expressed in *Fleeming v Howden* (1868) LR1 Sc & Div 372 (HL) and *Flintoft v Royal*

Bank of Canada [1964] SCR 631. Finch JA concluded that s 20(b)(i) of the PPSA (BC) could not possibly have the effect of transferring title from the lessor, the true owner, to the trustee in bankruptcy because this would give the trustee greater property rights than the bankrupt had enjoyed. Finch JA considered that both *International Harvester* and the primary Judge had failed to give due weight to the terms of Canada's (federal) bankruptcy legislation which reflected the *nemo dat* rule.

31 The Supreme Court of Canada said (at [26]) that the Court of Appeal "did not recognise that the provincial legislature in enacting the PPSA, has set aside the traditional concepts of title and ownership to a certain extent." The Supreme Court added (at [28]):

> "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. It is in this context that the *PPSA* must be given its intended effect ...."

32 How was it that the *Bankruptcy and Insolvency Act*, RSC, 1985, cB-3 (the BIA) operated to vest Giffen's rights under the lease of the car in the trustee? The answer was by the Supreme Court's construing the BIA's definition of "property", especially the words "including every description of estate, interest and profit, present or future, vested or contingent, in, arising out of or incident to property", so as to encompass Giffen's special form of "statutory property". (Almost identical words occur in the definition of "property" in s 10 of the *Bankruptcy Act 1966* (Cth).)

33 Once that conclusion was reached, the case became one of a competition between the special statutory property of the trustee and that of the Lessor under its unperfected security. Section 20 (b)(i) expressly resolved that competition in favour of the trustee.

34 While the Supreme Court distinguished authorities on which the Court of Appeal had relied, it also clearly accepted (at [45]) that s 20(b)(i) "modifies the principle that a trustee is limited to the rights in property enjoyed by the bankrupt". At [56] Iacobucci J, who delivered the judgment of the Court, said:

> "...the principle that a trustee in bankruptcy cannot obtain greater rights to the property than the bankrupt had has been modified through the policy choices of the legislatures represented in s 20 (b)(i) of the *PPSA*, and its equivalents in other provinces."

So, the PPSA (BC) had repercussions outside the four corners of that statute and raised a novel question of construction of the BIA.

35 The question arises, how would *Giffen* be decided in Australia under the PPSA (Cth)? As Roger Giles says in his paper, it is necessary to attend, closely, first and last, to the text of the Australian Act.

36 The relevant provisions of the BIA were similar to the relevant provisions of the *Bankruptcy Act 1966 (*Cth).

37 Section 12(3)(c) of the PPSA (Cth) defines "security interest" to include the interest of a lessor or bailor of goods under a PPS lease whether or not the transaction concerned, in substance secures payment or performance of an obligation, and as noted earlier, s 13 defines "PPS lease" to include a lease for a term of more than one year.

38 Also as noted earlier, s 19(5) of the PPSA (Cth) provides that a grantor has "rights in" collateral when the grantor obtains possession of them, for the limited purpose of satisfying the particular requirement of attachment stated in s 19(2)(a).

39 There is no equivalent of s 20(b)(i) of the PPSA (BC) in the PPSA (Cth). A different approach is taken. It is found in Part 8.2 of the PPSA (Cth) which is very important. It applies to security interests granted, inter alia, by individuals who become bankrupt and by companies or bodies corporate that are being wound up, where the security interest has not been perfected. Briefly, s 267 within Part 8.2 provides that the unperfected security interest of the secured party vests in the grantor immediately before, for example, the sequestration order is made or the winding up order is made (s268 creates exceptions which I will not discuss). Perhaps the Australian legislation was drafted in this way in order to address the argument that was raised (unsuccessfully) in *Giffen*.

40 The retrospective vesting removes any doubt as to the question of whether the grantor had a proprietary interest capable of being caught by the vesting provision of the *Bankruptcy Act 1966* and the liquidator's powers under the *Corporations Act 2001*. It also puts it beyond question that it is the personal property itself that vests or is available, not some lesser interest in it.

41 The Australian technique of overcoming the *nemo dat* rule may be seen to be more straightforward that of s 20(b)(i) of the PPSA (BC). The PPSA (Cth) converts the ownership interest of the lessor into a "security interest" by s 12(3)(c), and if it has not

been perfected by the time of the making of the sequestration order, vests it in the grantor. The statute gives the grantor title which, consistently with the *nemo dat* rule the *Bankruptcy Act 1966* is then able to vest in the trustee in bankruptcy, or the *Corporations Act 2001* is then able to make available to the liquidator.

42 It should be noted that the PPSA (BC) was a Canadian provincial statute and, as noted earlier, there was a challenge to its constitutional validity (which did not occupy the Supreme Court in *Giffen).* In New Zealand and Australia the PPSAs and the bankruptcy legislation and corporations legislation are the product of the one legislature – in New Zealand because of its unitary system, and in Australia because of the referral of powers by the Australian states under s 51 (xxxvii) of the *Constitution* that underlies the enactment by the Commonwealth Parliament of the PPSA (Cth).

Portacom

43 *Portacom* also demonstrated the vulnerability of the unperfected security interest of a lessor (Portacom) – a lessor of five portable buildings to a company (NDG).

44 NDG granted a debenture over its assets to a bank (HSBC) which subsequently appointed receivers and managers of the assets. Portacom and the receivers were in competition for the portable buildings.

45 Importantly, the debenture was registered under the PPSA (NZ) but Portacom's interest in the buildings was not. (The PPSA (NZ) came into force on 1 May 2002 and HBSC promptly registered the debenture under it on 28 May 2002.)

46 Section 17(1)(b) of the PPSA (NZ), like its Canadian and Australian counterparts as previously noted, provides that a security interest includes a lessor's interest under a lease of goods for a term of more than one year. Under all three provisions that is so whether the lease does or does not secure payment or the performance of an obligation. (A lease for less than that period will create a security interest only if it does secure payment or performance of an obligation: cf s 12 (1) of the PPSA (Cth).)

47 It was accepted that the debenture created a security interest (cf s 12 (1), (2)(a), (b) of the PPSA (Cth)).

48 Rodney Hansen J considered that the contest between Portacom and the receivers was resolved by s 66 of the PPSA (NZ) which gave priority to a perfected security

interest over an unperfected security interest in the same collateral (s 55 (3) of the PPSA (Cth) is to the same effect).

49 Before considering the issues posed by the case, His Honour referred to authorities and commentary on the nature of the interests of lessors and lessees under a lease of goods. He noted that whatever the position under general law principles, s 40 (3) of the PPSA (NZ) (cf s 19 (5) of the PPSA (Cth)) recognises that a lessee has proprietary, not just possessory, rights in the leased goods. His Honour said (at [28]): "as against the lessee's secured creditors, the lessee has rights of ownership in the goods sufficient to permit a secured creditor to acquire rights in priority to those of the lessor."

50 His Honour answered the two issues that arose favourably to the receivers: (1) whether the debenture created a security interest in the portable buildings; and (2) whether the security interest under the debenture attached to the buildings.

51 It is interesting that in a sense, s 40 of the PPSA (NZ) and s 19 of the PPSA (Cth), like s 267 of the latter previously noted, actually assume the existence of the *nemo dat* rule by ensuring that the debtor (in Australia, "grantor") has an interest in order to support the creation of the security interest.

52 How would *Portacom* have been decided under the PPSA (Cth)? I have noted the comparable provisions above. Apparently, s 55 (3) of the PPSA (Cth) would give the perfected security interest of HSBC priority over the unperfected security interest of Portacom as lessor of the buildings.

Waller

53 *Waller* also concerned a competition between the interests of a chargee and a lessor. SH Lock (New Zealand) Ltd (Lock) held a registered debenture charge over the assets of a company, Glenmorgan Farms Ltd (Glenmorgan). Lock registered a financing statement to perfect its security interest under the PPSA (NZ). Glenmorgan leased a stallion named *Generous* from New Zealand Bloodstock Ltd (NZB) under a "lease to purchase agreement". Title to *Generous* remained in NZB at all times. NZB did not register a financing statement under the PPSA (NZ).

54 NZB terminated the agreement with Glenmorgan and took possession of *Generous*. Shortly afterwards Lock, acting under its perfected security interest, appointed receivers to the assets of Glenmorgan.

55 The lease was for more than one year and therefore gave rise to a statutory "security interest" in the lessor, NZB, for the purpose of the PPSA (NZ).

56 In terms of s 40 of the PPSA (NZ) (cf s 19(2) of the PPSA (Cth)), Lock had given value; Glenmorgan had "rights in" *Generous*; and the security was enforceable against NZB.

57 On the date on which the PPSA (NZ) came into effect (1 May 2002), Glenmorgan had "rights in" *Generous* which it could in law provide as security to Lock, and those rights were part of its after-acquired property and enabled Lock's security interest to "attach" to *Generous* (s 43).

58 Lock's perfected security interest was enforceable against NZB (s 36 (cf s 20 of the PPSA (Cth)) and enjoyed priority over NZB's unperfected security interest (s 66(c) (cf s 55(3) of the PPSA (Cth)).

59 William Young J dissented, but on a ground that is not of ongoing importance – that Lock's debenture pre-dated the PPSA (NZ) and the consequences of that fact.

60 In point, the majority, Robertson and Baragwanath JJ stated (at [74]) as part of their Conclusion that with respect to competing interests under the PPSA (NZ), the *nemo dat* principle is "ousted".

61 Under the PPSA (Cth), the chargee would have had a security interest under the charge (s 12 (2)) which would have been perfected by registration: s 21. NZB would have had a security interest under the lease which would have been a PPS lease (ss 12 (3)(c), 13 (1)(a)) but it would not have been perfected. Lock's perfected security interest would have taken priority over NZB's unperfected security interest: s 55 (3).

Definitions

62 The PPSA régimes depend on their definitions. Naturally, novel terms (see [2] above) will drive the courts to the definition section (the Dictionary – s 10 of the PPSA (Cth)). Some familiar terms are given defined meanings – not all of them to be expected. While the definitions of "general law", "land", "personal property" and "penalty unit", for example, are what we might have expected, the definitions of certain other

familiar terms are otherwise. Examples are “control”, “debtor”, “grantor” and “matter”, which are defined as follows:

“Control has the meaning given by Part 2.3.
Note: ***Control*** has an extended meaning in section 341 (control of inventory and accounts in relation to fixed and floating charges).”

Part 2.3 comprises ss 23-29 and deals with “possession” as well as “control” in rather complex terms.

“Debtor means:

(a) a person who owes payment or performance of an obligation that is secured by a security interest in personal property (whether or not the person is also the grantor of the security interest); or

(b) a transferee of, or successor to, an obligation mentioned in paragraph (a).”

The alternative “or performance of an obligation” is foreign to the general law concept of a debtor, but otherwise this definition is not alarming. It marks the distinction between the grantor (actual or notional) (see below) of the security interest and the person who owes the personal obligation that is secured.

“Grantor means:

(a) a person who has the interest in the personal property to which a security interest is attached (whether or not the person owes payment or performance of an obligation secured by the security interest); or

(b) a person who receives goods under a commercial consignment; or

(c) **a lessee under a PPS lease**; or

(d) a transferor of an account or chattel paper; or

(e) a transferee of, or successor to, the interest of a person mentioned in paragraphs (a) to (d); or

(f) in relation to a registration with respect to a security interest:

(i) a person registered in the registration as a grantor; or

(ii) a person mentioned in paragraphs (a) to (e).” (my emphasis)

Some of the reasons for the breadth of this definition will be evident from the discussion above.

“Matter includes act, omission, body, person and thing.”

It is odd that a “matter” includes a body or person.

63 The definitions show that the courts (and practitioners) should not readily assume that ordinary terms are used in their ordinary senses.

Conclusion

64 The cases discussed above suggest that some persuasive force remains with the “old law” but that Australian courts, like their Canadian and New Zealand counterparts, will need to apply the new law as a fresh and generally self-contained régime. I predict that they will do so.

65 The PPSA (Cth) is, at least in many (but not all) of its provisions, so similar to the régimes of Canada and New Zealand, that decisions under those régimes will be of interest to Australian courts but they will not, of course, be binding and will, at most, suggest illuminating arguments and approaches. Australian courts will need to attend first and last to the text of the PPSA (Cth).

66 As lawyers, we necessarily approach any statute with the equipment that our legal education and experience in practice have given us. I predict that the parallel universe introduced by the PPSA (Cth) will lead, in the forensic setting and elsewhere in our legal world, to numerous correctives of the kind “ But just a moment that is not what this Act says”.