

Article Information

Author: Martin Lovell

Service: Banking & Finance, Corporate & Commercial, Corporate & Commercial Finance, Personal Property Securities, Restructuring & Insolvency

Sector: Financial Services

PPSA Case Law Update

Three recent decisions provide useful reminders for secured lenders and trust beneficiaries of the importance of accurately documenting and perfecting security interests under the Personal Property Securities Act 2009 (PPSA).

Keon Pty Ltd as trustee for Keon Family Trust v Goldfields Equipment Pty Ltd (In Liquidation) [2020] WASC 61

Keon Pty Ltd lent around \$300,000 to Goldfields Equipment Pty Ltd. This loan was documented in a deed which said the loan was made 'with an associated floating mortgage over all business assets' of the borrower and also contemplated the execution of a 'charge' by the borrower. However, no separate charge or security agreement was executed.

When a liquidator was appointed to the borrower, the lender claimed that it had a security interest under the deed. The Court disagreed, finding that the wording in the loan deed was not sufficient to create a floating charge. In doing so, the Court took into account that, on the face of the deed, a further security document was clearly contemplated by the parties.

This decision makes it clear that finance documents must include wording which clearly and unambiguously creates a security interest or charge. It is not sufficient to simply refer to the loan as being secured or to contemplate that a security interest or charge will, or may, be granted by the borrower or security provider. In practice, it is often prudent to document security separately from the loan agreement and to ensure that the security document is duly executed and registered.

StockCo Agricapital Pty Ltd v Dairy Livestock Services Pty Ltd [2020] NSWSC 318

This case involved a dispute over a sum of money which Dairy Livestock Services Pty Ltd (**DLS**) received from selling several hundred cattle on behalf of Reid Agricultural.

Reid Agricultural had a credit account with a stock and station agent DLS which granted DLS a purchase money security interest (PMSI) and a security interest over stock supplied by DLS. This security interest secured the purchase price for stock as well as feed and agistment. This was perfected by registration on the PPSR as a PMSI.

StockCo Agricapital Pty Ltd (**StockCo**) subsequently agreed to fund the purchase of certain cattle with DLS acting as purchasing agent and charging a fee for its service. StockCo's financing documents provided that: (a) all stock were acquired by the customer as agent for StockCo; (b) StockCo had a security interest over any acquired stock, any product derived from stock and proceeds; and (c) StockCo also took a general security over any other stock of the customer, whether purchased under the facility or not. This was perfected by registration on the PPSR as both a PMSI and as a non-PMSI, but lodged after the DLS registration was already in place.

DLS sold stock for Reid and there was a dispute over whether StockCo was entitled to the proceeds of that sale in priority to DLS.

The Court found that StockCo held a perfected PMSI over the cattle, despite the fact that Reid (as purchaser) had already taken possession of the stock before the Stock Co facility and PMSI registration was in place. DLS contended that this meant that StockCo had not perfected its security interest in the cattle by registration at the time the purchaser obtained possession, as required under section 62(2)(b)(i). The Court, however, applied the reasoning of the Supreme Court of South

Australia – Full Court in *Samwise Holdings Pty Ltd v Allied Distribution Finance Pty Ltd (2018) 131 SASR 506*, restating the principle that the “possession” referred to in section 62(2)(b)(i) of the PPSA is possession as *grantor* of the security interest. Prior possession in another capacity does not count. The purchaser only obtained possession of the cattle, for the purposes of section 62(2)(b)(i), when the stock became subject to the security interest under the agreement between it and StockCo.

DLS had already been reimbursed for the purchase price of the initial stock out of the funds advanced by StockCo and the other amounts for feed and agistment covered by the DLS security interest did not have PMSI priority. Accordingly, StockCo’s PMSI had priority over DLS’s non-PMSI security interest.

This is the first case in Australia to consider and uphold the view in *Samwise Holdings* that “possession” for the purposes of 62(2)(b)(i) needs to be interpreted as possession as a *grantor* of a security interest, not possession *simpliciter*.

Dalian Huarui Heavy Industry International Company Ltd v Clyde & Co Australia [2020] WASC 132

This case concerned the fate of \$27m held in a solicitor’s trust account as security for a claim being arbitrated in Singapore and considered the status of those trust arrangements under the PPSA.

Dalian Huarui Heavy Industry International Company Ltd (**Dalian**) and Duro Felguera Australia Pty Ltd (**Duro**) were involved in a contractual dispute in relation to an iron ore project in Western Australia with Dalian claiming payment for various goods supplied and delivered as a subcontractor to Duro. The dispute was the subject of arbitration in Singapore and a sum of \$27m had been deposited by Duro into an Australian trust account held by its solicitors, Clyde & Co Australia (**Clyde & Co**) to provide some assurance of available funds if Dalian’s claim was ultimately successful. The parties entered into a trust agreement setting out the terms on which the \$27 million could be dealt with or paid to Dalian, including in accordance with a direction of the tribunal (**Trust Agreement**).

Dalian was successful in obtaining an award from the tribunal and claimed that the \$27m should be transferred to it by Clyde & Co. However, Duro subsequently entered voluntary administration and the administrators’ lawyers requested that the funds not be distributed until the administration had been finalised.

As part of the judgement, Kenneth Martin J had to consider the nature of the trust arrangements and whether they gave rise to a security interest under the PPSA. It was held that the arrangements for security initially conferred on Dalian an equitable interest in the trust amount by way of security in the form of an equitable charge or lien. While Dalian’s interest was at first contingent on it winning its case against Duro, it was then “perfected to fully vest unconditionally” under the terms on the Trust Agreement on the tribunal’s issue of an order directing Clyde & Co to immediately release the trust amount to Dalian’s lawyers.

The Court held that the transactions under the Trust Agreement gave rise to a security interest under s12(1) of the PPSA with Duro, as grantor, creating a security interest in favour of Dalian over the trust amount held in Australia by Clyde & Co. Because the funds were held under a consensual arrangement in connection with the arbitration the Court held that it was not excluded by virtue of section 8.1(c) of the PPSA.

Dalian never registered this security interest on the PPSR and consequently there was an argument that it was unperfected and subject to the vesting rule under s267 of the PPSA at the time that Duro went into administration on 28 February 2020.

However, applying the extended definition of “possession”, by reference to section 24(2) of the PPSA, the Court considered that the trustee (i.e. Clyde & Co) held the funds on behalf of Dalian and that the security interest was therefore perfected under the PPSA by possession by Clyde & Co holding the funds for Dalian absolutely. This is despite the fact that the collateral was intangible property which is not generally subject to perfection by ‘possession’ and that at the time of the administration Duro did not have any continuing interest in the funds.

This decision suggests that a party with a right to funds held under an escrow or trust arrangement has a security interest under the PPSA which needs to be perfected against the party who retains the residual beneficial interest (not against the trustee or escrow agent itself). It also suggests that once a party becomes absolutely entitled to payment of funds held in escrow, that security interest may be treated as perfected by possession for the purposes of the PPSA, notwithstanding that the funds are intangible property and still held by the trustee or escrow agent.

We anticipate that this decision will be subject to considerable debate.

Key Takeaways

- The decision in *Keon Pty Ltd as trustee for Keon Family Trust v Goldfields Equipment Pty Ltd (In Liquidation)* [2020] WASC 61 highlights the risks of entering into a secured loan agreement without a separate security deed or clear charging clause.

- Parker J, in *StockCo Agricapital Pty Ltd v Dairy Livestock Services Pty Ltd* [2020] NSWSC 318, confirmed that the point in time from which a PMSI must be perfected in order to enjoy super-priority is calculated from when the grantor obtains possession of the particular collateral **as the grantor** of the security interest, notwithstanding prior possession of the collateral.
- In *Dalian Huarui Heavy Industry International Company Ltd v Clyde & Co Australia* [2020] WASC 132, the Supreme Court of Western Australia held that 1) a contingent equitable interest in funds held on trust pending an arbitral decision is a security interest under the PPSA and; 2) once a person becomes absolutely entitled to trust funds under a trust or escrow deed, that person's security interest may be perfected by "possession" under the PPSA, despite the funds remaining in the hands of the third party trustee.