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PERSONAL PROPERTIES SECURITIES ACT 2009 (CTH)

1. INTRODUCTION

1.1 For many practitioners and businesses the following statement aptly summarises their experience with the *Personal Properties Securities Act* 2009 (Cth) (**PPSA**) and the Personal Properties Securities Register (**PPSR**):

> *"..unfamiliar terms and uncertain concepts are used in complex provisions, in a way that can make it even more difficult to determine how those complex provisions inter-relate with each other. The cumulative effect is that the Act can be very difficult to understand and to work with."*[1]

1.2 Pursuant to s 343 of the PPSA and the terms of reference of the Honourable Attorney-General, Mr George Brandis QC, a review was undertaken of the PPSA culminating in a final report being issued in February 2015 (**the Review**).[2]

1.3 In discussing the Review, I will provide an overview of the:

(a) PPSA;

(b) purpose of the Review;

(c) the procedure undertaken;

(d) overview of the Review;

(e) the recommendations. In doing so I will deal with some of the specific recommendations.

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1 Review of the PPSA Final Report by Bruce Whittaker dated 27 February 2015- Chapter 3.2.3. The report may be found on the website: http://www.ag.gov.au/consultations/pages/StatutoryreviewofthePersonalPropertySecuritiesAct2009.aspx

2 The report was prepared by Bruce Whittaker. That report and the interim report of Bruce Whittaker dated 31 July 2014 is used in the preparation of this paper.

1.4 This will assist practitioners to obtain a better understanding of the PPSA and difficulties that have been encountered not only by professionals but a number of different stakeholders in dealing with this new legislative regime.

1.5 The Review provides an excellent point of reference for a better understanding of many of these issues. If a more in-depth appreciation of an issue is required, then it is suggested consideration be given to reviewing those stakeholder submissions which have been published on the review website.[3]

1.6 I will, also, consider a lawyer's lien in the context of the PPSA.

2. PPSA

2.1 The PPSA commenced in January 2012. At this time the *Corporations Act 2001* (Cth) (**Corporations Act**) was also amended to recognise this new regime.

2.2 The transitional provisions ended in January 2014.

2.3 The PPSA, being modelled on the New Zealand, Canadian and US legislation, was to establish a single national law governing security interests in personal property and replace the then existing regime which was considered complex. It was envisaged that the PPSA would result in more certain, consistent, simpler and cheaper arrangements for personal property securities.[4]

2.4 The contributions to the Review by the many stakeholders identified that this object may not yet have been achieved. Other legislation outside of the PPSA also continues to regulate some areas of security interests in personal property.[5] The PPSA is not truly a single national law governing security interests in personal property.

[3] Supra, footnote 1.
[4] Explanatory Memorandum.
[5] Such as the Corporations Act. Section 4A of the *Storage Liens Act* 1973 (Qld) provides that a storer's lien on goods is declared to be a statutory interest to which s 73(2) of the PPSA applies and has priority over all security interests in relation to the goods.

3. PURPOSE OF REVIEW AND PROCEDURE

3.1 Section 343 provided for a review of the operation of the PPSA to be undertaken and completed within three years of the registration commencement time.

3.2 The terms of reference were wide ranging and included the following aspects of the PPSA:

(a) effects of the reforms on Australian business and particularly small business, consumers and the markets for business and consumer finance in Australia;

(b) level of awareness and understanding of the PPSA;

(c) incidences, and where applicable, causes of non-compliance with the PPSA, particularly by small business;

(d) the interaction of the PPSA with the Corporations Act; and

(e) broadly, the opportunity for further efficiencies.

3.3 After calling for submissions and input from stakeholders, an interim report was delivered in July 2014.[6] The report recommended that action be taken to support a greater understanding of the PPSA amongst small business. I did not recommend any immediate legislative change.

3.4 Like the Review, the interim report highlighted the lack of awareness in small business of the PPSA, its operation and also the effect of the Act with respect to non-compliance. This lack of awareness included a failure to understand that ownership was no longer sufficient to protect a party's interest in personal property.

3.5 The interim report also identified that the submissions provided indicated a view that the PPSA was complex and that small business had difficulty determining the impact of the Act on their particular business. Such complexity also related to the PPSR and the difficulties being encountered by small business in understanding the registration process and how to complete the financing statement.

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[6] By Bruce Whittaker dated 31 July 2014.

3.6 Using the submissions provided by stakeholders for the interim review, Mr Whittaker identified potential areas of reform that would be considered by release of a series of supplemental consultation papers.

3.7 The Review identifies that 37 submissions were provided for the interim report and 55 second round submissions were provided. Following the receipt of the second round submissions, four consultation papers were issued as follows:

(a) reach of the PPSA;

(b) creation and perfection of security interests, take free rules, priority rules and other dealings in collateral;

(c) enforcement of security interests, vesting of interests on insolvency, interaction with other legislation, governing law rules, other provisions of the PPSA and layout of the PPSA;

(d) the PPSR.

3.8 It is identified that 83 responses were received from a wide range of stakeholders, including industry organisations, individual businesses, law firms, law societies, government bodies and academics (both in Australia and overseas). Those responses provided a foundation for many of the recommendations.

4. THE REVIEW IN SUMMARY

4.1 The overall response of the submissions received is that there was support for the overall framework of the PPSA, but the Act required legislative change to reduce its complexity.[7]

4.2 The Review, importantly for stakeholders, identifies that according to the submissions more still needs to be done by way of reform if the PPSA is to achieve its goals of being certain,

[7] Interim Report, Executive Summary; Review, Chapter 1 - Executive Summary and Chapter 4.1.4.2 and 4.1.4.3.

consistent and simpler, and to provide cheaper arrangements for personal property securities There was no one single change identified that may greatly improve the Act.[8]

4.3 Like for the interim report, it was identified by the Review that a fresh educational campaign was needed if any legislative reforms were to realise the objectives of the PPSA.[9] The lack of awareness and understanding of the PPSA among users was the primary reason why businesses are failing to comply with the Act.[10]

4.4 Apart from the lack of awareness and understanding, other causes of non-compliance were identified as utilisation of concepts and terminology adopted from other jurisdictions which are not relevant to commerce or business in Australia and that the design of the legislation is "too divorced from the realities of the market place for which it was designed".[11]

5. RECOMMENDATIONS OF THE REVIEW – AN OVERVIEW

5.1 The Review considered 394 potential legislative changes and provided a recommendation with respect to each of these.[12] A number of the recommendations for change are interdependent. That is, a recommendation will only be relevant if another recommendation is adopted or alternatively, will only be relevant if another recommendation is not adopted.[13]

5.2 Each proposed legislative change was considered in the context of identified criteria and segregated into the following chapters:

(a) the reach of the PPSA – Chapter 3, which deals with types of transactions that should be covered by the Act and why, the "in substance" security interests under s 12, deemed security interests under s 12(3), meaning of "personal property" and exclusions as provided by s 8;

(b) creating an effective security interest – Chapter 5 which considers attachment, enforceability against third parties and perfection;

8 Chapter 1 - Executive Summary.
9 Chapter 1 - Executive Summary.
10 Chapter 3.2.3.
11 Chapter 3.2.3.
12 These are summarised in Annexure E to the Review.
13 Chapter 10.1.1.

(c) perfection by registration – Chapter 6. This chapter considers the PPSR;

(d) dealings with collateral – Chapter 7 which, considers terminology, transfers or collateral, leases, proceeds, temporary perfection, taking free rules, priority rules between security interests, priority rules with other interests in the collateral, accessions, processed and commingled goods and ss 79 to 81,

(e) enforcement of security interests and insolvency of grantor – Chapter 8. This chapter considers ss 267 and 267A dealing with vesting of a security interest on a grantor's insolvency;

(f) interaction with other laws; other matters relating to the content of the PPSA – Chapter 9, which includes consideration of circulating assets, s 588FL of the Corporations Act, insolvency proceedings and requests for information under s 275.[14]

5.3 Each recommendation is addressed using a standard format which firstly, identifies and discusses the relevant issue to which the recommendation is addressed, secondly discusses the stakeholder feedback and thirdly provides an outcome in the form of the recommendation.

5.4 Chapter 10 discusses and provides recommendations for the consideration and implementation of reforms.

5.5 In broad terms, the following were identified as ways of achieving the legislative objective for the PPSA:

(a) simplify the content of the Act and the regulations, by using streamlined language and removing provisions of marginal benefit;

(b) simplify the register, by reducing the number of decisions for users and making options much clearer;

(c) using more customary and intuitive terminology;

(d) explain the concepts;

(e) better reflect Australian conditions.[15]

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[14] The criteria applied is set out in Annexure B to the Review.

5.6 Finally, the Review recommended that a further review be undertaken in consultation with stakeholders in five years to determine whether there is any need for further reform of the PPSA.[16]

5.7 For practitioners and those who read the Review, it will assist in providing a better appreciation and understanding of the issues being encountered by not only other practitioners, but also clients dealing with the PPSA and the PPSR.

6. SPECIFIC RECOMMENDATIONS OF THE REVIEW

IN SUBSTANCE AND DEEMED SECURITY INTERESTS

6.1 As stated in the Review the concept of a security interest "lies at the very heart" of the PPSA.[17]

6.2 By s 12 a security interest is an interest in personal property that "in substance", secures payment or performance of an obligation and an interest which the PPSA deems to be security interest.[18]

6.3 The term "interest" in personal property is defined in s 10 to include a right in personal property. Stakeholder submissions identified that this definition creates uncertainty as it is not clear whether a pure contractual right as compared to a proprietary right is an interest in personal property. The Review agreed that the current definition is unclear as to whether or not a purely contractual interest was caught by the definition and that a security interest should only capture interests that are proprietary in nature.[19]

In substance security interests

6.4 Section 12(2) identifies examples of "in substance transactions" that are security interests where they secure payment or performance of an obligation. Although a number of

15 Chapter 3.4.
16 Chapter 10.3.
17 Chapter 4.2.
18 Ss 12(1) & (2) (in substance security interests) and s 12(3) (deemed security interests).
19 Chapter 4.2.2.1.

submissions considered that this sub-section was superfluous, it was recommended that the provisions be retained.[20]

6.5 There were a number of recommendations for change to this sub-section as follows:

(a) section 12(2)(d) – conditional sale agreements. It is recommended that the provision be amended to read “an agreement to sell subject to retention of title” to avoid confusion and to make the PPSA easier to understand and use;

(b) sections 12(2)(h), (i) and (j) – interests that may be deemed security interests. Sub-sections (h) and (i) were considered to serve two purposes. Firstly, to confirm that a consignment or lease can be an “in substance” security interest on general principles and secondly, to confirm that a commercial consignment or a PPS lease can be an “in substance” security interest under s 12(1) as well as a deemed security interest under s 12(3). It was thought that s 12(2)(j) dealing with an assignment could be clarified by changing the sub-section to read “a transfer of an account”;

(c) section 12(2)(k) – transfer of title. It is recommended that this provision be deleted. The expressions “assignment” in s 12(2)(j) and “transfer” in s 12(2)(k) cover, it was said, very similar concepts;

(d) section 12(2)(l) – flawed asset arrangements. It is recommended that this provision be deleted. The Review identified that this provision has generated controversy and uncertainty. It is not clear, it was said, what the term “flawed asset arrangement” captures. The Review identified that amongst financiers this was understood to refer to a right to receive a payment of money that is subject to a condition that must be satisfied before payment is made. Such an arrangement may not provide the financier with any proprietary interest in the money. If the transaction “in substance” secures the payment or performance of an obligation then it will be caught by s 12(1).

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[20] Chapter 4.2.3.

Deemed security interests

6.6 Section 12(3) deems three interests to be security interests as follows:

(a) an interest of a transferee under a transfer of an account or chattel paper;

(b) the interest of a consignor who delivers goods to a consignee under a commercial consignment; and

(c) an interest of a lease or bailor of goods under a PPS lease.

6.7 Whether or not as a matter of legislative policy these interests ought to be deemed as security interests was a significant issue in the submissions to the Review. The Review observed that the approach taken in s 12(3) was not readily reconcilable with the approach taken in s 12(1), as s 12(3) focusses on the form of the transaction rather than its substance.

6.8 For the purposes of this paper I only wish to consider PPS leases which is referred to below under the heading "PPS lease".

7. PERFECTION BY REGISTRATION – Chapter 6

7.1 The PPSA provides a number of ways in which a security interest can be perfected over collateral. If the security interest has attached to the collateral and is enforceable against a third party then it may be perfected by:

(a) firstly, registration;

(b) secondly, possession;

(c) thirdly, for certain types of collateral by control.[21]

7.2 As stated in the Review, these methods of perfection all have a publicity object in that they provide notice to outsiders that the property in question is subject to a security interest.[22]

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[21] S 21.
[22] Chapter 5.3.2.1.1.

7.3 The most common method of perfection is by registration on the PPSR.

7.4 As recognised by the Review and as identified in the submissions of stakeholders, registration on the PPSR has caused significant difficulties for small business and the system of registration is too complex.[23]

7.5 There is also a common theme in the submissions that the register is too cluttered. It is difficult to make sense of search results for a grantor as searches often contain information about numbers of registrations. It identified that as at 31 December 2014 the register contained 8,417,283 registrations and of those, 1,313, 629 had been migrated for earlier registrations with no end time and 688,356 had been migrated with an end time of 7 years. The data, it was said, suggests that clutter is limited to a small number of grantors.[24]

7.6 The Review recommended a number of changes to simplify the register and make it easier to use. It is said that the overall design of the register should be re-considered.[25]

7.7 The issues identified by stakeholders in using the register included the following:

(a) the layout of the register. A number of submissions suggested that the manner in which questions are presented could be more intuitive and user-friendly. It is recommended in the Review that the layout of the register and the order and manner in which questions are asked be reviewed to make the register as simple and easy to use as possible, particularly from the perspective of an unsophisticated user;

(b) the distinction between consumer and commercial property. The registration with respect to consumer property is for 7 years and if the collateral is also serial number property then the registration can only describe the collateral by its serial number and may not identify the grantor.[26] It is recommended that the PPSA be amended so that registration does not need to identify whether the collateral is consumer or commercial property with other amendments to maintain the 7 year term of registration for registrations against individuals or against serial numbered

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[23] Chapter 6.1.
[24] Chapter 6.9.1.
[25] Chapter 6.1.2.
[26] S 153, Item 2(a) of the table.

property that may not identify the grantor. A registration that is made against only a serial numbered property and that identifies the serial number may not identify the grantor, if the grantor is an individual. It is recommended that the definition of "consumer property" and "commercial property" in s 10 be deleted. Other recommendations are with respect to other provisions of the PPSA where those terms are used;

(c) item 8 in the table to s 153(1) enables the regulations to prescribe any matter to be included in the financing statement. Item 1 of the table in clause 4.1 of Schedule 1 to the *Personal Property Securities Regulations* 2010 (Cth) (**regulations**) provides with respect to registration of collateral that is commercial property that the financing statement must indicate "whether or not the collateral may include inventory". This item states that the purpose is to determine "whether the collateral may include inventory for Part 9.5 of the Act", which deals with circulating assets. As stated in the Review, this suggests the meaning of the term "inventory" used in this item is different to the definition in s 10. The Review agreed with a number of submissions that this question ought to be deleted on the basis that it is confusing and does not serve any useful purpose;[27]

(d) it is also recommended that item 2 of the table in clause 4.1 of Schedule 1 to the regulations be deleted, which requires a registration against collateral that is commercial property to indicate "whether or not the collateral may be subject to control". It was suggested in the submissions that this question created confusion;

(e) item 7 of the table to s 153(1) relevantly requires the registrant to state whether the security interest is, or is to be, a purchase money security interest to any extent if the security interest is in respect to a class of collateral prescribed by the regulations for that purpose. Regulation 3.1 prescribes for item 7 that property is in a prescribed class for such purposes if the collateral can be subject to a PMSI under s 14(1). Section 66(2)(c) provides as one of the conditions for a PMSI to take priority over other security interests, as provided for in that provision, that the registration that perfects the security interest complies with item 7 of the table to

[27] Chapter 6.2.

s 153(1) by stating that the interest is a PMSI. The Review identified that a number of the submissions contended that both item 7 of the s 153(1) table and s 66(2)(c) ought to be deleted as registrants may be confused as to whether in fact the security interest was a PMSI and ramifications for not ticking the "PMSI box" are draconian.[28] In Chapter 7.7.8.11.3 of the Review it is recommended that s 62 be amended to require a secured party who claims a PMSI to give notice of this to existing secured parties or provide other information in its registration. It is then recommended that s 62(2)(c) and item 7 of the s 153(1) be deleted. Alternatively, if item 7 is to be retained, it be made clear that a registration that does not tick the box can nonetheless perfect a PMSI, but on the basis that the PMSI cannot benefit from the super-priority provided by s 62.[29]

7.8 The functionality and uncertainty of the collateral classes is considered.[30] A registrant, particularly an unsophisticated one, may have difficulty identifying the appropriate class of collateral, particularly where item 4(c) of the s 153(1) table prescribes that one class of collateral is to be identified in the financing statement. This may result in a number of financing statements being registered with respect to different classes of collateral.

7.9 A number of different options for change were identified in the submissions, including reducing the number of classes, allowing registration in a financing statement to be against more than one class and creating a further class called "all present and after acquired property relating to". Although there was a consensus in the submissions that there was a need for legislative change there was not a consensus as to the form of the amendment.[31]

7.10 The Review considered this issue in the context of the stated core purpose of the register "to provide a person who is proposing to take an interest in another person's personal property with an opportunity to determine whether a secured party might have a competing interest in the property".

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28 Chapters 6.2.5 and 7.7.8.11.

29 Chapter 6.2.5.3,

30 Item 4(c) of the s 153(1) table provides that the collateral covered by a financing statement "must belong to a single class of collateral prescribed by the regulations". Clause 2.3 of Schedule 1 to the regulations prescribes nine classes.

31 Chapter 6.3.1.

7.11 It is said that such purpose may be fulfilled by requiring the financing statement to include an exact description of the collateral and only provide for registration of the financing statement after security agreement has been entered into. Abolition of the classes of collateral, it is considered, does not fulfil this purpose.

7.12 A reduction in the number of classes and simplification of the distinctions between them is the preferred approach, which is supported by the majority of the submissions. The ability for a financing statement to refer to a number of classes at the same time is recommended.

7.13 The Review also considers and makes recommendations regarding other fields in the financing statement including the "free text field", serial numbered property, including what types of property should be serial numbered property, motor vehicles and the definition in regulation 1.7 and grantor identifiers, particularly in relation to individuals, body corporates, trusts, multiple grantors and details of security holders.[32]

7.14 The effectiveness or ineffectiveness of registrations is an important issue for security holders and this is considered by the Review. The question identified is, what is the consequence of not-complying with s 153(1)?[33] This provision provides that a "financing statement with respect to a security interest ….consists of data that complies" with the table. The opinion of the author of the Review is that it was not intended that any error in the data in a registration would stop it from being a financing statement for the purposes of the PPSA. It is recommended, however, that this be clarified by amending s 153(1).

7.15 Then for the purposes of 164, when is a registration ineffective? The Review noted that a number of the submissions identified that there is an overlap between ss 164(1)(a) and (b). Yet, s 166 provides qualifications to s 164(1)(b), but not to s 164(1)(a). It is therefore unclear if the exception should apply if both ss 164(1)(a) and (b) are applicable in the relevant circumstances.

7.16 The Review recommends that ss 164(1)(a) and (b) be amended to read as follows:

> "(a) a defect mentioned in s 165; or

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32 Chapters 6.7 and 6.8.
33 Chapter 6.10.

(b) any other defect in any data relating to the registration, other than a defect of a king prescribed by the regulations, if the defect is seriously misleading."

7.17 There is no guidance in the PPSA to the meaning of "seriously misleading defect in any data" as provided for in s 164(1)(a). In a number of the submissions it was considered that the PPSA ought to clarify what is meant by "seriously misleading".

7.18 The Review, however, in the context of the authorities in Canada which have considered this term did not recommended that the PPSA be amended to include a definition of "seriously misleading".

7.19 It is also recommended that s 165(c) be repealed. That provision provides that a registration is taken to be defective if it indicates a security interest that is a PMSI, however the security interest is not a PMSI to any extent.[34]

8. PPS LEASE

8.1 The PPSA has and continues to have a significant impact on the hire industry in Australia. A number of submissions were made on this area by various stakeholders.

8.2 The Review identified that the concept of the PPS lease, and the consequences thereof for the owner, was the subject of more comments (and criticisms) in the submissions than for any other topic subject of the Review.[35]

8.3 The issues considered in the submissions and by the Review included:

(a) the legislative policy for inclusion in the PPSA of the deemed security interests, which includes the PPS lease;[36]

(b) the concept of a PPS lease;[37]

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[34] Chapter 6.10.3.2.3.
[35] Chapter 4.3.5.1.1.
[36] Chapter 4.3.1.2.
[37] Chapter 4.3.5.

(c) dealings in collateral: whether a lease of goods can be a transfer of goods for the purposes of the PPSA; leases and s 267 and chains of leases/sub-leases.[38]

Policy of including deemed security interests

8.4 Section 12(3) provides that a security interest includes the interest of a lessor or bailor of goods under a PPS lease, whether or not the transaction concerned, in substance, secures the payment or performance of an obligation.

8.5 The Review identified that the approach taken by the PPSA in s 12(3) is not easy to reconcile with nature of the security interest prescribed by s 12(1).[39] One possible policy reason for including the PPS lease is to ensure that persons may be able to ascertain whether there is an existing security interest in the goods. Otherwise, there may be capacity for a person who is not the owner of the goods to mis-represent the extent of their rights in the property to third parties.[40]

The PPS lease concept

8.6 By s 10 the term "PPS lease" has the same meaning given by s 13. Section 13 defines a PPS lease as follows:

> (1) A ***PPS lease*** means a lease or bailment of goods:
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> (a) for a term of more than one year; or
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> (b) for an indefinite term (even if the lease or bailment is determinable by any party within a year of entering into the lease or bailment); or
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> (c) for a term of up to one year that is automatically renewable, or that is renewable at the option of one of the parties, for one or more terms if the total of all the terms might exceed one year; or
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> (d) for a term of up to one year, in a case in which the lessee or bailee, with the consent of the lessor or bailor, retains uninterrupted (or substantially uninterrupted) possession of the leased or bailed property for a period of more than one year after the day the lessee or bailee first acquired possession of the property (but not until the lessee's or bailee's possession extends for more than one year); or

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38 Chapters 7.3 and 8.7.4.
39 Chapter 4.3.1.2.
40 Ibid.

(e) for goods that may or must be described by serial number in accordance with the regulations, if the lease or bailment is:

(i) for a term of 90 days or more; or

(ii) for a term of less than 90 days, but is automatically renewable, or is renewable at the option of one of the parties, for one or more terms if the total of all the terms might be 90 days or more; or

(iii) for a term of less than 90 days, in a case in which the lessee or bailee, with the consent of the lessor or bailor, retains uninterrupted (or substantially uninterrupted) possession of the leased or bailed property for a period of 90 days or more after the day the lessee or bailee first acquired possession of the property, (but not until the lessee's or bailee's possession extends for 90 days or more).

(2) However, a ***PPS lease*** does not include:

(a) a lease by a lessor who is not regularly engaged in the business of leasing goods; or

(b) a bailment by a bailor who is not regularly engaged in the business of bailing goods; or

(c) a lease of consumer property as part of a lease of land where the use of the property is incidental to the use and enjoyment of the land; or

(d) a lease or bailment of personal property prescribed by the s for the purposes of this definition, regardless of the length of the term of the lease or bailment.

Bailments for value only

(3) This section only applies to a bailment for which the bailee provides value.

8.7 On 19 March 2014 the *Personal Property Securities Amendment (Deregulatory Measures) Bill* 2014 (Cth) was introduced into the House of Representatives. On 14 May 2015 the Bill was passed through the House of Representatives and was introduced into the Senate and read for the first time. It is proposed by the Bill to repeal s 13(1)(e). A corresponding amendment will be made to repeal s 268(1)(a)(ii) to delete the reference to this type of PPSA lease as an exception to the vesting provisions under ss 267(2) and 267A.

8.8 The Review supported in its recommendations the removal of s 13(1)(e).[41]

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[41] Chapter 4.3.5.2.3.

8.9 A significant issue considered by the Review is whether a PPS lease should apply to a lease for an indefinite term of 1 year if it is not an "in substance" security interest. The submissions identified that it was common to lease goods for a short period and often circumstances of short notice and which may involve serial number goods or equipment that will be inventory in the hands of the lessee. It may be impracticable to register a financing statement before handing over the goods.[42]

8.10 It was identified that the submissions suggested that the current regime is a major risk and source of concern for the hire industry, particularly as the PPS lease includes short term hiring arrangements for an indefinite term. This exposes lessors to risk. The Review noted that the majority of the submissions were in favour of a proposal that a lease for an indefinite term of 1 year should only be a PPS lease if it in fact runs for more than a year.

8.11 It is recommended by the review that s 13(1)(b) be deleted and the words "an indefinite term or" be inserted at the start of s 13(1)(d).[43]

8.12 Consideration is also given to whether or not the one year test should be changed. It is recommended that no change be made.[44]

<u>Dealings in collateral</u>

Sections 267 and 267A

8.13 In broad terms, s 267 provides that for those insolvency administrations described in sub-section (1)(a) where the security interest is not perfected by the times set out in sub-section (1)(b), the security interest held by the secured party vests in the grantor immediately before the event mentioned in sub-section (1)(a).[45]

8.14 The Review specifically considers the concerns of the hire industry by the impact of s 267, which states in part as follows:

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[42] Chapter 4.3.5.4.1.
[43] Chapter 4.3.5.4.3.
[44] Chapter 4.3.5.5.
[45] S 267(2). This provision does not apply to those security interests described in s 268.

"It was argued in a number of submissions from the hire industry that ss 267 and 267A should not apply to a PPS lease if it is not an in-substance security interest under s 12(1)".

8.15 The Review identified that what was telling by s 268, is that ss 267 and 267A did not apply to other types of deemed security interests, such as transfers of account or chattel paper and commercial consignments. It was considered that there was no sound policy reason for excluding those types of deemed security interests and not PPS leases as well.

8.16 It is recommended that the exception prescribed by s 268(1)(ii) be amended to read "(ii) a PPS lease".[46]

8.17 It is also recommended that the definition in s 13 be amended to remove all reference to "bailments" as the retention of bailments will continue to cause uncertainty and produce undesirable outcomes.[47]

8.18 Such an amendment will alleviate to a significant extent the concerns financiers and the hire industry have with respect to leases/sub-leases chains, but there will still remain an issue of competing priority.

Lease/sub-lease chains

8.19 The lease/sub-lease chains has been the subject of considerable controversy, particularly when a sub-lessee becomes insolvent and s 267 operates. As identified in the Review the leasing industry is adversely impacted by the way in which the PPSA operates. Equipment may also be made available to other companies in a group.

8.20 The submissions provided by the Law Council of Australia at paragraph 4 provide examples of the sub-leasing and chains of security interests.[48] Where an owner of goods (SP1) leases the goods to a lessee (SP2) who in turn leases them to a sub-lessee (G), the head lease and the sub-lease are both PPS leases. The sub-lease, however, is not perfected. If G is a corporation and goes into liquidation then by operation of s 267 and the "take free

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[46] Chapter 8.7.4.2 and 8.7.4.3.
[47] Chapter 4.3.5.3.2 and 4.3.5.3.3.
[48] Which are published in the Review Website at: http://www.ag.gov.au/Consultations/Documents/PPSAReviewSubmissionsRound2/052LawCouncilofAustralia.pdf.

rules" the widely held view is that the security interest in the goods of SP2 will vest in the grantor, being the company in liquidation.[49] If there is with respect to G another security holder that also has security in respect of such goods, such as an "ALLPAP" registration, then it will defeat SP2.[50] The head lessor will lose its security interest. SP1 will be in no better position than SP2.[51]

8.21 The Review identified that the opinions expressed in the submissions were split in the way in which this issue ought to be treated in the context of s 267.

8.22 On the one hand it was argued that a secured party's security interest ought not to be exposed to loss because of an insolvency of a lessee.

8.23 On the other hand, it was argued that a secured party's security interest could be no greater than the interest of the lessor and if the lessor's security interest under the lease was unperfected and so vested in the lessee on the lessee's insolvency, then the security interest held by the lessor's secured party does too. Expressed in another way, the secured party only has security over the lessor's interest in the goods and if that interest vests by operation of s 267 then there is nothing left for the secured party's security interest to be attached to.[52]

8.24 The Review agreed with the latter argument.

8.25 It is recommended that the Government allow interested stakeholders an opportunity to provide further input on this issue.[53] This recommendation should be read in the context of the recommendation of the Review regarding s 267 generally as to PPS leases.[54]

8.26 It is also recommended that the Act not be amended to provide that a registration against one member of a corporate group is sufficient to perfect a security interest that is granted against another member.[55]

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49 As to the "take free rules" see s 46.
50 Priority rules: s 55(3).
51 SP1's security interest will not reattach in the leased asset unless SP2 is able to recover possession of the leased asset (s 37) prior to G's insolvency or enforcement, SP2.
52 Chapter 7.3.2.
53 Chapters 7.3.2.2 and 7.3.2.3.
54 Chapter 8.7.4 and as referred to above.
55 Chapter 7.3.3.3.

9. RECOMMENDATIONS WHICH IMPACT ON INSOLVENCY ADMINISTRATIONS

9.1 A number of provisions of the PPSA and the Corporations Act interact with insolvency administrations.

Sections 267 and 267A[56]

9.2 These provisions have a significant adverse impact for those secured parties of security interests which have not been perfected.

9.3 Two issues arose for consideration firstly, whether the provisions ought to be retained and secondly, whether the term "vest in the grantor" should be retained.

Notional Vesting

9.4 By ss 267 and 267A, subject to the exceptions in s 268, an unperfected security interest notionally vests in the grantor immediately before the occurrence of an insolvency event described in ss 267(1) and 267A(1).

10. There is no equivalent provision in the New Zealand PPSA.

11. A like, but not identical, provision is found in the in the Saskatchewan and Ontario PPS legislation.

12. The Saskatchewan PPSA (s 20(2)) provides:

> *"(2) A security interest in collateral is not effective against:*
> *(a) a trustee in bankruptcy if the security interest is unperfected at the date of bankruptcy; or*
> *(b) a liquidator appointed pursuant to the Winding-up Act (Canada) if the security interest is unperfected on the day that the winding-up order is made."*

13. The Ontario PPSA (s 20(1)(b)) provides that an unperfected security interest:

56 Chapter 8.7.

> "*in collateral is not effective against a person who represents the creditors of the debtor, including an assignee for the benefit of creditors and a trustee in bankruptcy;*"

14. The Supreme Court of Canada in *Re Giffen* [1998] 1 SCR 91 described the operation of the Saskatchewan legislation as follows:

> *"[42] … the purpose of s 20(b)(i) is, at least in part, to permit the unsecured creditors to maintain, through the person of the trustee, the same status vis-à-vis secured creditors who have not perfected their security interests which they enjoyed prior to the bankruptcy of the debtor.*
>
> *[44] Section 20(b)(i) does not grant title or any other proprietary interest to the trustee, but it prevents the lessor from exercising rights against the trustee. Admittedly, the effect of s. 20(b)(i), on the present facts, is that the trustee ends up with full rights to the car when the bankrupt had only a right of use and possession.*"

15. The rationale given in *Re Giffen* was subsequently elaborated further upon by the Ontario Court of Appeal in *In The Matter Of The Bankruptcy Og 1231640 Ontario Inc.* (formerly known as The State Group Limited) 2007 ONCA 810, 37 C.B.R. (5th) 185 at [68]:

> "*In Giffen, Re, Justice Iacobucci put the case for PPSA, s. 20(b)(i) in fairness terms: when the debtor becomes bankrupt the execution creditor loses the priority it previously had over unperfected security interests but this is offset by giving priority to the trustee instead. However, the justification can by expressed in economic terms. The thinking goes like this: Bankruptcy creates a common pool problem, which bankruptcy law addresses by substituting a mandatory system of collective debt collection for the individual first-come, first-served debt collection system that operates outside bankruptcy. Creditors' relative entitlements should be the same inside bankruptcy as they are outside bankruptcy because otherwise there will be incentives for individual creditors to use the bankruptcy laws opportunistically.*"

16. The Australian courts have distinguished the Canadian legislation from the Australian PPSA in that the latter goes further than merely rendering the security interest "ineffective" against the liquidator/trustee etc. *In Re Maiden Civil (P&E) Pty Ltd; Albarran v Queensland Excavation Services Pty Ltd* [2013] NSWSC 852 Brereton J held:

> *"[70] The first answer to this submission is provided by PPSA, s 267(2), which provides that any security interest granted by a corporation that is unperfected at the commencement of its administration or winding up vests in the corporation. This provision is analogous to, but goes further than, the Canadian statute, considered in Re Giffen, which relevantly provided (by s 20(b)(i)), that a security interest in collateral is not effective against a trustee in bankruptcy if the security interest is unperfected at the date of the bankruptcy. The Supreme Court of Canada explained that the rationale of*

the provision was to enable trustees to defeat unperfected security interests because of the representative capacity of the trustee and the effect of bankruptcy on the enforcement rights of unsecured creditors, so as to permit the unsecured creditors to maintain, through the trustee, the same status vis-à-vis secured creditors who have not perfected their security interests which they enjoyed prior to the bankruptcy.

[71] Section 267 of the Australian PPSA differs, in that, rather than merely rendering the unperfected security interest ineffective against the grantor's trustee in bankruptcy or liquidator, it vests the interest in the grantor.

[72] The consequence, in the present case, is that upon the commencement of the administration and/or winding up of Maiden, QES's unperfected security interests in the Caterpillars vested in Maiden … The practical effect is that QES's security interest is extinguished; QES has no further interest in the Caterpillars; and Maiden holds them subject only to the perfected security interest of Fast."

17. However, the following observations by Le Miere J in *White v Spiers Earthworks Pty Ltd* [2014] WASC 139 (**appeal currently pending**) are also pertinent:

"[39] Section 267(1) provides the circumstances in which the security interest held by a secured party vests in the grantor. The circumstances are where the grantor is insolvent and hence the vesting of the security interest in the grantor adjusts the competing rights of the secured party on the one hand and the unsecured creditors of the grantor on the other hand in relation to the personal property in relation to which the secured party has a security interest.

[40] PPSA s 267(2) does not effect an acquisition of property within the meaning of "acquisition of property" in s 51(xxxi) of the Constitution. The operation of s 267 to vest the defendants' interest in the Hire Assets does not result in an acquisition of property within the meaning of "acquisition of property" in s 51(xxxi) of the Constitution, and hence PPSA s 252B does not apply to the circumstances of this case. The result is that PPSA s 267(2) applies and the interests of the defendants in the Hire Assets are vested in the Company by reason of PPSA s 267 notwithstanding PPSA s 252B."

18. In the Explanatory Memorandum to the *Personal Property Securities Bill* (2009) (at [8.2], [8.5]) it was stated that:

"*These provisions would operate in conjunction with other provisions in the Corporations Act and the Bankruptcy Act 1966 which specify the circumstances in which a security interest is void as against a trustee, liquidator or administrator. For example, the Corporations Act provides that certain unregistered charges are void as against the liquidator.*

> *This outcome is not new to Australian law. The High Court in Associated Alloys v ACN 001 452 106 (Pty) Ltd (in liquidation) [2000] HCA 25 and in General Motors Acceptance Corporation Australia v Southbank Traders (Pty) Ltd [2007] HCA 19, held that a supplier could lose their security interest as a result of failing to register the interest.*"

18.1 Yet, the operation of the notional vesting in the grantor of the unperfected security interests will benefit holders of security interest who had lower priority in the collateral.

Retention of provisions

18.2 None of the submission, it was noted in the Review, suggested that ss 267 and 267A be repealed. It is recommended that the provisions be retained.[57]

Vests in grantor

18.3 The provisions provide that the unperfected security interest "vests in the grantor". It is noted that the Canadian PPSA provides that the security interest is "void" or "not effective", as referred to above.

18.4 One issue with this terminology is that if there is a security holder that has a perfected security interest, such as by an ALLPAP, over the collateral that was subject to the unperfected security interest that vested in the grantor then the other secured party will be advantaged by the operation of s 267 or s 267A and not the creditors in the liquidation.

18.5 The Review did not recommend any change as it was considered that the meaning of the language used is clear.[58]

Corporations Act and s 588FL[59]

18.6 The Review considers whether or not s 588FL ought to be repealed and if it were to be changed what amendments ought to be made to the provision.[60]

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[57] Chapters 8.7.2.1 and 8.7.2.3.
[58] Chapters 8.7.3.2 and 8.7.3.3.
[59] Chapter 9.2.2.
[60] Chapters 9.2.2. Section 588FL is the successor to s 266.

Section 588FL

18.7 The effect of s 588FL(2) is that when a company is being wound up, an administrator has been appointed or a deed of company arrangement executed, any PPSA security interest which was perfected, registered, or enforceable against a third party after the latest of six months before the critical time or 20 days after the security agreement came into force or such later time as the court may fix under s 588FM, vests in the company.

18.8 The Note to s 588FL(1) in the Corporations Act states:

> *"A security interest granted by a company in relation to which paragraph (a) applies that is unperfected at the critical time may vest in the company under section 267 or 267A of the Personal Property Securities Act 2009."*

18.9 Similarly, the Note to s 588FM(1) in the Corporations Act states:

> *"If an insolvency related event occurs in relation to a company, paragraph 588FL(2)(b) fixes a time by which a PPSA security interest granted by the company must be registered under the Personal Property Securities Act 2009, failing which the security interest may vest in the company."*

18.10 The term "may" in these two notes is potentially used to avoid any possible conflict with the operative force of the relevant PPSA provisions. Thus, if a party has not complied with s 588FL (and is further unable to obtain the benefit of an order under s 588FM), then the vesting provisions of the PPSA would arguably apply. By failing to register within the latest of the times provided by s 588FL(2)(b) of the Corporations Act, the security interest in this case vests in the company prior to the court making the s 588FM order. The difficulty with fixing the registration time pursuant to s 588FM after the interests vests is that, at the time the secured party purports to register their security interest, there is, in fact, no relevant security interest in favour of the secured party to register.

18.11 In this sense, an order pursuant to s 588FM is therefore limited to preventing the operation of s 267 (and s 267A where relevant) of the PPSA but has no effect after s 267 (and s 267A where relevant) has been enlivened.

18.12 The Explanatory Memorandum to the PPSA and to the amending legislation adding s 588FL do not address this issue.

Recommendation of Review

18.13 It is recommended that s 588FL be repealed for the following reasons:

(a) there are existing reasons under the PPSA why a security holder will want to perfect the security as early as possible;

(b) the deadline under s 588FL makes it very difficult to register effectively for some types of security interests;

(c) the provisions runs contrary to the PPSA's underlying principle, because it only applies to companies and not to all grantors.[61]

18.14 If the provision remained, it is recommended that it be amended as follows:

(a) to remove references to "deeds of company arrangement";

(b) to allow for the possibility that a security interest can be perfected by means other than registration; and

(c) so that it does not apply to deemed security interests, consistent with the exceptions prescribed in s 268 of the PPSA.

Requests for Information[62]

18.15 The underlying policy of the PPSA and the PPSR is the notification of the security interest to third parties by one of the methods of perfection. With respect to perfection by registration, the register provides notification to third parties of the claim by a security holder that it has a security interest in the classes of collateral specified in the financing statement.

18.16 There is no requirement to lodge any documents to support such claim.

18.17 Sections 275 to 283 are provisions which enable the prescribed persons to request the security agreement and other information be provided.[63] The request is to be responded to before the end of 10 days after the day the request is received.[64]

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61 Chapters 9.2.2.1.2 and 9.2.2.1.2.
62 Chapter 9.3.1.

18.18 For insolvency practitioners this process is often cumbersome and time consuming. For example there may be many security interests registered, such as for reservation of title PMSIs and security holders who do not respond to requests for information in a timely way or at all.

18.19 The Review made the following recommendations:

(a) The persons entitled to request information in s 275(9) be expanded to include a judgment creditor who is considering whether or not to enforce the judgment by seeking execution against the property described in the secured party's registration;

(b) The Government investigate whether it is sufficiently clear that company receivers and insolvency practitioners are able to make requests for information and if necessary amend the section to ensure that they are able to do so;

(c) The period in which a response is to be provided under s 277 remain at 10 days;

(d) Section 275 be amended to provided that a secured party is only required to provide that part of the security agreement relevant to ascertaining the identify of the secured party, the grantor, the identity of the collateral and the amount or obligation secured;

(e) Section 275(6)(a) be amended to read "*subject to subsection (7), the secured party has agreed with the debtor or the grantor (a* ***confidentiality agreement****) that the secured party is not obliged to respond to the request*";

(f) Section 275(7) be deleted;

(g) It is made clear that a banker's duty of confidence cannot be relied on to block a disclosure that would otherwise be required by s 275(1).

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[63] The prescribed persons are called "Interested persons" and are limited to the grantor in relation to the collateral in which the security interest is granted; a person with another security interest in that collateral; an auditor of a grantor; execution creditor; an authorised representative of the above: s 275(9).

[64] S 277.

19. CONCLUSION - THE REVIEW

19.1 The above is a sample of the matters considered by the Review.

19.2 I invite practitioners and stakeholders to take time to consider the Review. In doing so, you will obtain a greater understanding of the PPSA, the PPSR and the issues that stakeholders are encountering with the Act and register.

19.3 It is hoped that the Review results in positive legislative change to the PPSA in a timely way. This will assist in achieving the objects of the Act.

20. THE LAWYER'S ENTITLMENT TO HAVE COSTS PAID OUT OF A MONETARY JUDGMENT OR AWARD

<u>The nature of the right</u>

20.1 Jordan CJ in *Ex parte Patience; Makinson v Minister*[65] described the lawyer's (solicitor's) right as being one to have his or her costs paid out of the money obtained from a judgment or award or compromise, which is analogous to the right created by an equitable assignment of a corresponding part of the money by the client to the solicitor. The solicitor has an equitable right to be paid his or her costs out of the money.

20.2 Set out below is a number of principles extracted from *Firth v Centrelink*[66] with respect to the solicitor's rights over money recovered:

(a) The solicitor's right exists over money recovered through obtaining judgment in litigation, and also over money recovered through the settlement of litigation;

(b) The solicitor's right exists over both the amount of a judgment in favour of the client, and the amount of an order for costs in favour of the client;

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[65] (1940) 40 SR (NSW) 96 at 100. The decision of *Ex parte Patience* has been considered a decision of strong intermediate Court of Appeal, and one which should be followed. It indicates that the lien is more than a personal right of the solicitor to approach the court to obtain a charging order, the lien arises when the judgment is obtained and the assistance of the court is not invoked to create the rights but to enforce them: *Worrell v Power & Power* (1993) 46 FCR 214 at 224 (Full Court)

[66] (2002) NSWSC 564 at [35], [36], [38], [39] & [41] (per Campbell J). Also, some principles are referred to by Fogarty J as a member of the Full Court of the Family Court in *Re Twigg and Keady* (1996) 21 Fam LR 82 at 83 to 84

(c) It exists over money which is in the possession of the solicitor, and also over money which is in court;

(d) The solicitor need not be still acting for the client at the time that the money was recovered;

(e) For the right to arise it must be shown that there is a sufficient causal link between the solicitor's exertions and the recovery of the fund of money;

(f) The quantum of money for which the solicitor has the equitable right is the amount which is properly owed to the solicitor by the client, whether that amount is to be ascertained by taxation, or assessment, or pursuant to a costs agreement. In relation to those situations where taxation is necessary to ascertain the quantum owing to the solicitor, the solicitor's right exists in the fund prior to the occurrence of the taxation;

(g) The solicitor's equitable right exists before the court is asked to intervene to protect it; it arises immediately upon the recovery of monies through the exertions of the solicitor. If the lien is over the proceeds of a settlement, it arises when the settlement agreement is entered into. (These statements concern when the lien comes into existence as an item of present property — they are not concerned with the ability of the solicitor to deal with the rights under the lien as future property before the fund is in existence);

(h) The right of the solicitor is one which the solicitor can enforce against the client, entitling the solicitor to an injunction to prevent the payment of the fund to the client without notice to the solicitor until such time as the quantum of the solicitor's entitlement to be paid from the fund is ascertained. If the quantum of the solicitor's entitlement has been ascertained, the solicitor is entitled to an order that the amount of his entitlement be paid to him from the fund, notwithstanding opposition from the client;

(i) The right can also be enforced against people other than the client, in certain circumstances. When the money recovered takes the form of a debt owed to the client, which has been assigned, the right of the solicitor will prevail over the rights of an assignee of the debt, save where the assignee is a bona fide purchaser for value without notice;

(j) If the client is a company which goes into liquidation, the solicitor is entitled, in relation to costs arising from work done before the start of the liquidation, to claim the full amount of the costs from the fund, and is not required to prove in the liquidation. This has the same practical effect as enforcing the right against the other creditors of the company. The solicitor's lien attaches to property recovered through his exertions, ***even if the actual recovery occurs after the client goes into liquidation***;

(k) Likewise if the client is a natural person who becomes bankrupt, the solicitor is not required to prove in the bankruptcy for the amount of costs incurred, but can recover the costs from the debt which is the result of his efforts. The trustee in bankruptcy takes that debt subject to the equitable right of the solicitor to be paid his costs, and if the amount of the solicitor's costs exceeds the value of the debt, the debt does not vest in the trustee in bankruptcy at all;

(l) If the client is discharged from bankruptcy he can sue to enforce the debt as it never was property divisible among the creditors, and any amount that the client then receives is also subject to the solicitor's lien;

(m) If the client is the liquidator of a company in liquidation, the solicitor's lien over property recovered through his exertions is to be satisfied before the statutory order of priorities for distribution of the property of the corporation comes into effect;

(n) If the money recovered is held in the solicitor's trust account, and the solicitor is served with a garnishee notice, issued to enforce a debt which the client owes to another person, the garnishee notice is not effective to attach the money in the trust account, to the extent that the solicitor has a lien over it. Likewise if the money recovered is held by a third party, and a garnishee notice is served on that third party, the solicitor's lien prevails over the garnishee notice.

20.3 There is an inconsistency in the authorities as to whether the 'solicitor's lien' creates a proprietary right in the fund generated by the solicitor's efforts.[67] Campbell J was of the view that the equitable right which a solicitor has is a kind of proprietary interest in the fund. The

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67 For example in *Re Twigg and Keady* at 113 line 4, Kay J did not accept that the authorities referred to demonstrate that the equitable right acquired is in the nature of a proprietary right.

fact that the right of the solicitor can survive an insolvency administration of the client and is assignable is, His Honour said, strong indicia of it being a right of a proprietary nature.[68]

20.4 Also, in *Kelso v McCulloch*[69] (**Kelso**) Young CJ (as he then was) held that equity will not only enforce the fruits of the 'judgment lien' in favour of a solicitor who was on the record at the time of the judgment, but any solicitor who played at least a significant part in the conduct of the litigation which led to the verdict being recovered.[70] His Honour equated the holder of a 'judgment lien' as the holder of an equitable security and a 'secured creditor' within the meaning of s 90 of the *Bankruptcy Act 1966* (Cth).

20.5 The facts of Kelso are pertinent.

20.6 Mr Kelso, a solicitor, acted for Ms McCulloch in respect of two matters being Family Court proceedings and a claim for damages for personal injuries. Also, a litigation account was opened up with a bank which Mr Kelso guaranteed. That account was used to meet the costs and expenses of the litigation.

20.7 In February of 1993 Ms McCulloch provided in favour of Mr Kelso an irrevocable authority which provided in part as follows:

> "*IRREVOCABLE AUTHORITY I, Lynette Therese McCulloch, acknowledge that my solicitors, Kelso and Associates, have acted on my behalf in my family law matters on the basis that their reasonable scale costs and disbursements (including barrister's fees) are paid out of the proceeds of my common law Supreme Court injury claim against Cessnock District Hospital. I hereby irrevocably authorise my solicitors to deduct their reasonable scale costs and disbursements (including barrister's fees) out of my aforementioned injury claim. DATED: 18/2/93 LYNETTE THERESE McCULLOCH.*"

20.8 In April 1993 Ms McCulloch wrote to Mr Kelso saying she no longer wished him to act for her in the personal injuries claim and she instructed another law firm. The Family Court proceedings were settled in September 1993 and Mr Kelso's fees were certified by the court in the amount of $26,137.18.

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68 At [38] to [42]
69 (NSWSC 24 October 1994 unreported).
70 Applied in *Re Twigg and Keady* at 112.8 (per Kay J). Also, it was said that once notice of a solicitor's right to payment is given to the judgment debtor only the solicitor giving the notice can give discharge to the judgment debtor for an amount of money equivalent to the solicitor's costs. If payment is made in disregard of the notice, the judgment debtor or his or her solicitor becomes liable to the solicitor giving the notice and must pay again.

20.9 In October 1993 Ms McCulloch presented her own debtor's petition and a sequestration order was made against her estate.

20.10 The common law proceeding for the personal injuries was not finalised until August 1994 when an amount in excess of $45,000 was recovered.

20.11 Mr Kelso's claim was for three debts: firstly, the amount of the Family Law costs; secondly, the costs of the personal injury or common law claim; and thirdly, the pay-out figure of the litigation account.

20.12 His Honour found that the 'Irrevocable Authority' was properly categorised as an agreement to assign part of a fund when that fund comes into existence. However, to be effective it must be supported by consideration. It will then operate as an agreement to assign property when it is acquired and the agreement will be binding from its date, and binding on the property in equity if and when acquired by the assignor. On the facts of the case the 'Irrevocable Authority' referred to agreement for Mr Kelso to act in the Family Court proceeding and His Honour said that Mr Kelso had given consideration for the agreement and done everything that he was bound to do.

20.13 His Honour concluded that by operation of the principle in equity when the money falls in the amount needed to pay the Family Law fees it is held on trust by Ms McCulloch for the solicitor. It does not matter that the client has become bankrupt as the proceeds of the personal injury claim are not "property of the bankrupt" which vests in the trustee in bankruptcy and is available to creditors and the solicitor was entitled to the Family Law costs from the fund.

20.14 *Kison v Papasian*[71] held that a solicitor had a right to be paid the costs from an order for costs made in favour of the client after the bankruptcy of the client with respect to work undertaken by the solicitor before bankruptcy. The court said that an equitable estate exists in respect to the proceeds of the order and that the trustee in bankruptcy could only take the benefit of the order (as after acquired property) subject to the solicitor's equitable interest, which arises by operation of law.[72]

Competing claims

20.15 As Jordan CJ said in *Ex parte Patience; Makinson v Minister* the right is to have the costs paid out of the money obtained from a judgment or award or compromise. This right is

[71] (1994) 61 SASR 567.
[72] At 569.5, 576.5 (per King CJ and Mullighan J).

analogous to the right created by an equitable assignment of a corresponding part of the money by the client to the solicitor. This is an equitable right.

20.16 There is a dichotomy in the decisions in the Chancery Division and New Zealand as to priority between competing claims by consecutive solicitors acting in the matter.

20.17 In *Atkinson v Pengelly*[73] Tipping J determined that where there are competing claims for costs by different solicitors against a fund recovered by the joint or successive services of each of them the prima facie position is that the solicitors ought to share in the fund *pari passu*, if there are insufficient funds to satisfy them both. The prima facie position may be disturbed if in all the circumstances of the case equity demands that course. His Honour said that this would produce reasonable certainty. To depart from this position it was noted that there must be sufficient compelling circumstances such as the reason why the first solicitor ceased to act or the new solicitor has become involved as a matter of urgency or out of necessity. Also, the fact that the incoming solicitor may have poached the client from the first solicitor may be a factor.

20.18 Tipping J saw little justice in giving priority to the solicitor who brought the claim to a final solution where the successive solicitors have each contributed to the ultimate recovery and a solicitor taking over a matter from another solicitor subject to an agreement between them be required to recognise the previous solicitor ought to have a proper interest in the fruits of the litigation. In noting that the rights are conventionally described as common law rights, rather than rights in equity, there is force in the approach in the maxim equity favours equality (a *pari passu* approach).[74]

20.19 With respect to the "lien" this has been described in the Australian authorities as arising in equity.[75]

20.20 The position in the Chancery Division is that the solicitor who conducts the litigation to the conclusion has the first 'lien' upon any money recovered or preserved: but subject to this lien,

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73 [1995] 3 NZLR 104.

74 Page 108 line 54 to 109 line 18.

75 As referred to by Jordan CJ and also see discussion in *AMC Commercial Cleaning (NSW) Pty Ltd v Coade* [2013] NSWSC 192 at [24] to [27]; Keane JA (with whom Muir JA and Mullins J agreed) referred to the lien as an "equitable lien over the fruits of the litigation" citing the decision of Jordan CJ in *Ex parte Patience; Makinson v Minister*.

the court will grant a solicitor employed at an early stage a charging order in respect of the costs.[76]

20.21 The approach which is more likely to receive acceptance is that of *Atkinson v Pengelly* in the context that rationale for the existence of the 'lien' over a fund recovered through the efforts of a solicitor is that, if the solicitor had not done the work and spent the money, there would not be any fund in existence.[77]

20.22 Also, the efforts of both firms have contributed to work that enabled the fund to come into existence; the entitlements by way of the 'lien' of both firms arose upon the recovery of monies and there is no clear basis for distribution of the proceeds as the sum recovered is insufficient to pay both firms.

20.23 If the Irrevocable Authority is properly categorised as an agreement to assign part of a fund when that fund comes into existence it will then operate as an agreement to assign property when it is acquired and the agreement will be binding from its date, and binding on the property in equity if and when acquired by the assignor.

20.24 However, the property acquired by the assignor (the Client) is subject to the rights of the solicitors under the 'lien' which arises by operation of law. Upon the reasoning of Campbell J in *Firth v Centrelink* by the entitlement to a 'lien' a solicitor has a proprietary right in the fund. Therefore, the fund in the hands of the assignor capable of being assigned is that subject to the 'lien'.

20.25 A suggestion that an agreement to assign future property entitles the assignee to the fruits of the litigation without having to pay the solicitor's costs associated with obtaining it would be inconsistent with the rationale underlying the solicitor's 'lien'.[78]

<u>Impact of PPSA</u>

20.26 Section 8(1) of the PPSA exempts a lien or charge, or other interest in property, that is created, arises by or is provided for by operation of the general law. By ss 8(2) and 73(2),

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[76] As discussed in *Atkinson v Pengelly* at p 106 line 35 to 107 line 50; *Halvanon Insurance Co Ltd V Central Reinsurance Corp* [1983] 3 ALL ER 857 at 863d.

[77] *Firth v Centrelink* at [48].

[78] This analysis would also apply if the Irrevocable Authority was to be treated as an agreement to charge in favour of MacGillivrays the proceeds. The creation of a valid equitable charge is discussed in *Australian Receivables Ltd v Tekitu Pty Ltd* (2012) 260 FLR 243 at [97] to [109].

(7) and (8) the Act may, however, regulate priorities with that interest and other security interests.

Example

20.27 The facts:

(a) Claim for personal injury of client commenced by lawyer A on a speculative basis

(b) Client moves to a lawyer B who takes over the action on a speculative basis and takes matter to trial

(c) Client and lawyer A enter into agreement which in substances charges the fruits of the litigation

(d) No agreement between lawyer A and lawyer B

(e) Client goes bankrupt before matter proceeds to trial

(f) Judgment sum is insufficient to pay all of legal costs of A and B

(g) Solicitor's lien (equitable right to be paid costs out of the proceeds of litigation and exists over money recovered through obtaining judgment).

20.28 Personal injury action and proceeds do not vest in trustee (ss 5, 58 and 116 BA).

20.29 What is the effect of the bankruptcy on the claims of the lawyers as creditors of bankrupt?

20.30 Is the charge a security interest required to be registered? What about the liens? Does s 267 PPSA apply and if so how?

20.31 How do you determine priority? Which lawyer has priority?

20.32 This question will be discussed at the conference. The scenario may also equally apply to any piece of litigation.

Disclaimer: This paper covers legal and technical issues in a general way. It is not designed to express opinions on specific cases. This paper is intended for information purposes only and should not be regarded as legal advice. Further advice should be obtained before taking action on any issue dealt with in this paper.

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LEVEL

TWENTY SEVEN

CHAMBERS

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