ppsanews

kreissonlegal

"Perfect it or lose it"

Impact of PPSA on the Construction and related industries

February 2012

The new Personal Property Securities Act 2009 (Cth) (PPSA) which commenced on 30 January 2012 will have a significant impact on the construction and related industries.

What is it all about?

Generally, the PPSA is expected to improve the ability for businesses to use personal property as security to obtain finance.

The reform is radical and overturns basic property law concepts by introducing a completely new understanding of how security interests in personal property can be protected.

Although parts of the PPSA are relatively simple to understand, there are other parts which are complex/technical and uncertain.

What is clear however, is that the changes introduced by the reform will benefit those businesses who understand how the PPSA will work.

Those businesses that do not take steps to understand and use the PPSA may find that their interests in personal property are lost to third parties.

What are the key features?

In brief, the PPSA:

- applies to all kinds of personal property with limited exceptions;
- creates a security interest in transactions involving personal property even in some cases where the transaction does not secure payment or performance of an obligation;
- requires "perfection" of the security to ensure that the security interest has priority over other security interests;
- provides that perfection is achieved either by possession or control of the property or by registration on the online PPS Register;
- replaces the registration of company charges in ASIC with the PPS Register;
- establishes default rules for the creation, priority and enforcement of security interests in personal property;
- provides that a failure to register an interest on the PPS Register could lead to a loss of priority of the interest;
- creates a new category of security interest known as purchase money security interests (PMSIs) which is given a "super priority";

- includes rules for transition or migration of security interests that existed prior to the PPSA;
- requires minimal and consistent formal requirements for security agreements.

What is a security interest?

Under the PPSA, a security interest is defined widely and includes any personal property other than land and certain statutory rights.

A security interest will arise when a right in personal property is provided in a transaction that secures payment or performance of an obligation.

The PPSA also deems certain arrangements to be security interests even if they do not secure payment or performance.

In working out whether an arrangement establishes a security interest, the PPSA has adopted a functional approach.

This means that the PPSA will be more concerned about the effect of the transaction rather than the form of the transaction which was the case of the previous law.

As result transactions that were not previously considered to be security interests will now be caught by the PPSA.

Ownership is no longer king

One of the key shifts under the PSA is that title or ownership in personal property will no longer be enough to protect an owner on the insolvency of the provider of the security (the grantor) or against third parties

Before the PPSA, the law focused on title and ownership to establish property rights and interests.

This is no longer the case under the PPSA.

Instead the PPSA relies on the new concepts of attachment, enforceability and perfection to protect interests in personal property

Under the PPSA therefore, if a security interest has been "perfected" by the true owner or holder of the title; the PPSA will treat the grantor of the security as the owner of the property and a creditor (i.e. true owner or holder of the title) as a secured party.

Therefore in an insolvency **unless** security interests in assets have been "perfected" under the PPSA, those assets can be sold by a liquidator without regard to the interests of the true owner or holder of the title in those assets.

Registration

Under the PPSA all security interests have to be "perfected" in order to survive the insolvency of a grantor and to preserve priority against competing interests in the same property that may be held by others.

Perfection a technical term and can be achieved in different ways under the PPSA.

The safest course to perfecting a security interest and preserving priority is by registering the security interest on the PPS Register.

The Register is wholly electronic and subject to maintenance requirements is accessible 24/7.

The purpose of the Register is to provide a single notice board notification of information for consumers, business and the finance industry as to whether a security interest is registered against personal property.

Transitional provisions

The PPSA provides a 24 month transitional period to any security interest that existed prior to 30 January 2012 to register pre PPSA security interests (ie transitional security interest).

During the transitional period the PPSA deems the transitional security interest to be perfected.

If the pre PPSA security interest is not registered by the end of that period, the security interest becomes an unperfected security.

There are specific priority rules that apply to transitional security interests.

How will the PPSA affect the construction industry?

The impact of the PPSA on the construction industry will potentially be significant.

Some of the key areas where the PPS may apply include the following:

Temporary works

The PPSA applies to contracts that involve leasing or the right to use and dispose of equipment.

These types of contracts may include the provision of temporary works, for example scaffolding temporary power boards, site sheds, formwork and other equipment hired from specialist providers.

This type of equipment remains on a building site but which does not form part of the works and will be removed by the owners once the works are complete.

In each of these cases, legal title to the equipment is not enough to protect the interests of the owner.

Under the PPSA, the owner would need to register their interest to perfect the security so as to then protect their title in the equipment.

If they do not register their interest the owner may lose the goods to a liquidator or third party.

Retention of Title

The PPSA applies to agreements to sell goods and which are the subject of Retention of Title clause.

Retention of title clauses are standard in most supply contracts and generally provide that ownership in the goods does not pass until payment has been received for those goods.

Under the PPSA retention of title clauses now need to be registered. Unless the agreements are registered the interests of the supplier in the goods may be lost on the insolvency of the purchaser.

Tripartite Deeds

Tripartite or side deeds entered into by a Developer/borrower, Builder and financier and which give the financier step-in rights may constitute a security interest under the PPSA.

This is because in Tripartite Deeds a financier generally seeks security over the contractual rights of the borrower and will in the case of a default by the borrower “step in” to the borrower’s shoes and act as principal to complete the project.

Principal’s step in rights

In some construction contracts a principal is entitled on the substantial breach of the Contractor to take the works out of the hands of a contractor in the event of a substantial breach and then step in and complete the works and then sell contractor's plant and equipment to recover losses resulting from the breach.

It is possible that these take out and step in rights may constitute security interests for the purposes of the PPSA which may need to be registered.

Retention monies

It is also possible that monies held on retention create a security interest in favour of a Principal and need to be registered by a Principal.

As is well known, the purpose of retention is to provide a security interest in favour of the Principal for the performance of the contractor's obligations under the Contract.

Depending on the terms of the contract, a principal's rights to retention may constitute a security interest and may need to be registered to protect the principal's right to the retention monies.

Joint ventures

Another area of possible application of the PPSA is in relation to joint venture agreements where security interests are created under a cross charges or clause.

In particular a security interest may arise if the joint venture agreement provides for a dilution to a defaulting party's interests to the benefit of a non-defaulting party.

Any other clauses used to protect joint venture partners from the insolvency or default of a joint venture partners may be also caught by the PPSA and require registration.

What should you do?

Given the broad effect of the legislation and impact on the way you do business particularly in the construction industry, we recommend that you:

(a) **Review** your existing contracts to determine whether they create a security interest and what steps your business needs to take to perfect those security interests;

(b) **Identify** what interests in goods and services can and should be registered;

(c) **Understand** the transitional arrangements;

(d) **Review** existing transactions to make sure that you register security interests within the 2 year transitional period;

(e) **Consider** what systems and processes you need to establish to effectively manage registration and your security interests;

(f) **Use** PPSA language in your documents;

(g) **Make sure** you know who you are contracting with and obtain all relevant information to enable a valid PPSA registration;

(h) **Ensure** that there is a person in your organisation who understands how PPS works and who can answer questions from other staff;

(i) **Educate** your staff on how to register security interests and search the PPSR.

How we can help?

We can assist your business by providing:

(a) **Advice** on any PPSA priority rules including migrated and transitional security interests, extinguishment rules and enforcement provisions;

(b) **Assistance** on how to complete and register a financing statement to perfect the relevant security interest;

(c) **A Review** of and suggest changes to your contracts and standard terms of trade;

(d) **Training** and education to your staff to help your team understand the parts of the PPSA relevant to your business.

If you would like our PPSA briefing which provides additional details of the legislation or any further information please contact David Glinatsis Solicitor Kreisson Legal phone (02) 8239 6500 or email at david.glinatsis@kreissonlegal.com.au