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When possession is no longer nine-tenths of the law – how to protect your property interests and survive under the new PPS regime

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Picture this: You are in the transport business and either transport and store goods for your customers, or arrange for others to provide those services. As the economy heads towards a double dip recession, credit dries up and consumers vanish from the shopping centres, you have a customer who imports goods and is taking longer to pay your bills. If this is not bad enough, your service providers and suppliers are also asking you to pay their bills and at the same time, you still have to pay your rent and your staff - they have to feed their families too. Soon, you find yourself spending more time on the telephone with your customer chasing those outstanding bills rather than doing business with them. Polite reminders are met with promises to pay but come to nothing. As your exposure to that customer increases with services continuing, your polite reminders evolve into begging, only to be met with a more truthful response-your customer is in trouble and can only pay on the drip feed, otherwise you will not get paid at all. Your begging soon evolves into threats and you then cross that line - you decide that the customer is treating you as a line of credit and it is now time to take drastic action to get paid. As it happens, you are storing some of that customer's goods or are expecting them to arrive at port next week. It will be very tempting to hold onto the customers goods or documents until they pay the outstanding debts (i.e. you exercise a *lien* over those goods or documents) and eventually sell the goods to pay off the debts if the customer does not come to the party.

Rest assured, if you hold onto the goods and documents that the customer needs for their business until the outstanding debts are paid, you will have their undivided attention, but if you do not have the right to exercise the lien, you could be sued by the customer for any losses that they suffer by your wrongful detention of the goods, so you need to know your rights over the goods and also the rights of other parties who inevitably hear that you have the goods and claim that they have a better right than you over the goods. The game will change when the Personal Property Securities Act 2009 (PPSA) comes into force (now scheduled to commence on 30 January 2012, unless the time for commencement is extended under the PPSA), so you will need to be aware of both regimes and may need to change your practices to protect your interests under the new regime.

Currently, you can retain possession of goods or documents for services that relate to the unpaid invoices (a particular lien) and if your contract with the customer permits you to do so, you can also retain possession of all the customer's other goods or documents which are not the subject of the unpaid invoice or invoices (a general lien). Depending on the circumstances, you may eventually sell the goods to settle the debt or have to compete with other parties for the goods or proceeds of sale, including the supplier of the goods and/or the administrator or receiver of the customer.

Your right to exercise a lien will soon fall within the boundaries of the PPSA which is a law concerning security interests in all property other than land owned by companies or individuals. A lien is a *security interest* for the purposes of the PPSA because it secures payment of debt owed.

The PPSA will not apply to particular liens which will take priority over any other security interest in the goods or documents the subject of the lien. This means that you will have the first right to payment out of the proceeds of the sale of the goods in order to discharge the debt owed in respect of goods that relate specifically to the customer's unpaid invoices. However, the PPSA affects your right to exercise a general lien against the customer and third parties – you will need to comply with the requirements of attachment and perfection under the PPSA and carry out certain steps before you exercise the general lien.

Creating a general lien that is enforceable against the customer - attachment

The PPSA provides that if the general lien is to be enforceable against the customer, it must have "attached" to the goods or documents in question.

Attachment occurs when you enter into a contract for the carriage or storage of goods which includes a general lien clause. However, attachment will not occur unless the customer:

- has rights in the goods or documents, or the power to transfer rights in the goods or documents at the time the security interest is obtained, or
- will acquire rights in the goods (under the contract of sale) prior to a time that you wish to enforce the general lien.

For practical purposes, the requirement under the PPSA to "attach" the general lien to the goods or documents, vis-à-vis the customer, is no different to the existing law where you need to have a contractual right (the general lien clause) and the customer has to have some right to the goods in order to retain possession of goods that do not relate to the unpaid invoices. The PPSA comes into its own, however, when the third party claimants come out of the woodwork and want to take those goods.

Creating a general lien that is enforceable against third parties

If you want to enforce the general lien against a third party who may have an interest in the goods, the general lien must have "attached" to goods as detailed above, AND one of the following must occur:

- you possess the goods; or
- you have a "security agreement" with the customer in a form recognised by the PPSA. That is, a written document for every consignment carried or stored which provides that a general lien can be exercised over the specific goods.

Perfection

In addition to attachment, for a general lien to be enforceable against the customer and third party under the PPSA, "perfection" is required.

Perfection occurs if:

- the general lien is "temporarily perfected" by the PPSA, or
- ALL of the following apply:
  - » the general lien has attached to the goods as described above
  - » the general lien is enforceable against the third party as described above, and
  - » either a registration of the general lien in the (new) PPS Register is effective with respect to the goods, or you have possession of the goods over which you are exercising the general lien.

Perfection allows a general lien to take priority over other unperfected security interests in the goods at the time of enforcement. Without perfection of your general lien, you will not be able to enforce your general lien to protect your interests against the customer's winding up, entry into administration, or bankruptcy, and the goods will be available to all creditors.

For carriers and freight forwarders, the most practical means of perfecting their general lien will be through possession rather than registration. Registration will be a time intensive and expensive process and will not necessarily provide for higher priority of the general lien clause in the event of conflict between competing interests over the same goods. This is because the PPSA provides that "Purchase Money Security Interests" (or PMSIs), which include the interest of a bank funding the purchase of the goods in question, or a seller's retention of title clause, will ALWAYS have a super priority over other security interests, even if those other security interests are registered at an earlier point in time.

Enforcement

Okay, so your general lien satisfies the PPSA rules for attachment, and have perfected your general lien by obtaining possession of the goods. The PPSA requires you seize the customer's goods by giving notice to the customer that you are exercising the lien. As with the current regime, you can expect a robust exchange with the customer and their lawyers.

Following seizure of the goods, you will be able to dispose the goods to satisfy any debt owing from the customer by:

- selling the goods to a third party, or
- purchasing the goods.

Extinguishment of the Security Interest

If goods are sold during the course of transit by the customer then the right to exercise a general lien will be lost and you will not be able to exercise a general lien against the purchaser.

Priority among competing security interests

The new regime will be quite different when other competing parties show up and claim a right to the goods. The PPSA establishes rules for determining priority among competing security interests in the same goods. The priority rules are as follows:

priority between unperfected security interests in the same goods is determined by the order of attachment of the security interest; and

a perfected security interest in collateral has priority over unperfected security interest.

Accordingly, if you want to ensure that your general lien will take priority over other security interests in the same goods, then you will need to ensure that the security interest provided by the general lien is perfected at the earliest possible time. This is because an earlier perfected security interest will take priority over a later perfected security interest, as well as a non perfected security interest.

As discussed above, the PPSA establishes special priority rules for purchase money security interests (PMSIs) such as a seller's retention of title clause in a contract for the sale of goods. All of these security interests will take priority over a carrier's or freight forwarder's general lien. It is unlikely that you will hold any super priority security interest if you provide freight forwarding services and do not sell goods. For this reason, possession as a means of perfecting a security interest, rather than registration, will be the most practical means of ensuring perfection at the earliest possible time.

The PPS Register and the registration process

If you wish to perfect your security interest by registration, you will lodge a "financing statement" with the single national register set up under the PPSA for the registration of all security interests in personal property, regardless of the form of the security interest, the legal personality of the grantor, or the nature of the goods. A fee must be paid for this lodgement. This financing statement will detail the grantor of the security interest (the customer), the party who has the benefit of the security interest (the carrier/freight forwarder), the collateral the subject of the security interest (goods), and how long the security interest will last. However, as discussed above, it is unlikely to be practical for carriers or freight forwarders to register their security interests.

Carrying goods between two countries - will the PPSA apply?

In the context of the international carriage of goods, the PPSA deals with perfection differently than for domestic carriage. It does so by providing for "temporary perfection" which can occur before you possess the goods. Temporary perfection is important if you are based in Australia and are acting as agent for a principal carrier or freight forwarder (often a related entity) overseas.

For temporary perfection to apply:

the general lien over the goods must have been either perfected, registered, or be effective against third parties under the law of the overseas jurisdiction; and

the choice of law rules in the PPSA must apply to make the PPSA govern the enforcement of the general lien in Australia. These rules provide that the PPSA will apply where the goods are transferred or carried to Australia, or the customer who provides a carrier or freight forwarder with the right to exercise a general lien is located out of Australia but transfers goods to a person located in Australia.

Temporary perfection occurs when a bailee possesses the goods on behalf of the carrier or freight forwarder pursuant to a bill of lading relating to the carriage of goods either to or from Australia.

Temporary perfection will not apply when a carrier or freight forwarder has physical possession of the goods. It only applies where the carrier or freight forwarder has subcontracted the carriage to another carrier or freight forwarder who then issues to the carrier or freight forwarder a document of title, negotiable or not, for the goods that are covered by the general lien.

Once the goods leave the possession of an ocean carrier who has issued an ocean bill of lading for the goods to an Australia based carrier or freight forwarder, the temporary perfection of the general lien during the carriage would have ended. The carrier or freight forwarder will then have to perfect its general lien by either possession or registration if they want to be able to enforce the general lien against a third party.

Temporary perfections will be extinguished if a buyer purchases the goods or negotiable document of title.

Interaction of the PPSA with insolvency

An unperfected general lien will not be enforceable in the insolvency process and is void against a liquidator or bankruptcy trustee. The goods the subject of the lien will become part of the pool of assets available to the liquidator or bankruptcy trustee to deal with under the insolvency process. Accordingly, you would only be able to recover in the liquidation as an unsecured creditor despite the right to exercise a general lien. However, if your general lien has been perfected, it will be enforceable in the insolvency. In that event, the priority rules operating under the PPSA will apply in the insolvency process to determine the order of distribution between the competing secured parties.

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