McKEAN PARK LAWYERS

MATTERS

MARCH 2010

PERSONAL PROPERTY SECURITIES LAWS: A CREDIT REVOLUTION

BY DERRICK TOH & TONY ROGERS

After a series of national consultations and several Senate Inquiries, the *Personal Property Securities Bill 2009* and the *Personal Property Securities (Consequential Amendments) Bill 2009* ("PPS Laws") were unceremoniously passed by the Government on the 26 November 2009 and received royal assent on 14 December 2009. The PPS Laws will commence in May 2011.

It is safe to say that the PPS Laws will represent the most significant reform to commercial lending practices in Australia seen in decades. Although it will only commence in May 2011, the rapid change in economic conditions and the scale of insolvency events evidenced today highlights the need for a comprehensive understanding of these new laws and the need to develop new business practices prior to its commencement. Depending on the type of business involved, a lengthy lead time could be required.

As most businesses these days involve providing some form of credit, you will need to be familiar with these new laws. Needless to say, those who are quickest to adapt to these reforms will gain a significant advantage over their competitors.

WHAT IS IT ABOUT?

The PPS Laws will govern security interests in personal property. Personal property is defined broadly as any property that is not real property (namely land and buildings), including tangible assets (such as motor vehicles and boats) and non-tangible assets (such as shares and leasehold interests).

WHAT IS A SECURITY INTEREST?

A security interest is an interest in personal property that is created whenever you enter into a transaction that uses personal property to secure payment or performance of an obligation.

Common situations where the PPS Laws apply include:

- **hire-purchase transactions;**
- **goods sold on your behalf by a retailer;**
- **leases of goods or equipment;**
- **goods stored in someone else's possession.**

THE PERSONAL PROPERTY SECURITIES REGISTER ("PPSR")

There will be a national public register where security interests over personal property may be registered, searched and updated. Transactions will be carried out in 'real time'.

WHY SHOULD YOU REGISTER?

Registering a financing statement records your security interest on the PPSR. A financing statement contains information about your security interest, but you will not be required to provide copies of your security agreement or detailed financial information.

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'ALSO FREE WILL REVIEW OFFER – DETAILS FOLLOW'

By registering your security interest, you will be in a better position if your debtor is made bankrupt or is put into receivership or liquidation than other creditors.

Whilst this does not guarantee you will necessarily recover the amount that is owed, it will ensure that other secured creditors' claims will not have priority over your claim in relation to that property, even where you may in fact own that property.

PRIORITY RULES

Generally speaking, a registered security interest will take priority over an unregistered security interest.

If there is more than one registered security interest the party who was first to register will normally take priority. However, the party with possession or control of the collateral property has priority over any registered and unregistered security interest.

The PPS Laws also contain special priority rules for certain categories of transactions, including margin lending arrangements, hire purchase agreements, equipment/ finance leasing, and security over crops, livestock and intellectual property.

WHY NOT RELY ON EXISTING TERMS OF AGREEMENT?

Most terms of agreements relating to the supply of goods on credit contain what are known as "retention of title" clauses, whereby title to the goods being sold is not legally transferred until the entire value of the goods being supplied is paid. Under the PPS Laws, these "retention of title" clauses will no longer be effective against third party claims. That means if you supply goods on a "retention of title" basis but have not registered a financing statement on the

PPSR, you will be an unsecured creditor if your debtor subsequently becomes bankrupt or insolvent.

Other common terms of agreement which will be affected include:

- **if you supply goods on commercial consignment without registering your security interest on the PPSR, you will be vulnerable during insolvency events. For example, if you supply hardware goods or computer accessories to a retailer on commercial consignment and fail to register a financing statement on the PPSR, you will be unsecured and unable to retrieve your goods if the retailer goes into liquidation or receivership.**
- **if you supply goods under a lease for a term of more than one year or for an indefinite term, but fail to register your security interest on the PPSR, again you will be vulnerable during insolvency events. For example, if you lease hospitality equipment to restaurants and cafes but fail to register on the PPSR, you will find your priority is deferred as against a bank taking a better (registered) security interest over the assets of the business.**

WHAT TO DO NOW?

We suggest that all businesses supplying goods on credit undertake the following:

- **Review your business practices now in light of the impending PPS Laws.**
- **Develop a procedure to implement any changes required to your business.**
- **Contact us if you are unsure about any aspect of the PPS Laws and how it could affect your business.**

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PROFILE: JIM MELLAS

Jim was admitted to practice as a barrister and solicitor in 1985. He has now been in legal practice for almost 25 years and is a Partner of McKean Park and head of our Family Law department.

Throughout his 25 years Jim has practised predominantly in Family Law having become an Accredited Specialist in Family Law in 1991. He advises clients on a range of complex matrimonial and family issues particularly as they relate to businesses. While Jim handles varied matrimonial cases his practice has a commercial focus in keeping with the McKean Park areas of practice. He advises clients on intricate financial matters involving companies, trusts and family businesses.

Family Law is an area of law that can be quite emotional and difficult. Jim has a particular interest in advising on protecting premarital assets and minimising the effect of a relationship breakdown on a family business. He also has extensive experience in parenting matters and in cases involving child support and maintenance.

In the course of his practice Jim appears regularly for clients as counsel in the Family Court of Australia and the Federal Magistrates' Court of Australia. He is also a regular speaker at legal seminars and conferences and in the past has spoken on a range of subjects from Family Law to succession planning and family business. Jim has had a number of papers published on a range of Family Law topics and will feature in a forthcoming DVD on Family Law and estate planning which is being released by the Television Education Network. In the past, Jim also had a regular legal segment on 3AW speaking on various legal matters.

Jim is a member of the Executive Committee of the Family Law section of the Law Institute of Victoria and is also a member of the Courts Practice Committee. Outside of the law, Jim is a former director and vice president of the South Melbourne Football Club and was heavily involved in the negotiations with the Victorian State Government for the $70 million redevelopment of the Lakeside Oval at Albert Park. In 2008 Jim also lead a consortium known as Southern Cross FC which was bidding for the second A League licence in Melbourne.

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MORE REASONS WHY YOU SHOULD MAKE A WILL

BY ELISABETH BENFELL & GEOFF PARK

BACKGROUND

Clients will be aware, from previous newsletters that if one dies without leaving a valid Will then the *Administration and Probate Act 1958* prescribes who will benefit from the estate. You will recall that in general the closest living relatives benefit. However you will also recall that this does not always accord with what you would want, had you thought about it carefully. For example should a husband predecease a wife, without leaving a valid Will, then the wife would receive all of the personal chattels and the first $100,000.00 in value of the estate and 1/3rd of the balance of the estate – the other 2/3rds passes to the children. Very few people who sit down and think about their situation and subsequently execute a Will would make a Will along those lines.

RECENT CHANGES

In recent years legislative changes have made it even more complicated to cover the situation where people live together but are not married and irrespective of gender. Furthermore situations where a deceased may leave a spouse but also leave one or more "domestic partners" are now covered by legislation. Example. Using the example above then consider the situation where the wife had been estranged for a few years and the husband had a domestic partner at the time of his death. The wife and domestic partner would share the benefits that the wife would otherwise take in the example above.

MORE CHANGES

Now more changes have been made from 1 December 2008, under the *Relationships Act 2008*, as outlined below. These changes affect both the *Administration and Probate Act 1958* and the *Wills Act 1997*.

The *Relationships Act 2008*, provided for the establishment of a relationships register.

A "registrable relationship" is defined to mean:

a relationship (other than a registered relationship) between two adult persons who are not married to each other but are a couple where one or each of the persons in the relationship provides personal or financial commitment and support of a domestic nature for the material benefit of the other, irrespective of their genders and whether or not they are living under the same roof, but does not include a relationship in which a person provides domestic support and personal care to the other person:

(a) for fee or reward; or

(b) on behalf of another person or an organisation (including a government or government agency, a body corporate or a charitable or benevolent organisation);

This Act amended the *Administration and Probate Act 1958* by substituting the definition of "domestic partner" in s 3(1) with:

"domestic partner" of a person who dies means a registered domestic partner or an unregistered domestic partner of that person;

and inserting new definitions as follows:

"registered domestic partner" of a person who dies means a person who, at the time of the person's death, was in a registered relationship with the person within the meaning of the *Relationships Act 2008*;

"unregistered domestic partner" of a person who dies means a person (other than a registered domestic partner of the person) who, although not married to the person

(a) was living with the person at the time of the person's death as a couple on a genuine domestic basis (irrespective of gender); or

(b) either

- **(i) had lived with the person in that manner continuously for a period of at least 2 years immediately before the person's death; or**
- **(ii) is the parent of a child of the person, being a child who was under 18 years of age at the time of the person's death.**

To determine whether persons are unregistered domestic partners, section 3(3) of the *Administration and Probate Act 1958* states that: "All the circumstances of their relationship are to be taken into account, including any one or more of the matters referred to in section 35(2) of the *Relationships Act 2008* as may be relevant in a particular case."

Section 35(2) of the RA provides:

In determining whether a domestic relationship (other than a registered relationship) exists or has existed, all the circumstances of the relationship are to be taken into account, including any one or more of the following matters as may be relevant in a particular case

(a) the degree of mutual commitment to a shared life;

(b) the duration of the relationship;

(c) the nature and extent of common residence;

(d) whether or not a sexual relationship exists;

(e) the degree of financial dependence or interdependence, and any arrangements for financial support, between the parties;

(f) the ownership, use and acquisition of property;

(g) the care and support of children;

(h) the reputation and public aspects of the relationship.

Further changes have occurred as a result of the *Relationships Amendment (Caring Relationships) Act 2009* (No 4 of 2009), which came into operation 1 December 2009. This Act introduced the concept of a registered caring relationship, which means:

"a relationship (other than a registered relationship) between two adult persons who are not a couple or married to each other and who may or may not otherwise be related by family where one or each of the persons in the relationship provides personal or financial commitment and support of a domestic nature for the material benefit of the other, whether or not they are living under the same roof, but does not include a relationship in which a person provides domestic support and personal care to the other person

(a) for fee or reward; or

(b) on behalf of another person or an organisation (including a government agency, a body corporate or a charitable or benevolent organisation);";

Where such a relationship is registered, each registered caring partner acquires rights on intestacy and has rights to a property adjustment if the relationship beaks down.

The *Relationships Act 2008* and *Relationships Amendment Act 2009* amend the intestacy provisions in the *Administration and Probate Act 1958*. Thus, s 51A(1) of the *Administration and Probate Act 1958* is changed to this:

If an intestate leaves both a spouse or registered domestic partner or registered caring partner and an unregistered domestic partner, the entitlement to the partner's share of the intestate's residuary estate is to be determined in accordance with the following table.

Period that unregistered domestic partner has lived as domestic partner of intestate continuously before intestate's death	Spouse or registered domestic partner's or registered caring partner's entitlement to partner's share	Unregistered domestic partner's entitlement to partner's share
less than 4 years	two-thirds	one-third
4 years or more but less than 5 years	half	half
5 years or more but less than 6 years	one-third	two-thirds
6 years or more	none	all

NOTE

There is a minimum requirement that the unregistered domestic partner lived with the intestate continuously for at least 2 years immediately before the intestate's death, unless such domestic partner is the parent of a child of the intestate who was under 18 at the time of the intestate's death—see definition of unregistered domestic partner in section 3(1).

The *Relationships Act 2008* also amends the Wills Act 1997 by substituting the definition of "domestic partner" in section 3(1) with

"domestic partner" of a deceased person means

(a) a person who was at the date of death in a registered relationship with the person; or

(b) a person to whom the person was not married but with whom the deceased person was living at the date of death as a couple on a genuine domestic basis (irrespective of gender).

and by substituting the s 3(1)(A) with:

"For the purposes of the definition of domestic partner in subsection (1)

(a) "registered relationship" has the same meaning as in the Relationships Act 2008; and

(b) in determining whether persons who were not in a registered relationship were domestic partners of each other, all the circumstances of their relationship are to be taken into account, including any one or more of the matters referred to in section 35(2) of the Relationships Act 2008 as may be relevant in a particular case."

FREE WILL REVIEW OFFER

During the months of March, April and May 2010 we will review your existing Will free of charge in our office on the following conditions:

- **maximum time 20 minutes per person per couple or per family;**
- **if we do not hold your Will, then a copy of your present Will is to be brought with you to the interview;**
- **if any changes to your Will are undertaken fees will be charged to you and the time at the interview will be recovered in the fees charged for the work;**
- **every effort will be made to see you at a mutually agreeable time and date.**

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SONS OF GWALIA - WHO IS RIGHT?

On 31 January 2007, the High Court of Australia handed down its decision in the case of *Sons of Gwalia v Margaretic*. The decision had immediate repercussions in the corporate world, and caused, and continues to cause, a division of opinion among commentators in relation to whether, in fact, the decision was one which ought to be applauded, or overruled by legislation. *BY* DAVID BRETT

The case revolves around the interpretation of Section 563A of the *Corporations Act 2001* ("the Act"). That section states *"Payment of a debt owed by a company to a person in the person's capacity as a member of the company, whether by way of dividends, profits or otherwise, is to be postponed until all debts owed to, or claims made by, persons otherwise than as members of the company have been satisfied"* (emphasis added). In other words, when a company goes "broke", the shareholder comes last.

The case centred around the expression *"in the person's capacity as a member"*. The Directors of the company, which was a publicly listed gold mining company, were alleged to have breached the stock exchange listing rules by failing to notify the stock exchange that it would not be able to meet its contracts and would not be able to continue as a going concern. Mr Margaretic, a shareholder of the company, claimed that the company, by its actions, had engaged in misleading and deceptive conduct in breach of s.52 of the Trade Practices Act, and s. 12DA of the Australian Securities and Investments Commission Act.

Mr Margaretic claimed that the damages suffered by him as a result of the breaches were monies owed to him, not in his capacity as a shareholder of the company, but in the capacity of an individual who had suffered damage and he was therefore entitled to seek, in the liquidation of the company, payment of the damages suffered.

The liquidators took the view that s. 563A of the Act prevented Margaretic from claiming, and the matter ultimately went to the High Court, where the claim of Margaretic was upheld.

This lead to a fierce debate – those in favour of the decision believe that a shareholder ought to be in no worse position than any other party who has suffered loss or damage as a result of the incorrect actions of others, and that the decision represents a strong incentive for companies to ensure that they comply with the continuous disclosure requirements required by the stock exchange. Transparency, it was felt, was vital, and directors and companies ought not to be able to withhold information from the public that would have an effect on the share price, and the decision of the members of the public whether to buy or sell shares in a particular company.

Those against the decision felt that the difficulties created by the decision were such that it would be preferable to overturn it. Difficulties were foreseen for the liquidators, in that shareholders claiming against a company under s.52 of the Trade Practices Act would not have their claims tested in Court in the normal manner, as when a company is placed into liquidation, such actions against the company are stayed. Therefore, a liquidator would have to assume the role, effectively, of a judge, and decide whether the claims made were valid,

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CHANGES TO *OWNERS CORPORATIONS ACT 2006*

The *Consumer Affairs Legislation Amendment Act 2010* (Act) amends the *Owners Corporations Act 2006* (OCA). The Act was assented to on 9 February 2010 and the sections amending the OCA will come into operation on the earlier of a day to be proclaimed or on 1 January 2011. *BY* ROBYN CROZIER

Some of the major amendments to the OCA are:

Section 11 – Power to Delegate

- The instrument of delegation of power must be made at a general meeting.

The instrument of delegation must therefore be executed at the general meeting.

Section 29 – Penalty interest on arrears

- **The imposition of penalty interest on arrears of fees or another amount payable by a lot owner must be authorised at a general meeting.**
- **Owners corporations will be required to report to an annual general meeting any decisions to waive or not waive penalty interest.**

Previously an owners corporation had an automatic discretion as to whether or not it would charge interest. The amendment requires that at a general meeting of the owners corporation an ordinary resolution be passed that the owners corporation will charge penalty interest on any arrears of amounts owing by a lot owner to the owners corporation.

The reporting requirements to an annual general meeting may lead to members asking for reasons why decisions to waive penalty interest were made which could be embarrassing for lot owners who made late payments of fees due to financial hardship eg. loss of their job.

Section 54 - What is an insurable building?

- **A new definition of shared services is included and refers to pipes or cables used to provide services including water, electricity, gas and telecommunications to the building that are shared with a person other than the owners corporation or any of its members.**

This will be relevant to plans with multiple owners corporations and will trigger insurance requirements under section 61 of the OCA (reinstatement and replacement insurance) where previously there was no obligation.

Section 59 - Reinstatement and replacement insurance

- Mandatory insurance under this section will include reinstatement and replacement insurance for the owners corporation's portion of any shared services (as defined by section 54).

Insurance policies for plans with multiple owners corporations may need to be reviewed.

Section 94 - Can a lot owner vote if fees are unpaid?

- **A lot owner whose fees or other amounts owing to the owners corporation are in arrears is not entitled to vote in respect of an ordinary resolution unless the amount in arrears is paid in full. For the purposes of determining if a lot owner is in arrears, except in the case of payment by cash, an amount is only taken to be paid in full if it is paid not less than four business days before the vote in question.**

An unfinancial lot owner may be counted for the purposes of determining a quorum for a meeting of members and is entitled to vote in respect of a special or unanimous resolution but is not entitled to vote in person, by ballot or proxy in respect of an ordinary resolution. An unfinancial lot owner or his/her proxy is not eligible to be elected as a committee member and if already a committee member when he/she becomes unfinancial is suspended as a member of the committee until he/she becomes financial - see sections 77, 94,103(7) of the OCA

Section 101 – Functions and Powers of Committee

- **A committee will only have the powers and functions that are delegated by instrument in accordance with the provisions of section 11.**

In our view previously section 101 of the OCA gave an automatic delegation of power to the committee and the amendment therefore represents a change in policy.

Section 109 – Notice of Meetings

- **Notice of a meeting of a committee must be given at least 3 business days before the meeting or as determined by the owners corporation and the notice must include the minutes of the previous meeting and a statement that a member may appoint a proxy for the purpose of the meeting.**

Where the OCA specifies a time period for the giving of a notice of a meeting, the notice period means clear days. This means the day on which the notice is posted must not be counted. For example where a notice is sent on a Friday, the meeting can not be held until the following Thursday unless the owners corporation has determined another time period. If the committee of the owners corporation has not been delegated all the powers and functions of the owners corporation or the power to determine the number of days notice required to be given before a committee meeting is held then the committee cannot hold a meeting until three clear business days notice is given.

Previously a committee member did not have the right to appoint a proxy. Ostensibly this means a committee may hold a meeting and no elected members of the committee may be in attendance but may be represented by proxies (who may not be lot owners) - presumably not an event contemplated by the members of the owners corporation who elected the committee.

Section 151(4)(b) - Owners Corporation Certificate

- **An owners corporation certificate must be sealed with the owners corporation's common seal.**

Currently there is no requirement that a certificate be signed. Section 21 of the OCA requires the use of the common seal on a document to be witnessed by 2 persons who are owners of separate lots and are members of the owners corporation. Where there are certificates prepared for unlimited and limited owners corporations it will be necessary to ensure that the persons witnessing the affixing of the common seal are members of the relevant owners corporations. This will cause added expense and delay in providing certificates. This is also problematic as a vendor of a property is required to provide a vendor's statement to a purchaser prior to entering into a contract of sale. Section 32(3)(A) of the Sale of Land Act requires that a copy of an owners corporation certificate is attached to a vendor's statement.

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and, if so, the extent of the alleged losses. Bearing in mind the number of shareholders in public companies, and the propensity of people to seek to claim damages to avoid losses that would otherwise occur, it would reasonably be expected that in many cases, the claims of the shareholders would delay the proper administration of the liquidation of a company by many months, and, in some cases, many years. The costs of the liquidation would be hugely increased, to the detriment of the other creditors. Secured creditors such as banks etc. were of the view that the value of their security would be diminished and that funding, an important requirement for companies, would be a lot more difficult to obtain. This, it was felt, would have an adverse effect on the economy as companies would be restricted in their ability to raise funds and therefore undertake important projects.

Despite the finding of the Corporations and Markets Advisory Committee (CAMAC) that *"Any move to curtail the rights of recourse of aggrieved shareholders where a company is financially distressed could be seen as undermining legislative initiatives to provide shareholders with direct rights of action in respect of corporate misconduct"* , the Government has announced that it intends to introduce legislation to overrule the decision of the High Court, on the basis that the decision *"undermined the distinction between debt and equity"*

The decision in the Sons of Gwalia case does not, in our view, undermine that distinction. Nor does it, or should it, affect the ability of companies to raise capital funding for projects. What it does do, however, from a practical point, is to increase the length and cost of administrations and liquidations, and impose upon liquidators the requirement to make quasi judicial decisions regarding any claims by shareholders. The complexity of ascertaining whether a claim was valid would be substantial, and, even if valid, the difficulties in assessing the damages resulting from the claim would be similarly substantial. For example, if a company fails to report poor financial data, claims could be made that damage had been suffered for the difference between the share price at the time of withholding the information and the final share price, which in a liquidation, is often nothing. But that is simplistic. If the announcement had been made, the price of the shares would have dropped substantially in any event. The situation is clearly different for those who purchase shares in the company at the relevant time, but who would not have purchased them if the disclosure had been made This illustrates the complexities involved in such claims.

Does the Government's decision to legislate harm the continuous disclosure requirements of companies? Arguably it does. But the best way to make directors disclose full information is to sue them personally – representations are normally made by one or more directors, and claims can therefore usually be brought against them personally. Potential bankruptcy and disqualification from acting as a director normally focuses directors' minds on doing the right thing. It is our view that, whilst the High Court decision is correct, and the Government decision to overrule it is made on the basis of some spurious arguments, the end result may still be acceptable. Actions against directors are often better than claims against companies in liquidation - after all, in most cases, unsecured creditors, including shareholders, usually get very little if any return for the monies owed to them. Whilst directors often arrange their financial affairs to make themselves financially "bullet proof", there may still be more likelihood of getting some money from them than the company in liquidation, and the public opprobrium, and potential financial cost, would go along way to keeping rogue directors on the straight and narrow.

Until legislation is enacted, directors and shareholders of companies in financial difficulty should be wary of their respective legal positions. David Brett can provide advice to clients requiring further information on how this proposed change in the law may impact upon their personal circumstances.

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FORTHCOMING SEMINARS

McKean Park Litigation Department will conduct a series of seminars as follows:

21 April 2010	Traps under the Trade Practices Act and Fair Trading Act – Misleading and Deceptive Conduct
9 June 2010	How Litigation Works – An Overview of the Process of Litigation and What you can do to Reduce the Costs
4 August 2010	What is a Contract? Do we have a Deal?

The seminars commence at 7.30am in the Boardroom of McKean Park at Level 11/575 Bourke Street Melbourne.
A light breakfast will be served.

Please contact Melanie Shea on 8621 2860 or melanie.shea@mckeanpark.com.au to reserve your place.

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