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When is a bailment a PPS lease under the PPSA?

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It is trite to say that the passing of the Personal Property Securities Act 2009 (Cth) (PPSA) significantly changed the securities landscape of Australia. One of the most dramatic effects has been the statutory deeming of a series of transactions as "PPS leases", which allow, in certain prescribed circumstances, an external controller of a company to gain a better title to an asset subject to a PPS lease than the formerly solvent company could have had.[1] As a result, there has been commercial uncertainty about what kinds of transactions constitute a PPS lease. Such uncertainty can have potentially significant consequences for the original owner of goods deemed to be the subject of a PPS lease. The classic example is the lessor of goods, where the lease is a PPS lease and has been unperfected under the PPSA, whose title is subordinated to the external controller of the lessee. The gateway issue to the flood of legal consequences that follow is determining whether a particular transaction is in fact a PPS lease.

The threshold definition of a PPS lease, however, under s 13 of the PPSA, extends beyond mere leases and, relevantly, includes bailments. Prior to September 2017, the questions around what sort and in what circumstances bailments could constitute PPS leases were uncertain and confused.[2] However, these issues came to the forefront in *Bredenkamp v Gas Sensing Technology Corp, Re Welldog Pty Ltd (in liq) (recs and mgrs apptd)*[3] (*Bredenkamp*), handed down on 7 September 2017. *Bredenkamp* largely clarified several important issues about the operation of s 13, with particular respect to bailment.

What constitutes a bailment under the PPSA?

Section 13(1) of the PPSA defines a PPS lease as a "lease or bailment of goods" for certain specified time periods. However, "bailment" is not defined in the PPSA's dictionary at s 10. Because the threshold question for any transaction resembling a bailment which may fall under the PPSA is whether the impugned transaction is in fact a bailment under the PPSA, the identification of what is a bailment under the PPSA is a critical issue requiring determination.

In *Bredenkamp*, this was the first issue for Barker J. The proceeding concerned whether the Gas Sensing Technology Corporation (GSTC) or the receivers of Welldog Pty Ltd (in liq) (the company) were entitled to the possession of the certain equipment (the GSTC equipment). The company was a subsidiary of GSTC, and GSTC, a technical services company in the resource sector, would sometimes store the GSTC equipment on the company premises before shipping it to other projects where it would be used. Sometimes, the company made use of the equipment for projects in its Australian business, on the condition it would be returned to GSTC after the projects were completed.

The receivers claimed that the GSTC equipment, which was plainly personal property, was the subject of a bailment that met all the features of a deemed PPS lease as at 20 March 2017, being the date on which the receivers were appointed. Because GSTC had not perfected their security interest under the PPSA, if the equipment was subject to a deemed PPS lease, the relevant equipment would be vested in the company as at the date of the administrators' appointment.

Of the four issues raised in the proceeding regarding the characterisation of the GSTC equipment as being subject to the PPS lease under s 13, the first was whether it was a bailment under s 13(1).

Barker J adopted the reasoning of the receivers that the *legal* meaning of the word "bailment" from *Hobbs v Petersham Transport Co Pty Ltd*[4] (*Hobbs*) should be used.[5] That case provides:

> A bailment comes into existence upon a delivery of goods of one person, the bailor, into the possession of another person, the bailee, upon a promise, express or implied, that they will be re-delivered to the bailor or dealt with in a stipulated way.[6]

In this case, there was a bailment because the equipment was left in the care, custody and control of the company, and to varying extents had been used in connection not only with GSTC's business but also the company's Australian business. GSTC both delivered the equipment into the possession of the company and the company was taken to have made the implied promise that it would redeliver the relevant equipment to GSTC or otherwise deal with the equipment as required by GSTC. Therefore, the *Hobbs* criteria of a bailment

were satisfied, and a s 13(1) bailment came into existence, subject to the operation of the rest of s 13.[7] In coming to this decision, Barker J rejected GSTC's submissions that a bailment required there to be "exclusive possession".[8]

In *Bredenkamp*, Barker J confirmed that the common law definitions of bailment and statutory requirement under s 13(1) of the PPSA are relevantly the same, adding some useful clarification to the law. In coming to this position, Barker J's reasoning is consistent with the principle that where a word is used in an Act which has an established legal meaning, it is assumed that it is used with that meaning unless the context requires otherwise.[9]

What does it mean to regularly engage in the business of bailing?

A determination that a transaction is a bailment is not, however, sufficient to constitute a PPS lease under s 13, even once the temporal requirements for the bailment in s 13(1) are satisfied. This is because there are several statutory exclusions from the definition of a PPS lease, and those exclusions apply to bailments as well. Critically, s 13(2)(b) provides an exclusion from the operation of the PPSA in the following terms: "a PPS lease does not include … a bailment by a bailor *who is not regularly engaged in the business of bailing goods*" (emphasis added).

It was this exclusion where the receivers' argument came apart, being the third issue in the proceeding.[10]

GSTC denied that it was regularly engaged in the business of bailing goods. The receivers relied on *Forge Group Power Pty Ltd (in liq) (recs and mgrs apptd) v General Electric International Inc*,[11] where Hammerschlag J provided (albeit in the context of leasing as opposed to bailing) that the exclusion in s 13 is directed to activity which constitutes engaging in the business of leasing (by analogy, bailing), not to engaging in the activity of entering into leases (bailments).[12] The receivers in this case pointed to what they said was an aggregation of evidence that indicated that GSTC was regularly engaged in the business of bailing goods.

However, GSTC's argument was that, in reliance on a decision of the New Zealand Court of Appeal, *Rabobank New Zealand Ltd v McAnulty*[13] (*Rabobank*), they were not in the *business* of bailing goods at all, let alone regularly. In *Rabobank*, the New Zealand Court of Appeal held that a syndicate merely stabling a horse at a stud farm was not in the business of bailing goods because it was not intending to profit from the stabling and instead was in the business of maintaining and profiting from the stallion. It was a case where the bailment was *incidental* to the business.

This reasoning was later applied by Master Sanderson in *Re Arcabi Pty Ltd (recs and mgrs apptd) (in liq); Ex parte Theobald & Herbert in their capacities as recs and mgrs of Arcabi Pty Ltd*[14] (*Re Arcabi*). In this case, GSTC made the argument that it profited from supplying services to clients using its skilled personnel and its equipment and *did not profit* from bailing property to the company's clients. Even if GSTC were to pay the company a fee for the bailment, which it did not, that fee would merely be an incidental expense to the business and would not be the business itself. On GSTC's submission, the fundamental precondition to the operation of s 13 is the identification of a bailing business that is a "proper component" of GSTC's business, and it is only once that has occurred that an analysis of the regularity follows.

Barker J ultimately found favour with GSTC's arguments,[15] on the basis that there was no evidence of a "business model" through which GSTC made money by storing the equipment with the company, and therefore merely because profit might be made by a string of conduct where one of the steps was the storage of the equipment with the company, does not mean that GSTC was regularly engaged in the business of bailing goods.[16] Therefore, s 13(2)(b) was not satisfied because a PPS lease does not include a bailment by a bailor who is not regularly engaged in the business of goods.[17]

Following on from *Re Arcabi* and now *Bredenkamp*, it follows that the s 13(2)(b) exclusion has two elements, both of which must be satisfied in order for the impugned bailment to be a PPS lease:

- First, there must be a "business of bailing goods", in that the bailments cannot be merely incidental to the business but be a core part of the business itself.
- Second, there must be regular engagement with the business of bailing.

Section 13(2)(a) is in substantially similar words but with respect to leasing, there would be no apparent reasons why s 13(2)(a) should operate differently, and therefore identification of a business of leasing goods, it follows, would also be a precondition for establishing a PPS lease (with respect to an impugned lease).

Bailments and value

Finally, even if there is a business of bailing goods, with sufficient regularity, that alone is not sufficient. Section 13(3) prescribes that the section "only applies to a bailment for which the bailee provides value."

"Value" is defined by s 10 of the PPSA and:

> (a) means consideration that is sufficient to support a contract; and

(b) includes an antecedent debt or liability; and
(c) in relation to the definition of purchase money security interest — has a meaning affected by section 14.

Although, in *Bredenkamp*, the failure of the receivers to establish that s 13(2)(b) was satisfied was fatal to their case, Barker J heard the argument and determined the question, in the alternative, of whether the bailment in the circumstances was for "value". More specifically, as the receivers claimed the para (a) definition was satisfied, his Honour needed to determine if there was sufficient consideration to support a contract.[18]

The receivers relied on a definition of consideration from Carter's *Contract Law in Australia*.[19] The issue came down to two competing applications of consideration first raised but not decided in *Re Arcabi*: whether it was sufficient for consideration given for a contract of which bailment was one part (and may be incidental to the contract's performance) or whether it was sufficient for consideration needed to be specifically given for the bailment.[20]

As noted by Duggan in *Australian Personal Property Securities Law*,[21] the problem is that if a "global" approach to consideration is taken then, because every bailment arrangement has consideration at some point in the overarching financial arrangements, s 13(3) has virtually no work to do. As submitted by GSTC, the legislative intention of parliament by including s 13(3) was to impose a limitation and therefore, it should be given the narrower view of the two readings.

Barker J again found in favour of GSTC and determined that while GSTC had received value in one sense, in that the bailments supported the Australian business which made money for GSTC, there was no value sufficient to support a contract provided in respect of the bailments specifically. The indirect financial benefit could not, in the circumstances, be understood as constituting sufficient consideration. In doing so, Barker J adopted Duggan's narrower understanding of value in that it needed to be more specific than simply being part of a global financial or business arrangement.[22] Whilst his Honour expressly stressed that he was not suggesting that an indirect financial benefit can never relevantly constitute consideration, the diffuse nature of the GSTC business model meant that the financial arrangements by which they earned profits were not sufficiently connected for the bailing of the equipment to constitute consideration.[23]

Accordingly, GSTC was successful, meaning the bailing arrangements, despite being found to be bailments, nonetheless were excluded by either s 13(2)(b) or (3) from being a PPS lease. Accordingly, the confiscatory effect of s 267 did not apply and GSTC was entitled to possession of the equipment.[24]

Conclusion

The impact of *Bredenkamp* is to add a refreshing degree of clarity on the proper analytical process to be followed when identifying whether a specific transaction is a PPS lease/bailment. The relevant questions to be determined could now be stated as the following:

1. Is there a bailment, in that there was delivery of goods of one person, the bailor, into the, not necessarily exclusive, possession of another person, the bailee, upon a promise, express or implied, that they will be redelivered to the bailor or dealt with in a stipulated way?
2. If so, does the bailment fit the stipulated temporal requirements of s 13(1)?
3. If so, was there a business of bailing goods, in that the bailments were not merely incidental to the generation of profit?
4. If so, did the bailor regularly engage in said business?
5. If so, was value, including consideration sufficient to support a contract, provided by the bailee for the specific bailment?

If the answers to those five questions are yes, then the transaction constitutes a PPS lease. Accordingly, the impact of *Bredenkamp* is both to narrow the scope of arrangements that could be considered as PPS lease/bailments (by adopting a narrower approach to questions 3 and 5), and to provide commercial certainty for those fearful of whether a certain arrangement is susceptible to the confiscatory effect of the PPSA. The latter, at the very least, is a wholly welcome development.

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Footnotes

1. Specifically, where the PPS lease is deemed a security interest and is then unperfected pursuant to the PPSA, it can be vested in the grantor on the grantor's winding up or bankruptcy.
2. Some of the relevant issues were briefly considered in a decision of Master Sanderson in *Re Arcabi Pty Ltd (recs and mgrs apptd) (in liq); Ex parte Theobald & Herbert in their capacities as recs and mgrs of Arcabi Pty Ltd* (2014) 288 FLR 236; [2014] WASC 310; BC201407252 (*Re Arcabi*) at [18]–[27] on an application by the receivers for directions from the court under s 424 of the Corporations Act 2001 (Cth), but of the issues canvassed, his Honour only determined one.
3. *Bredenkamp v Gas Sensing Technology Corp, Re Welldog Pty Ltd (in liq) (recs and mgrs apptd)* [2017] FCA 1065; BC201707116.
4. *Hobbs v Petersham Transport Co Pty Ltd* (1971) 124 CLR 220.
5. Above n 3, at [66].
6. Above n 3, at [39] citing above n 4, at 238.
7. Above n 3, at [64]–[66].
8. Above n 3, at [64].
9. *Hamersley Iron Pty Ltd v Forge Group Power Pty Ltd (in liq) (recs and mgrs apptd)* (2017) 320 FLR 259; [2017] WASC 152; BC201704639 at [329] per Tottle J.
10. The second issue in the proceeding concerned a question regarding the meaning of "indefinite period" rendered obsolete by subsequent legislative amendments to s 13.
11. *Forge Group Power Pty Ltd (in liq) (recs and mgrs apptd) v General Electric International Inc* (2016) 305 FLR 101; [2016] NSWSC 52; BC201604555.
12. Above n 11, at [40] and [50].
13. *Rabobank New Zealand Ltd v McAnulty* [2011] 3 NZLR 192; [2011] NZCA 212.
14. *Re Arcabi*, above n 2, at [24]–[27].
15. Above n 3, at [104].
16. Above n 3, at [108]–[110].
17. Above n 3, at [112]–[113].
18. Above n 3, at [117]–[118].
19. J W Carter, *Contract Law in Australia*, 6th edn, LexisNexis, 2013.
20. Above n 3, at [120].
21. A Duggan and D Brown, *Australian Personal Property Securities Law*, 2nd edn, LexisNexis, 2016, [3.39] as cited in above n 3, at [122].
22. Above n 3, at [146]–[147].
23. Above n 3, at [149].
24. Above n 3, at [151].