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Corporate Newsletter

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Appeal allowed in PPSA retention of title decision: Update on *Central Cleaning Supplies (Aust) Pty Ltd v Elkerton* [2014] VSC 61

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Background

In a newsletter published in March 2014 entitled '*Out of time – transitional PPSA provisions no longer provide protection*', Carter Newell discussed a decision of the Supreme Court of Victoria where it was held a business involved in the hire of industrial cleaning equipment and supply of cleaning services was unable to rely on a retention of title (**ROT**) clause in their standard credit application agreement to recover property that was claimed to have vested in one of its customers immediately prior to that customer's insolvency. At the time, the decision in *Central Cleaning Supplies (Aust) Pty Ltd v Elkerton* [2014] VSC 61 served a vital reminder to business owners to ensure that adequate steps had been taken to protect their security interests in personal property and, in particular, whether the transitional protections provided by the *Personal Property Securities Act 2009* (Cth) (**PPSA**) could be relied upon as giving rise to such protection.

On 12 May 2015 the Court of Appeal in Victoria handed down their decision of the appeal brought by Central Cleaning Supplies (Aust) Pty Ltd (**Central Cleaning**).[1] In allowing the appeal and determining that the commercial arrangement between Central Cleaning and its customer Swan Services Pty Ltd (**Swan Services**) was a '*transitional security agreement*', the Court of Appeal's decision essentially relied on principles of contractual interpretation which may be relevant to future PPSA disputes involving parties transacting business on the basis of standard terms of supply supplemented by individual purchase order or invoicing terms.

ROT clauses and the PPSA

It is well established that a provision in the trading terms or other governing agreement between a supplier and its customers that constitutes a ROT clause (e.g. where the supplier retains ownership and title to the goods supplied to the customer) creates a '*security interest*' in the supplied goods in favour of the supplier for the purposes of the PPSA.

Generally speaking, in order for that security interest to maintain its priority over later in time security interests, it must then be '*perfected*'. While there are other avenues

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available for perfection depending on the type of personal property subject to the security interest, registration on the Personal Property Securities Register (**Register**) is the most common method of perfection.

If the supplier (as the secured party) does not register (or otherwise perfect) their security interest, the PPSA provides that on the customer (the grantor) suffering an '*insolvency event*' – for example, being placed into administration or liquidation – the supplier's security interest in the supplied goods will vest in the customer immediately prior to that insolvency event. As a result, those goods will be available to the administrator or liquidator to satisfy claims by creditors generally, or to otherwise be used in the ordinary course of administering the affairs, of the insolvent customer.

Central Cleaning Supplies (Aust) Pty Ltd v Elkerton: Background facts

It is worthwhile briefly revisiting the circumstances of the commercial arrangement between Central Supplies and Swan Services before discussing the appellate judgment.

Commercial arrangement between Central Cleaning and Swan Services

Central Cleaning operated an industrial cleaning equipment and services business. In the present case, Central Cleaning supplied cleaning equipment to Swan Services on trading terms which included a ROT clause.

In September 2009, Swan Services signed a credit application form. On the reverse side of this form was an itemised list of 'Credit Application Terms' (**Credit Terms**), which stated that the supply of equipment from Central Cleaning to Swan Services would be governed by Central Cleaning's '*Standard Terms and Conditions as in force from time to time*' (**T&Cs**), which, although referenced, were not provided with the Credit Terms. The Credit Terms also indicated that Swan Services would be given 30 days to pay Central Cleaning for any equipment supplied.

Central Cleaning did not subsequently sign the credit application form. However it instead started to provide equipment to Swan Services and provided an invoice in respect of each supply. The first invoice was provided to Swan Services in September 2009 and included the T&Cs on the reverse side.

One of the clauses within the T&Cs included on the invoice was a ROT clause, stating that the equipment supplied to Swan Services under the invoice remained the property of Central Cleaning until it had been fully paid for. Relevantly, Central Cleaning did not action any registrations on the Register in respect of the supplies of equipment under the invoices.

Administration and liquidation of Swan Services

In May 2013, Swan Services was entered into administration, and subsequently liquidation. Elkerton was appointed as one of two liquidators of Swan Services.

In accordance with their trading arrangement, Central Cleaning had supplied equipment to Swan Services (prior to it entering administration) which had not been paid for. Central Cleaning therefore sought to rely on its ROT clause contained in the T&Cs to have their equipment returned.

The liquidator sought to rely on Central Cleaning's failure to perfect their security interests in the supplied equipment through registration on the Register to resist any demand for its return. In doing so, the liquidator argued that each supply of equipment entered into after 30 January 2014 (e.g. the end of the period granting transitional protection to security interests created prior to this date) gave rise to a separate contract of sale containing a ROT clause, and that as the transitional period under the PPSA had expired, goods provided under invoices dated post 30 January 2014 gave rise to security interests which were not perfected and therefore vested in Swan Services upon its insolvency.

Decision at first instance

At first instance, the Supreme Court ruled in favour of the liquidator. Her Honour Justice Ferguson held that:

1. as the Credit Terms themselves did not expressly include a ROT clause or otherwise '*provide for the granting of a security interest*' (in accordance with s 308 of the PPSA) in respect of future supplies, there was no transitional security agreement in place capable of protection under the PPSA's transitional protection provisions; and

2. furthermore, each invoice tendered to Swan Services constituted separate contracts of sale each requiring perfection (which may have occurred through registration) and the failure of Central Cleaning to perfect security interests (for example, by registration) arising from the invoices tendered to Swan Services after 30 January 2014 meant that those interests vested in Swan Services immediately prior to its administration.

As a result, Central Cleaning's security interest in the supplied goods vested in Swan and Central Cleaning was relegated to the status of an unsecured creditor in Swan's liquidation.

Central Cleaning appealed the decision to the Court of Appeal.

Decision on appeal

As the Court of Appeal stated in its judgment, Central Cleaning's '*claim to recover the equipment [could] only succeed if its interest in the relevant equipment [was] covered by the transitional provisions of the PPSA*'.

The key issues to be decided on appeal were whether a ROT clause was part of the broader supply and services agreement between Central Cleaning and Swan Services, and if so, whether that ROT clause came into effect prior to 30 January 2014.

In a unanimous judgment, the Court of Appeal resolved these issues in favour of Central Cleaning and **allowed the appeal** on the basis that there was a transitional security agreement which featured a ROT clause between the parties.

Reasoning of Court of Appeal's decision

The Court of Appeal respectfully disagreed with the judge at first instance by finding that a transitional security agreement was created by Swan Services signing and returning the Credit Terms, and Central Cleaning subsequently supplying goods and services to Swan Services pursuant to the T&Cs contained in the standard invoice.

The Court of Appeal explained that this finding was reached by examining the circumstances and exchange of documents between the parties from the commencement of their trading relationship and looking beyond the argument relied upon by the liquidator that there was no security agreement capable of transitional protection due to the absence of a ROT clause in the signed Credit Terms.

The Court of Appeal found that:

1. Swan Services' signing of the Credit Terms constituted an agreement to be bound by Central Cleaning's T&Cs from time to time (as was expressly stipulated in the Credit Terms) in respect of every supply of equipment;

2. notwithstanding that it was not included in the Credit Terms, a ROT clause was incorporated in the T&Cs included on the reverse of the first invoice (which was supplied to Swan Services the day after the Credit Terms were signed), and also in all future invoices; and

3. as Swan had accepted under the Credit Terms that future supplies of goods and services would be subject to Central Cleaning's T&Cs from time to time, '*the terms on which Central Cleaning agreed to provide credit to Swan Services included provision for the ROT clause as a standard term of each future supply of equipment*'.[2]

It is also interesting to note that the Court of Appeal's decision was reached after finding that Swan Services' return of the signed Credit Terms was a '*unilateral act*' that should not, of itself, be construed as acceptance of an offer or the creation of a contract. Instead, the return of the signed Credit Terms signified Swan Services' intention to create legal relations with Central Cleaning[3] and that the proper conclusion to reach in the circumstances was that the contract was formed at the time of the first supply of equipment.[4] As the first invoice relating to that supply of equipment included the T&Cs that Swan Services had earlier agreed it would be bound by, it was therefore bound by the ROT clause included in those T&Cs.

Discussion

The successful appeal of the Supreme Court's decision in *Central Cleaning Supplies (Aust) Pty Ltd v Elkerton* is yet another example of the ongoing importance of considered drafting and an awareness and understanding of the PPSA when preparing documentation governing commercial relationships. A strong understanding of the PPSA becomes even more essential where goods are supplied on credit and/or retention of title terms, whereby the owner of the goods or equipment is exposed to greater risk under the vesting provisions of the PPSA.

The decision also provides some guidance to businesses that may find themselves in a '*battle of priority*' for their own property, in that the Victorian Court of Appeal has demonstrated that it will approach such disputes by stepping back and looking at the overall history and circumstances of the commercial relationship between contracting parties. Even though transitional protection under the PPSA has now lapsed, the Court of Appeal's methodical yet common-sense examination of the conduct and exchange of documents between parties is still applicable in determining exactly when a security interest has arisen and calculating the time periods relevant to taking certain action under the PPSA.

[1] *Central Cleaning Supplies (Aust) Pty Ltd v Elkerton* [2015] VSCA 92
[2] Ibid [7].
[3] Ibid [32].
[4] Ibid [30].

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Professional Guides

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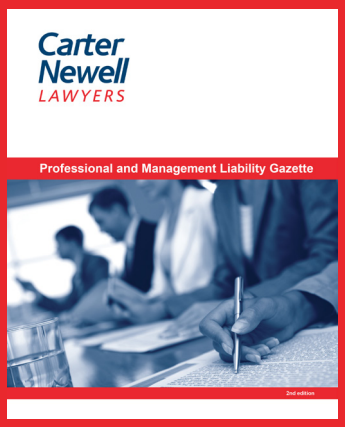

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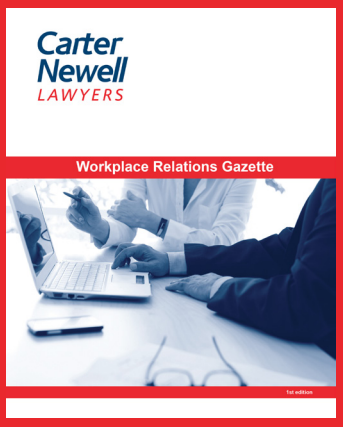
Joining Carter Newell's extensive suite of publications, this Gazette has been created by our specialised industrial / workplace relations and work health and safety practice in consultation with our internationally recognised insurance practice.



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