BUDDLEFINDLAY

If you have goods in storage you can breathe easy again

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It didn't create too much of a splash, but the recent New Zealand Court of Appeal case of Rabobank New Zealand Ltd v McAnulty[1] resolved a significant issue in New Zealand - albeit one that most people probably weren't aware of.

The case revolved around the definition of "lease for a term of more than 1 year" in the Personal Property Securities Act 1999 (PPSA). The court's interpretation was that the definition excluded bailments where the bailor was not regularly engaged in the business of bailing goods. Had the court based its decision more closely on the literal wording, it would not have made this exclusion, and many people could have been caught out.

Leases for a term of more than 1 year

To appreciate the significance of the exclusion, it is necessary first to understand the significance of the term "lease for a term of more than 1 year".

Under the PPSA, if there is a "lease for a term of more than 1 year" between two entities (referred to in this article as the lessor and lessee) in relation to any goods, the lessor is deemed to merely have a security interest in those goods. In other words, the lessor's rights are, in many respects, given the same status as those of a financier that has taken security in the leased goods. The principal consequence is that if the lessee grants a security interest in those goods to a third party (such as a bank), the lessor cannot simply recover the goods on the basis that it is the owner of them - it must show that its rights as lessor are a security interest which has priority over the security interest of that third party.

There is a protection for lessors, which is that if they register a financing statement on the Personal Property Securities Register (PPSR) within 10 working days of the lessee taking possession of the goods, their security interest takes priority over other security interests. However, despite this protection, the width of the definition of "lease for a term of more than 1 year" is still very significant. This is because many lessors do not realise (or have not historically realised) that they have a security interest, and therefore do not register a financing statement in time to gain this protection. Further, even those that do realise, need to go to the trouble of registering, and satisfying other requirements in the PPSA.

Risk of PPSA being overlooked

The principal part of the definition of "lease for a term of more than 1 year" states that it is "a lease or bailment of goods for a term of more than 1 year". This captures a number of transactions which are not financing transactions, and thereby affects many people that are not accustomed to dealing with finance regulation, and do not naturally consider it or monitor changes to it. For example, in New Zealand, many gaming trusts have arrangements under which they place gaming machines in pubs. Although there is no lease, there is almost certainly a bailment[2], so it is likely that gaming trusts hold a mere security interest in their machines. The fact that a finance-related statute applies to such arrangements would surprise many people and is easily overlooked.

The experience in New Zealand to date has been that many initially overlooked the application of the PPSA to their businesses. The most significant early cases related to leases for a term of more than 1 year which the lessors had not identified as security interests. However, over time, it appears that those whose business it is to regularly enter into leases or bailments have become aware of the issue. Law firms and industry groups have, by and large, identified such businesses and warned them of the risks.

Issue considered in Rabobank New Zealand Ltd v McAnulty

The definition of "lease for a term of more than 1 year" has a significant exclusion, which is that it excludes "a lease by a lessor who is not regularly engaged in the business of leasing goods". However, there is an apparent gap when you put the wording of that exclusion together with the principal part of the definition and read "a lease or *bailment*[3] of goods for a term of more than 1 year ...[excluding] a lease by a lessor who is not regularly engaged in the business of leasing goods". The gap is that, while bailments are brought in by the principal part of the definition, the exclusion does not mention them.

In the case of *Rabobank New Zealand Ltd v McAnulty*, the court had to consider whether this meant that a bailment by a bailor who is not regularly engaged in the business of bailing goods is a mere security interest. The consequences if this was the case were potentially far reaching. People who are not regularly engaged in the business of bailing goods are unlikely to have been identified and educated by law firms or industry groups about potential PPSA risks.

For example, very few people going overseas and leaving their furniture with a storage company would think to register a financing statement against that storage company. (I know this from the surprised and outraged phone call one of my friends received from a storage company when he did that very thing.) To give a more commercial example, it is unlikely that all organisations that have major computer systems housed in data centres run by third parties will have registered against those third parties.

Decision in Rabobank New Zealand Ltd v McAnulty

The court noted that the literal words may suggest that the exclusion does not apply to bailments. However, it considered that the intention must have been for that exclusion also to apply to bailments, and ruled that the use of the words "lease" and "lessor" in the exclusion must be short-hand for "lease or bailment" and "lessor or bailor".

Consequently, bailments of goods by those who are not regularly engaged in the business of bailing goods are outside the scope of the PPSA.

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(1) [2011] 3 NZLR 192

(2) A bailment is an arrangement under which possession, but not ownership, passes

(3) Emphasis added

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