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# **LEASES AND THE PERSONAL PROPERTY SECURITIES ACT 2009**

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## LEASES AND THE PERSONAL PROPERTY SECURITIES ACT 2009

The *Personal Property Securities Act 2009* (Cth) ("the Act") came into effect on 30 January 2012. The laws of each state and territory have now been brought together under one national system and online register called the Personal Property Security Register ("the PPS Register").

Although the operation of the Act is limited to personal property and expressly excludes interests in land and fixtures, the Act will still affect leases to the extent that they involve personal property and other security interests. Landlords should make themselves aware of the effect of the Act and take appropriate action to protect their interests under the new laws where required.

### How will leases be affected?

The Act expressly notes that personal property does not include land or fixtures. The definition of 'land' includes leasehold interests and therefore the Act does not apply to leases of land. However if a lease of land also includes the lease of personal property that is not a fixture, for example where a landlord leases fitted out premises, furniture or plant and equipment, the lease may give rise to a security interest under the Act and require registration on the PPS Register.

It is therefore important for a landlord to determine, before entering into a lease, whether the items leased with the premises are fixtures or personal property and therefore whether the Act applies.

### "Fixture" or "Personal Property"?

In order to determine whether an improvement on the land is a fixture or personal property case law must be consulted. Generally speaking property is a fixture when it has been permanently affixed to the land in order to improve the land or the buildings on the land. As outlined above, this type of property is not affected by the Act.

Inclusions can be defined as items that improve the use of a building. For instance an office fit-out and partitions are usually affixed to improve the use of the building rather than to improve the building itself, and are inclusions. This type of property falls within the definition of personal

Similarly, a bank guarantee is a contractual promise to pay and, consequently, does not constitute a security interest in favour of the landlord.

property under the Act and can therefore be registered on the PPS Register.

Whilst the Act generally does not apply to fixtures, there is still a potential for the Act to apply in relation to tenants fittings *if* under a lease agreement, a landlord is able to take certain tenant-owned fixtures as security to ensure the performance of the tenant's obligations. In this circumstance the landlord holds a security interest capable of registration. If the landlord does not register such a security interest on the PPS Register, the tenant's other financiers (who may have security over the fittings) will take priority over the interest of the landlord, thereby potentially preventing the landlord from obtaining any benefit from such security interest.

### Abandoned goods clauses in leases

If a landlord is able to retain goods left by an outgoing tenant, as security for outstanding rent or other obligations, then the landlord can register this interest on the PPS Register and take priority over other creditors. This is provided that those creditors had not previously registered their own interest in the same items.

In order to ensure that an abandonment clause creates a security interest in favour of the landlord the clause should be clearly drafted to allow a landlord to sell any property left by the tenant and to use the proceeds of sale to meet any of the tenant's unfulfilled obligations under the lease.

If goods or equipment have been abandoned by a tenant, a landlord should search the PPS Register before selling any items. A search of the PPS Register would identify the holders of any security interest in these goods or equipment.

### Guarantees

The Act does not apply to contractual promises to pay because a contractual promise to pay does not confer a security interest in personal property. Consequently a personal guarantee in a lease does not create a security interest as it only creates contractual rights against the guarantor and does not give the landlord any interest in the guarantor's property.

### Security Deposits

Where a landlord receives a security deposit from a tenant which it holds on trust it is possible to register a security interest on the PPS Register in relation to the deposit. A security interest is created because the security deposit secures the tenant's obligations.

### **Fit-out**

Leases often contain a clause allowing the tenant's fit out to remain at the premises at the expiry of the lease if the tenant elects not to remove it. Under such a clause, the landlord takes ownership of the tenant's fit out and the premises can be re-let with the fit out included. Before agreeing to such an arrangement a landlord should search the PPS Register to determine if a third party has a registered interest in the tenant's assets. If the search indicates that another party has a charge over the assets, the lease should require the tenant to remove the fit out at the expiration of the lease.

Where the landlord retains a tenant's fit out at the end of a lease, the landlord may need to register its interest in that property before or shortly after giving possession of the premises to a new tenant.

### **Assignments and subleases**

A security interest in connection with a lease that has been registered by a landlord may need to be re-registered following an assignment of the lease or if the tenant grants a sublease. This is because a landlord's security interest may not survive an assignment or sublease if as a result there is a change in

possession of any personal property leased with the premises.

### **Consent of Secured Parties**

Landlords should amend their standard lease terms to ensure that any security interest arising under the lease can be registered on the PPS Register. This is particularly relevant because the tenant's consent is required before a registration can be made.

Consent can be inferred from the tenant signing the lease, however to protect landlord's interests leases should include a specific provision in which the tenant agrees that any security interests arising pursuant to the Act can be registered on the PPS Register by the landlord.

In addition, landlords should consider including a clause in the lease which will contractually require tenants to provide information required to enable registration on the PPS Register. This clause should also require tenants to advise of any changes to their details during the life of the security interest.

### **How to register a security interest**

The process of registering involves lodging a completed financing statement with the applicable registration fee on the PPS Register. This can be accessed at the following website: <http://www.ppsr.gov.au>

A 'finance statement' uploaded on PPS Register will require you to include details of the parties to the transaction, the collateral and details of the security interest.

Immediately following registration, the landlord will receive a verification statement. A copy of this statement must be provided to the tenant as soon as practical after registration, unless the tenant has waived the right to receive it.

Once the landlord has registered its interest on the PPSR and provided a verification statement to the tenant no further action is required in respect of the registration unless or until something in respect of that security changes.

### **When to register security interests**

Pursuant to the Act a security interest may be registered after the interest has 'attached' itself to the personal property by way of possession and is enforceable through a written agreement. A security interest is considered to have 'attached' to personal property after the grantor does an act which gives them rights in the property, for example executes a document (such as a lease).

Generally a security interest should be registered within 15 business days of the tenant taking possession of the relevant property.

It should be noted that a security interest's priority is determined by the time of registration, so registration should be completed as quickly as possible.

Security interests created in leases are most likely to be registered for up to 7 years. If the lease exceeds 7 years in duration, a financing statement can either be registered for between 7 and up to 24 years. Alternatively a landlord's registration for up to 7 years can be extended for a further 7 years. The latter option may be a better

alternative if the lease contains options to renew which, if not triggered, would not extend beyond seven years. However, the risk is that the landlord may forget to update its financing statement.

The costs of registering interests on the PPS Register can be passed on to the tenant under the lease.

### **What if an interest is not registered?**

Registration on the PPS Register will allow landlords to protect their ownership of personal property. It will also prevent a landlord, as a secured party, from losing its priority against any other secured party with a competing interest in the same personal property.

If landlords fail to register on the PPS Register, then they may run the risk of someone else gaining a superior interest in the property, if it is in their possession. Not only will this include situations where the tenant becomes insolvent, but also a third party could 'purchase' the leased equipment from the tenant and landlords may have no recourse against the purchaser to regain the property (although they may still have a claim against the tenant). The new PPS laws place an emphasis on *possession* of property and therefore a third party could gain better rights in property even though the landlord is technically the owner.

### **Time to discharge**

There is no time specified in the Act by which a discharged security needs to be removed from the

register. Discharging a financing statement is free.

If nothing is done to a registered financing statement, it will 'drop off' the PPS Register after the registration time expires. For example, if your financing statement is for up to 7 years and no financing change statement is registered, the financing statement will 'drop off' the PPS Register even if the security has not been discharged. This means the landlord will lose any priority it may have enjoyed and would need to lodge a fresh financing statement if the security interest continues.

A provision in the lease may have a clause which requires the landlord to remove its financing statement once it is clear that there are no longer any obligations being secured.

### **Leases prior to 30<sup>th</sup> January 2012**

Consideration should also be given to registering security interests which arose prior to 30 January 2012 to ensure that they are also protected. The Act contains a Transitional Security Interest Regime that establishes a bridging period to allow transition to the new system. This will be effective until the 30<sup>th</sup> January 2014. During this period security transactions that were created before the Act came into effect will be deemed to be capable of registration regardless of whether the security agreement meets the criteria established by the Act.