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Off the rack

K&L Gates' **Stephen Hume** and **Anna Smith** advise on protecting interest in your garments.

AUSTRALIAN FASHION RETAILERS are facing a number of challenges, increasing rents, online competition and the arrival of low-cost international chains, to name a few. All of these factors have contributed to the insolvency of some of Australia's prominent fashion retail names.

It is usual practice for suppliers in the fashion industry to supply goods on credit or consignment terms and to maintain an interest in the goods as security for payment of the purchase price. This is referred to as a retention of title (ROT) arrangement. ROT arrangements aim to protect the supplier in the event that the customer runs into financial difficulty.

ROT arrangements can either be 'simple' or 'all moneys'. Simple ROT clauses state that legal ownership (title) to the goods will not pass to the customer until the customer has paid for those particular goods. An 'all moneys' clause reserves title in all goods supplied to the customer until the customer has settled all outstanding invoices with the supplier.

Increased volatility in the retail sector means it's vital for those who supply goods under an ROT arrangement, to ensure their interest in the unpaid goods is adequately protected in the event of the retailer's insolvency.

Previously suppliers could rely on ROT provisions in their supply contracts to recover unpaid goods, without having to take additional steps to protect their position. However, the Personal Property Securities Act 2009 (PPSA) created a new regime and requirements for protecting interests in personal property.

The PPSA introduced a national online registration system, the Personal Property Securities Register (PPSR). Suppliers are required to 'perfect' their security interest by entering a registration on the PPSR. Suppliers who register an interest in unpaid goods will be entitled to 'super' priority (compared to general security agreements). Failure to perfect a security interest correctly, or at all, may result in a supplier losing its super priority and/or effectively becoming an unsecured creditor of the company.

Key Questions for Suppliers

Do you have a security agreement that gives rise to a security interest?

An ROT clause is usually part of the supplier's terms of trade, which are either annexed to a credit application or individual invoices. This is called a 'security agreement' under the PPSA. The security agreement does not need to be executed by the customer, but must be adopted or accepted by the customer (also known as the grantor) by an act or omission (such as placing an order for goods).

Has the security interest 'attached' to collateral?

For attachment to occur, the customer must have rights in the goods (e.g. by taking delivery or possession of them), and value is given or the customer does an act by which the security interest arises (i.e., a debtor/creditor relationship is created).

How to perfect the security interest?

In order to be enforceable against a customer, an ROT clause should be perfected by registration as a purchase money security interest (PMSI). For suppliers, the most common type of perfection will be

via registration of a 'financing statement' on the PPSR.

Suppliers must tick the box marked 'PMSI' when completing the registration to claim super priority. One registration can usually cover all supplies to the grantor if the ROT clause relied on is a simple ROT clause (depending on the description in the financing statement). However, if the supplier's ROT clause is an all moneys clause, the supplier should register two registrations, this is because:

- a PMSI only operates as a PMSI for goods which have not been paid for
- a registration is defective, and therefore ineffective as a perfection of that security interest, if it indicates that the security interest in the collateral is a PMSI (to any extent) and in fact the security interest is not a PMSI (to any extent).

The PMSI registration will protect goods that have not been paid for (giving the supplier a super priority over all others with a security interest over the customer) whereas the second registration will protect goods that have been paid for as an ordinary security interest (giving the supplier priority over subsequently registered security interests).

Timing Requirements

To receive super priority a PMSI must be registered within specific timeframes which vary according to the type of personal property and its intended use. Where the goods supplied constitute tangible inventory (e.g., items of clothing, fabric, buttons etc), the supplier must ensure that its security interest is registered before the customer takes possession of the goods. A PMSI that is not registered within that timeframe is still valid, however will not enjoy super priority.

It is relatively inexpensive and straightforward to register a financing statement on the PPSR, and helpful instructions are available at: www.ppsr.gov.au/register-security-interests. Getting your house in order at the outset will help to protect you in the event that your customer falls into financial difficulty down the track. ■

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