

FORGE - TURBINES - DECISION PROVIDES GUIDANCE ON PPS LEASES AND CONFIRMS OPERATION OF VESTING PROVISIONS IN PPSA

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Legal Briefings - By **David John** and **Tony Coburn**

On 11 February 2016, the NSW Supreme Court provided some helpful guidance about the circumstances in which an operating lease will constitute a PPS lease and the operation of the vesting provisions in the *Personal Property Securities Act 2009* (Cth) (**PPSA**).

The decision of Hammerschlag J in *Forge Group Power Pty Ltd (In Liquidation) (Receivers and Managers Appointed) v General Electric International Inc* [2016] NSWSC 52 confirmed that two mobile gas turbine generator sets (**Turbines**) which had been leased by General Electric International Inc (**GE**) to Forge Group Power Pty Limited (In Liquidation) (Receivers and Managers Appointed) (**Forge**) but were unregistered on the PPSA, vested in Forge immediately before the appointment of administrators to Forge on 11 February 2014.

Whilst the conclusion is not surprising, the decision provides some useful guidance around:

- the scope of a PPS lease, particularly the exclusion for lessors not regularly engaged in the business of leasing goods, and
- the test to be applied to determine whether the exclusion for fixtures should apply.

The decision represents a timely reminder to all lessors about the paramount importance of registering PPS leases and the very significant consequences of failing to do so.

BACKGROUND

The Turbines had been leased by GE to Forge in connection with certain services which Forge was providing to Horizon Power in relation to establishing a power station. GE failed to register its interest in the Turbines against Forge on the Personal Property Securities Register (**PPSR**). In circumstances where Forge fell into administration, s.267 of the PPSA provides that the Turbines vest in Forge, with the consequence that GE 'lost' its interest in the Turbines, which had a value in the order of \$60m, and as it turns out the secured creditor who held 'all assets' security over the assets of Forge received a 'windfall'. Given the very substantial value of the Turbines, GE ran two quite difficult arguments in an attempt to avoid this adverse outcome, namely it sought to argue that the lease of the Turbines should be excluded from the operation of the PPSA because:

- First, GE was not regularly engaged in the business of leasing such goods within the meaning of s.13(2)(a), being a carve out on the definition of a PPS lease which otherwise requires registration on the PPSR.
- Second, the Turbines had become fixtures for the purposes of s.10, thereby taking them outside the operation of the PPSA by reason of s.8(1)(j) (with land not being subject to the PPSA).

WHETHER GE WAS REGULARLY ENGAGED IN THE BUSINESS OF LEASING GOODS?

GE tried to argue that:

- Whilst it conceded that it has engaged in the business of leasing goods outside Australia, it was not regularly engaged in such business within Australia.
- The date at which the assessment is to be made is not the date the lease was entered into, but is rather the date on which the security attaches to the collateral or alternatively the date on which the event occurs that brings about the vesting. The significance of this second argument was technical, in that GE had, following the execution of the lease, sold a large portion of its leasing business in Australia.

The Court found that:

- In testing whether a person is (or is not) regularly engaged in the business of leasing goods, consideration should be had to activity wherever it occurs, and not only to activity in Australia.
- The test applies when the lease was entered into.
- In any event, when the lease was entered into and at all material times thereafter, GE was regularly engaged in the business of leasing goods in Australia.

In assessing the meaning of 'regularly engaged', the Court noted that there was no relevant Australian authorities, and hence was prepared to look at judicial guidance from Canada and New Zealand. The Court proposed that the *"...question (which is one of fact) is whether or not, at the material time, leasing goods was a proper component of [the lessor's] business"* (at [46]). So it need not be the principal or even a substantial part of the business of the lessor, rather it can be simply something that the lessor does in its business, or even, according to this judgment, something an entity sets itself up to do and tries to do (even if not yet successfully).

In this case, it was considered relevant that GE advertised and promoted its desire to lease the Turbines, was engaged in leasing turbines to other sites in Australia prior to selling a large portion of its leasing business and following the sale, continued to be willing to and did in fact provide replacement turbine engines to certain customers.

WHETHER THE TURBINES BECAME FIXTURES?

Interestingly, GE sought to argue that the Turbines had become a fixture on the Horizon Power land, thereby taking them outside the operation of the PPSA. The Court noted the counterintuitive nature of this argument, whereby GE felt compelled to argue that, objectively viewed, it intended its own property to become part of the land owned by another, Horizon Power.

GE argued that a bespoke meaning of fixture should be adopted for the purposes of s.10, to the effect that a non-trivial attachment will make something a fixture, rather than apply the usual common law test for affixation. The Court rejected GE's argument and found that the common law test applies and confirmed that the Turbines did not become fixtures, because the objective intention with which the Turbines were put in place was not that they should become fixtures. The Court noted a number of factors, including that:

- The Turbines were designed to be demobilised and moved to another site easily and in a

short time.

- The Turbines were only intended to be on the Horizon Power site for a temporary, 2 year period.
- Forge was contractually obliged to return the Turbines at the end of the rental term.

CONCLUSION

The Court ultimately found that the lease of the Turbines by GE to Forge constituted a PPS lease and that, where GE did not register its interest on the PPSR, as a result of s.267(2) of the PPSA, GE's interest in the Turbines vested immediately before the appointment of the administrators to Forge.

GE will no doubt be very disappointed with the result. However, the decision represents a timely reminder to all lessors about the paramount importance of registering PPS leases and the very significant consequences of failing to do so.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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