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SALE OF BUSINESS AND THE PPS ACT

1. Introduction

The sale of a business often includes the sale of personal property such as equipment, stock in trade and motor vehicles. Practitioners for both vendors and purchasers need to understand what personal property is included in the sale and how the Personal Property Securities Act 2009 (Cth) (**PPS Act**) may impact on that sale. This Bulletin is not intended to be a comprehensive list of what to do in a sale of business, but to highlight issues in relation to the PPS Act.

2. Personal Property

Personal property included in the sale of a business may be subject to a security interest registered on the Personal Property Securities Register (PPS Register). For example, a purchaser may:

- take on obligations pursuant to existing equipment hire contracts and/or stock in trade contracts. The contracts may contain a retention of title clause. A security interest may be registered as a result of this type of clause.
- take a transfer of a license, such as a liquor licence. A security interest may be registered over the licence on the PPS Register.
- purchase a motor vehicle. A buyer only acquires a motor vehicle free of any security interest if the seller is a prescribed person (licenced dealer / trader). (s.45 of the PPS Act).

The exception in s.46 of the PPS Act that a purchaser takes personal property free of any security interest only applies where the sale is in the ordinary course of the vendor's business. This exception does not apply to the sale of the business notwithstanding personal property is included in the sale of the business.

3. Acting for the vendor

3.1 Search the Personal Property Securities Register

The vendor's practitioner needs to know what security interests are registered over the personal property involved in the sale of the business because the grantees (those who hold the security interests) will need to be informed of the sale and in most cases the interests need to be released.

The vendor's practitioner should search the register to find any security interests registered in

the name of the vendor. To do that the practitioner will need to know certain information, such as:

- (a) name and date of birth of any individual grantor;
- (b) name of any organisational grantor;
- (c) ACN for any organisational grantor;
- (d) ABN for any organisational grantor that has an ABN;
- (e) ARBN for any organisational grantor that has an ARBN; and
- (f) ARSN for any organisational grantor that is the responsible entity of a registered scheme, if the scheme has an ARSN.

Specific security interests can also be searched if the vendor has details such as:

- VIN number (ie for any motor vehicles included in the sale);
- Serial number (ie for any boat included in the sale);
- Registration number ie the number allocated to the financing statement upon registration on the PPS Register.

Beware!

Sometimes searching the PPS Register alone is not enough to find all security interests.

In some circumstances it is not necessary to register a security interests on the PPS Register: for example where the secured party has perfected the security interest by possession. See s.21 and s.24 of the PPS Act.

Control of the personal property is, in some circumstances, effective to perfect a security interest. See s.21, s.25 - 29 of the PPS Act.

Practitioners should also refer to the factsheet “Searching the PPS Register – Considerations regarding migrated registrations” available from the “Factsheets” page under the “Ask the Registrar” tab at www.ppsr.gov.au. In this Fact Sheet you will find some tips on how to search for a grantor. For example, this Fact Sheet explains that, the form in which the name of an individual appears on the PPS Register, will depend on which register it was migrated from. As a result it may be necessary to search by one or more family names or a first name, the initial of the second given name and the family name.

The practitioner should give details to the vendor client of any registered security interests and also ask the client whether or not they are aware of any unregistered ‘encumbrances’ so that these can be dealt with in the contract, as necessary.

3.2 Release of security interests

The purchaser will clearly want any security interests registered over the personal property being purchased to be released at settlement. In most cases, the practitioner acting for the

vendor, will be instructed to obtain any necessary releases. If the client elects to arrange the release of any security interests for settlement purposes, then clear written advice should be given to the client as to what is required and when and the consequences of failing to do this.

The purchaser may also want any registered security interests, not only released but also removed from the register by having the secured party lodge a financing change statement. Some security interest registrations will relate to just the assets in question and it will be relatively simple to have that security interest removed where the secured party registers a financing change statement that states the security interest is discharged.

Where the personal property being sold is part of the collateral in an all present and after acquired property security interest (an **ALLPAAP**) then a financing change statement can also be lodged removing the specific property from the registration.

However, where the personal property being sold makes up just part of a class of goods included in a financing statement it can be more problematic. Individual goods cannot be removed from a 'non' ALLPAAP financing statement without lodging a new financing statement with the particular goods omitted. Lodging a new financing statement would result in a loss of priority for the security holder.

For example, the vendor/grantor owns 5 refrigerators and a financing company has a security interest registered over all 5 refrigerators in one financing statement. Where the vendor sells only one refrigerator with the business a financing change statement cannot be lodged to remove this one refrigerator.

In some instances, the form of release will contain an undertaking that the secured party will lodge a financing change statement within a certain time following settlement, usually 10 business days. In other instances the financing change statement will be lodged prior to settlement, which may remove the need to obtain a release.

3.3 Form of release

Practitioners should carefully consider the wording of the form of release.

The Australian Banker's Association has issued a form for use by banks when releasing a security interest. This form is available at:

<http://www.bankers.asn.au/Submissions/Personal-Property-Securities/Personal-Property-Securities>

Beware!

- Some banks are not using this form of release.
- Some banks are using a modified version of this form.
- Non-banks will probably have their own form of release.
- A financing change statement cannot be registered in certain circumstances, for example for a 'non' ALLPAAP security where only some collateral is released.
- The ABA release is issued in favor of the grantor/vendor i.e. not the purchaser.

- Some releases provide that the security holder will lodge the financing change statement within 10 business days of providing the release. Instructions should be obtained well prior to the settlement date as to whether or not the client or practitioner will be responsible for checking this has been done by the security holder.

3.4 Sale of Business Contract

The January 2010 version of the sale of business contract, as approved pursuant to s.53A(1)(a) of the *Estate Agents Act* 1980 (Vic), **does not** contain any express reference to the PPS Act.

The approved contract is currently under review and it is expected that the next edition will include a PPS Act clause.

The following should be considered in any contract for the sale of business:

- A condition which specifies the security interests to be released at settlement.
- Include any relevant serial numbers, VIN, PPS Register registration numbers in the contract for the avoidance of any doubt, especially in relation to describing the releases which must be provided at settlement.
- Where a full release is to be provided, a condition in the contract that the vendor will require any relevant secured party to register the necessary financing change statement either at settlement or within a reasonable specified period following settlement.
- A condition in the contract that a copy of any releases be given to the purchaser within a reasonable time prior to settlement. This is to give the purchaser's practitioner and financier sufficient time to verify the details prior to settlement.
- Where assets include goods and fixtures, prescribe in the contract which items are goods and which items are fixtures. This will avoid a dispute as to what items require a release because the PPS Act does not apply to 'fixtures' so no PPS Act release is required.
- Where the vendor is a natural person, their date of birth to enable the purchaser to search the PPS Register.
- Usually a contract of sale specifies the 'encumbrances' which are to remain or are to be removed at settlement. Encumbrances should be defined to include a reference to any PPS Act registrations.
- A vendor warranty in relation to the assets being sold that the PPS Act does not apply, and/or that there are no PPS Act registrations that encumber the assets or that any security interests will be removed before settlement.

4. Acting for the purchaser

4.1 Advice pre-contract

Where a purchaser's practitioner has been given the opportunity to see the contract of sale of the business before it has been signed he or she should discuss with the client if there is any personal property included in the sale. See the discussion about what might be included

in a sale of business in the “Personal property” section of this bulletin.

During the pre-contract period, the purchaser may instruct the practitioner to undertake certain due diligence enquiries in relation to the business. Part of this due diligence usually includes identifying any encumbrances. Registrations on the PPS register is only one such encumbrance. There may be others.

Where there is personal property included in the sale:

- Consider whether the contract contains the conditions discussed in the section of this bulletin, “Acting for the vendor - Sale of business contract”. Negotiations should be entered into in relation to those issues if the contract is silent.
- Search the PPS Register to determine if there are any security interests registered over the relevant assets. Where the vendor is a natural person, their date of birth will be required. If it is not listed in the contract the information should be requested from the vendor’s practitioner. The purchaser should be advised not to enter the contract without this information.

Where there are any security interests over the assets being acquired, the practitioner should discuss with the purchaser the need to obtain a release of any security interest at settlement.

4.2 Advice where the client has already signed the contract

Where a purchaser’s practitioner has not been given the opportunity to review the sale of business contract before the purchaser signed, the following should be considered in relation to the PPS Act.

- Discuss with the client if there is any personal property included in the sale. See the discussion about what might be included in a sale of business in the “Personal property” section of this bulletin.
- If personal property is included in the sale, look at the contract of sale for the issues raised in the section of this bulletin “Acting for the vendor - Sale of business contract”.
- A search of the PPS Register should be made to determine if there are any security interests registered over the relevant assets. Where the vendor is a natural person, their date of birth will be required. If it is not listed in the contract the information should be requested from the vendor’s practitioner.
- Where there are any security interests over the assets being acquired, the practitioner should discuss with the purchaser the need to obtain a release of any security interest, or evidence that the security interest has been discharged at settlement and the consequences if no releases are provided.

4.3 Advising on finance documents

If a practitioner acting for the purchaser is asked to advise on the purchaser’s finance documents he/she should carefully consider any clauses in in relation to the PPS Act.

Common provisions include:

- Requiring the client to “do anything” the bank requires in connection with the PPSA. This seems very broad and the possible impact of this should be highlighted to the client.

- Contracting out of any notices that the financier is able to under the PPS Act, for example, the right of the client to receive notice of registrations on the PPS Register. (see s.157 of the PPS Act).
- Contracting out of providing any information requested by interested parties under s.275 of the PPS Act.
- Stating that the purchaser/borrower will be in default if there is a registration of any new security interest. This may be a problem because there could be many further security interests created by the purchaser in the running of the business, for example, a 'retention of title' clause in any supply agreement will create a security interest which can be registered on the PPS Register.

Special attention should be paid to the impact that the PPS Act may have where a vendor is financing the purchase of the business. This may include the vendor registering a security interest over the assets of the business as security for repayment of the vendor's loan. This security interest (often arranged at the last minute) may cause the purchaser to be in default of other security interest obligations.

5. The retainer

Practitioners should carefully consider what matters need to be included in their retainer letter in relation to the PPS Act. One example is to specify who is responsible for checking the register (the practitioner or the client) to determine whether or not a financing change statement has been registered after settlement.

6. Audit of agreements

When acting for the purchaser, a practitioner may receive a copy of various documents that relate to the business such as supply agreements, leases and hire purchase agreements.

Practitioners should advise their clients of the need to review the documents for appropriate PPS Act clauses.

Legal Practitioners' Liability Committee

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