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DEBTOR-INDUCED PAYMENTS

Abstract

The Australian *Personal Property Securities Act 2009* (Cth), as do the other personal property security acts of New Zealand and the Canadian provinces, clearly states that the recipient of a debtor-induced payment made by a grantor of a security interest in collateral is immunised from a proceeds claim or priority entitlement by a secured party. The policy behind debtor-induced payments is primarily to ensure that a debtor is able to pay his or her general unsecured creditors in priority to the debts owed to a secured party. An additional policy reason is the protection of the economy through the maintenance of the payments system generally. This article critically examines the legislation in the various Personal Property Securities Acts, including the case law, identifies the policy arguments in support of a broad application of the rule and suggests that the American provision in Article 9 of the Uniform Commercial Code provides a better solution as it will enhance the ability of a debtor to pay his or her unsecured debts and thereby ensure the free flow of cash and negotiable instruments used to pay debts.

I Introduction

The purpose of this article is to explore the interrelationship between a secured party's right to collateral secured by a security interest, including proceeds, and the right of third party creditors to receive payments of their unsecured debts free of the secured party's security interest. In particular, this article explores whether or not the personal property security legislation (in those jurisdictions, including Australia, that have adopted a form of legislation modelled on art 9 of the United States' Uniform Commercial

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Code[1] ('Article 9')) has changed the way courts deal with conflicting rights outside the insolvency laws. Those statutes will be collectively referred to as the '*PPSA*s'.[2] Do those rights of an unsecured creditor withstand the rights of a bank that has a security interest in the account perfected by control,[3] or the rights of a bank to set off any proceeds payment paid to the debtor's account with it? Such rights being accorded to a bank would defeat the object of ensuring that a debtor is able to pay his unsecured creditors free of any security interest granted in favour of a bank or a third party financier.

The Australian *Personal Property Securities Act 2009* (Cth) ('*AustPPSA*'),[4] like the other *PPSA*s, gives a secured party an automatic right to proceeds of collateral whether or not the instrument creating the security interest provides for proceeds as a class of collateral[5] or a description of the proceeds.[6] This proceeds entitlement therefore arises

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1 ('UCC'). The UCC was first promulgated in 1952 under the joint sponsorship of the American Law Institute and the National Conference of Commissioners on Uniform State Laws. For a summary of the amendments, see Uniform Law Commission, *UCC Article 9 Amendments (2010) Summary* <http://www.uniformlaws.org>: 'Article 9 was substantially revised in 1998, and the 1998 revisions are in effect in all states and the District of Columbia. The 2010 amendments to Article 9 modify the existing statute to respond to filing issues and address other matters that have arisen in practice following over a decade of experience with the revised Article 9 … [T]he 2010 amendments provide greater guidance as to the name of a debtor to be provided on a financing statement. … More importantly … provide significantly greater clarity as to the name of an individual debtor to be provided on a financing statement.'

2 The Canadian provinces have adopted a model developed by the Canadian Conference on Personal Property Security Law, with the exception of Ontario whose legislation is distinctively different. New Zealand adopted the Saskatchewan legislation with minor changes. The Canadian and New Zealand models predate the Article 9 revision in 1998. The Australian legislation is somewhat idiosyncratic although modeled on the New Zealand legislation but has been substantially redrafted to include a number of the Article 9 1998 revision changes, significantly perfection by control. The drafting style and change of terminology, such as 'grantor' for 'debtor' and 'personal property' in place of 'goods', and significant policy differences make the legislation difficult to compare with the overseas jurisdictions and to comprehend.

3 Under *AustPPSA*, s 12(4)(a) a bank that is an authorised deposit-taking institution (an ADI) is able to take a security interest in an ADI account held with it and perfect the security interest by control (s 21(2)(c)(i)). Perfection by control trumps perfection by any other means, usually perfection by registration, because of ss 57 and 75. Apart from Article 9, the other *PPSA* jurisdictions do not permit perfection by control. The idea of control derives from UCC § 8-106. It was originally confined to investment securities and other investment property under Article 8. It was applied to deposit accounts under § 9-104 under the 1999 Revision of Article 9. See UCC Article 9 § 9-104 Official Commentary. Perfection is automatic with a signed control account agreement. Perfection by registration of a financing statement is not required.

4 This Act commenced operation on 30 January 2012.

5 *AustPPSA* s 32(1).

6 Ibid s 20(6). A secured party must also comply with the requirements of s 153 Item 3 and the regulations when completing the financing statement. See Ronald CC Cuming, Catherine Walsh and Roderick J Wood, *Personal Property Security Law*

by operation of the statute.[7] It does this by providing that if collateral gives rise to proceeds, the security interest (a) *continues in the collateral*, unless the secured party authorised the disposal; and (b) *attaches to the proceeds* unless the security agreement provides otherwise. The first part of the provision allows the secured party to follow the collateral into the hands of a third party transferee, while the second part allows the secured party to trace or follow the collateral proceeds in the debtor's hands and beyond. If a sale of inventory occurs in the ordinary course of business of the seller (debtor), the secured party will have expressly or impliedly authorised the disposal. The right to the original collateral is therefore lost and the secured party must rely on the proceeds. Proceeds can be represented by cash, a substitution (trade in goods or an exchange), cheques and other negotiable instruments,[8] but not real property.[9]

This article originally arose in response to the New Zealand Court of Appeal decision in 2012 in *Commissioner of Inland Revenue v Stiassny ('Stiassny')*.[10] There were two main issues in the case, one involving the operation of s 95 of the New Zealand *Personal Property Securities Act 1999* (NZ) ('*NZPPSA*') and the other in relation to the recovery of a mistaken GST payment. The receiver unsuccessfully appealed to the Supreme Court of New Zealand. These decisions are discussed below.

II Background

One objective of the *PPSA*s is to enable inventory financiers to secure more effectively their reservation of title supplies or loans against new or used inventory. Prior to the enactment of the *PPSA*s, there were a number of uncertainties in relation to proceeds claims and protecting a proceeds-secured inventory financier.[11] The uncertainties apply to the two main types of inventory financing; namely, the supply of inventory on a reservation of title basis to a trader or a provision by a financier of a line of credit to enable a trader to acquire inventory. In each case, the supplier or financier will want access to the proceeds of sale represented by cash, cheques or proceeds in a bank account or any trade-in received by the trader to satisfy its security interest. This entitlement to proceeds is contrasted with the need of the trader to pay his or her general creditors.

(Irwin Law, 2nd ed, 2012) 556–558; Anthony Duggan and David Brown, *Australian Personal Property Securities Law* (LexisNexis, 2012) [11.29]–[11.31].

7 If not for this statutory entitlement a security agreement would require an after-acquired property clause or, in the case of a reservation of title arrangement, a trust proceeds clause.

8 Proceeds are extensively defined in *AustPPSA* s 31. They include identifiable or traceable personal property that is derived directly or indirectly from a dealing with the collateral or proceeds of collateral. See Cuming, Walsh and Wood, above n 6, 562–567; Duggan and Brown, above n 6, [11.08]–[11.14].

9 Cuming, Walsh and Wood, above n 6, 562.

10 [2013] 1 NZLR 140.

11 See generally N W Caldwell, 'Security Interests in Proceeds, Account Consolidation and the *PPSA*' (1995) 59 *Saskatchewan Law Review* 165.

As we have seen a proceeds claim or security interest is automatic under the *PPSA*s. It arises on dealing with the original collateral (or the proceeds of collateral) to which a security interest has attached that results in identifiable or traceable personal property.[12] By contrast, an after-acquired property clause in a debenture or general or specific security agreement will also attach to these items of personal property and they will be easily claimed. If the proceeds comprise a trade-in vehicle, or another item of personal property is swapped, there will be no difficulty for the secured party claiming it, as it will automatically be caught by the after-acquired property clause as original collateral and not as proceeds, which are substitute collateral. The question will be: does the charging or collateral clause cover the personal property that is represented by the proceeds, or must the secured party rely on the statutory entitlement to proceeds?[13] The policy behind a proceeds rule is that the secured party should be able to keep or have a claim to the resultant proceeds.[14]

Under the prior Anglo-Australian law,[15] the after-acquired property clause in a debenture charge would attach to any property obtained by the debtor as proceeds of sale or as a substitution, such as a trade-in. The position was different under a sale of inventory on a retention-of-title basis, as the supplier's rights would be limited to the unsold goods in the possession of the buyer. Any claim to proceeds (book debts), or new products obtained in substitution, was treated by the courts as subject to a charge and in most cases the charge would not be registered as a charge on book debts and thus was void for want of registration under the *Corporations Act 2001* (Cth).[16] Despite this, the High Court of Australia in *Associated Alloys Pty Ltd v ACN 001 452 06 Pty Ltd*[17] upheld a proceeds clause drafted as a trust for proceeds (to prevent a windfall to the supplier) requiring a debtor to hold the part of the proceeds on trust for the supplier that corresponded to the amount owing to the supplier for the original goods.[18]

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12 *AustPPSA* s 31.

13 This was important under the prior law but does not matter under the *PPSA* because of *AustPPSA* ss 20(6) and 32(1)(b); *NZPPSA* s 45(1)(b); *SaskPPSA* s 28(1). Under *AustPPSA* s 20(6) it is not necessary to describe or define proceeds but the requirements of s 153(1) item 4 must be complied with when completing a financing statement.

14 See Caldwell, above n 11, 168.

15 See generally RP Meagher, JD Heydon and MJ Leeming, *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* (Butterworths LexisNexis 4ed 2002) at 6.50 et seq; Hugh Beale et al, *The Law of Personal Property Security* (Oxford University Press, 2007) [4.12]; Michael Bridge, Louise Gullifer, Gerard McMeel and Sarah Worthington, *The Law of Personal Property* (Sweet & Maxwell 1st ed 2013) [12-026]–[12-033].

16 See Duggan and Brown, above n 6, [11.3]–[11.7]; Hugh Beale et al, *The Law of Personal Property Security* (Oxford University Press, 2007) [5.09]–[5.25]; Roy Goode, *Proprietary Rights and Insolvency in Sales Transactions* (Sweet & Maxwell, 3rd ed, 2012), [5.58]–[5.66]; Gerard McCormack, *Secured Credit under English and American Law* (Cambridge University Press, 2004) 181–188.

17 (2000) 202 CLR 588.

18 Ibid 611. The proceeds claim failed as the majority described the inability to trace to the proceeds to the relevant invoices as 'the lacuna in the evidence' at [54].

Under the prior law, a debtor was empowered to use the proceeds of sale generated in his or her business to pay his or her creditors. This idea comes from the licence theory associated with the floating charge whereby the charge hovers over the assets of the business charged,[19] thus enabling the grantor to deal with his or her assets until the charge crystallises because an event of default has occurred. At this time the charge fixes upon the then property of the chargor. Until crystallisation the chargee has no property interest in the assets of the chargor that are subject to the floating charge, which would include cash at bank. With the fixed charge the chargee has a fixed interest or real right that can only be cut off by a disposition to a bona fide purchaser for value without notice.[20]

This licence theory endures under the *PPSA*s despite the security interest being a fixed legal interest.[21] Iacobucci J in *Royal Bank of Canada v Sparrow Electric Corp* expressed the licence theory in the following terms:

> Briefly, the licence theory holds that a bank's security interest in the debtor's inventory, though it be fixed and specific, is subject nevertheless to the licence in the debtor to deal with that inventory in the ordinary course of business … Consequently, says the theory, the bank's claim to the inventory must give way to any debts incurred in the ordinary course of business. … The security interest in inventory disappears only if the debtor actually sells inventory and applies the proceeds to a debt to a third party. [22]

A further objective of the *PPSA*s is to ensure that, subject to issues of insolvency law, a debtor is free to pay his or her unsecured creditors. The *PPSA*s in Canada, New Zealand and Australia, as well as UCC Article 9, provide a statutory solution to this objective in respect of negotiable instruments and credit transfers initiated by a debtor. Essentially these provisions are intended to replicate the prior law. The power given to a debtor by these provisions is equivalent to the power of a chargor under a floating charge before crystallisation,[23] as absent this power the chargor's

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19 *Stiassny* [2013] 1 NZLR 140, [37]; *Stiassny* [2013] 1 NZLR 453, [53]; Duggan and Brown, above n 6, [10.9]; Michael Gedye, Ronald CC Cuming and Roderick J Wood, *Personal Property Securities in New Zealand* (Thomson Brookers, 2002) [95.1].

20 Goode, above n 16, 4–10.

21 *Bank of Montreal v Innovation Credit Union* [2010] 3 SCR 3; *Royal Bank of Canada v Radius Credit Union Limited* [2010] 3 SCR 38; *iTrade Finance Inc v Bank of Montreal* [2011] SCC 26.

22 [1997] 1 SCR 411 ('*Sparrow*'), [91]–[93].

23 Ronald CC Cuming and Roderick J Wood, *Saskatchewan and Manitoba Personal Property Security Acts Handbook* (Carswell, 1994) 244. The same authors suggest at the sole purpose of the provision in relation to instruments is to remove any suggestion that a secured party can succeed in an action against an unsecured creditor who receives a negotiable instrument in payment of a debt that is covered by the collateral of a secured party of the debtor: Ronald CC Cuming and Roderick J Wood, *Alberta PPSA Handbook*, (Carswell, 1990) 183. See also Gedye, Cuming and Wood, above n 19, [95.1].

business would come to a grinding halt.[24] Absent this statutory right, a debtor would need to seek the consent of the secured party to each cheque, electronic transfer or cash payment of a third-party debt.

III Policy

The policy behind the statutory solution is found in *Flexi-Coil Ltd v Kindersley District Credit Union Ltd* ('*Flexi-Coil*'),[25] a decision of the Saskatchewan Court of Appeal, where it was said: 'The goal of these sections is to leave money and cheques largely free from security interests to preserve the integrity of the payment system in Canada which now includes credit transfers.' This policy can be refined to reflect two goals: first, the need to maintain finality in the payment system;[26] and, secondly, to ensure that the debtor's right to pay his or her ordinary creditors is preserved. These two goals do not give way to the existence of the right of a secured party to take security over the debtor's authorised deposit-taking institution ('ADI') account.[27]

In these circumstances, the existence of a security interest over the debtor's deposit account should not affect the broad policy goals. This is important because if the rule were otherwise, the existence of a security over an ADI account or the accounts of an inventory purchase money security holder would severely impair the free flow of funds. This freedom also minimises the likelihood that a secured party will enjoy a claim to the recipient's purchase with the funds.[28] As will be seen later in this article, the policy objectives are somewhat undermined by reason of the special protection given to ADIs in the *AustPPSA*.[29] There is a tension between the policy objectives of certainty in the banking system and preserving the rights of debtors to pay their creditors on the one hand, while on the other, protecting the proceeds of a secured party, particularly inventory financiers.

IV Proceeds

A security interest in personal property continues in the proceeds by operation of *AustPPSA* s 32(1). Proceeds of collateral to which a security interest is attached

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24 [2013] 1 NZLR 453, [53]–[54].

25 107 DLR (4th) 129. This case suggested public policy dictated that the section should be read as applying to EFT payments: Ronald CC Cuming, Catherine Walsh and Roderick J Wood, *Personal Property Security Law* (Irwin, 2005) 385. See generally Linda Widdup and Laurie Mayne, *Personal Property Securities Act: A Conceptual Approach* (LexisNexis, revised ed, 2002) [24.26]–[24.27].

26 Barkley Clark and Barbara Clark, *The Law of Secured Transactions under the Uniform Commercial Code* (A.S. Pratt, 3rd ed, 2012) [1.08[12][b]].

27 Defined in *AustPPSA* s 10 to mean an account with an authorised deposit taking institution licensed under the *Banking Act 1959* (Cth).

28 Note 3 to UCC § 9-332 official commentary.

29 See above n 3.

means identifiable or traceable personal property.[30] Proceeds include property that is derived directly or indirectly from a dealing with the collateral (or proceeds of the collateral).[31] Proceeds include intangible property and negotiable instruments. Notably, intangible property referred to in *AustPPSA* s 31(1)(c)(ii)) includes financial property,[32] which in turn includes currency. Negotiable instruments include cheques.[33] Proceeds also include a negotiable instrument such as a cheque.[34]

When considering a proceeds claim we are looking at two distinct things. One is *following,* which is the identification of an original asset in a different time or place. The other is *tracing,* the identification of a new asset as the exchange product of the original asset.[35] Tracing is not a remedy or a claim as commonly thought; it is a process undertaken by the court to determine an entitlement.[36] The entitlement is conferred by the *PPSA* but the remedy may be enforced by way of a restitutionary claim for money had and received, a constructive trust, an equitable lien or subrogation.

AustPPSA s 32(1) allows a secured party to assert its security interest in the traceable proceeds by stipulating that the security interest:

(a) continues in the collateral, unless:
    (i) the secured party expressly or impliedly authorised a disposal giving rise to the proceeds;
    (ii) the secured party expressly or impliedly agreed that a dealing with giving rise to proceeds would extinguish the security interest, and
(b) attaches to the proceeds unless the security agreement provides otherwise.

Personal property that falls within *AustPPSA* s 31 will not be proceeds unless it is derived directly or indirectly from a dealing with the collateral (or proceeds of the collateral) by the debtor. The debtor must have or acquire an interest in those proceeds, or have the power to transfer rights in the proceeds to the secured party

30 *AustPPSA* s 31.

31 *AustPPSA* s 31(a).

32 *AustPPSA* s 10. Intangible property *includes* financial property and financial property includes currency and negotiable instruments.

33 *AustPPSA* s 10.

34 *AustPPSA* s 31(1)(c)(v) because a cheque is a negotiable instrument.

35 Lionel Smith, 'Tracing the Proceeds of Collateral under the *PPSA*: *Flexi-Coil Ltd v Kindersley District Credit Union Ltd*' (1995) 25 *Canadian Business Law Journal* 460, 462. See generally Lionel D Smith, *The Law of Tracing* (Oxford: Clarendon Press, 1996) 6–18.

36 *Boscawen v Bajwa* [1996] 1 WLR 328, 334 per Millet LJ: 'A process where a person traces what happened to his property, identifies the persons who have handled or received it, and justifies his claim that the money which they handled or received (and, if necessary, which they still retain) can be properly regarded as representing his property.'

or a person nominated by the secured party.[37] The wording 'the power to transfer rights in the proceeds'[38] is not present in the Canadian or New Zealand *PPSA*s.

It is important to recognise that a payment initiated by a debtor, by way of negotiable instrument or electronic funds transfer, is not proceeds of the deposit account to which a security interest in an ADI account has attached. This means that the proceeds provisions in the *PPSA*s will not apply to such a transfer. The existence of a security interest in the ADI account itself does not give rise to a security interest in a cheque drawn on it by the debtor. The same is true of the debtor-initiated debit from the ADI account. If it were not so, it would limit the effect of the provisions and defeat the second policy goal. These provisions only protect a creditor after payment has been made. In the case of a cheque, only after clearance as a cheque is provisional payment until paid. This is because until actual payment, the drawer can countermand the cheque.

V Transferees Of Negotiable And Other Property

The *PPSA*s provides a number of ways whereby a general security agreement holder or an inventory financier's priority interest in proceeds is lost. These special priority rules are designed to protect holders of negotiable instruments and money. They include rules protecting creditor payments, negotiable instruments, chattel paper and negotiable documents of title.[39] This article will deal mainly with creditor payments in *AustPPSA* s 69.[40] Negotiable instruments are dealt with in *AustPPSA* s 70. The difference between the payment of a debt by means of a negotiable instrument to which *AustPPSA* s 69 relates and the purchase of a negotiable instrument under *AustPPSA* s 70 is that this latter section is concerned with a bona fide purchaser for value without notice.

AustPPSA s 70 is concerned with a consensual transaction whereby a person *acquires* an interest consisting of (a) a negotiable instrument or (b) an interest in a negotiable instrument for value. An acquirer's interest has priority over a perfected security interest in the negotiable instrument if he or she (i) gave value and (ii) took possession or control of the negotiable instrument and (iii) lacked knowledge in the relevant sense.[41] In the 'relevant sense' deals with a person whose business it is to acquire interests of this kind. If so, did he or she acquire the interest without actual or constructive knowledge that the acquisition constituted a breach of the

37 *AustPPSA* s 31(3).

38 This wording derives from the definition of attachment in s 19, which in turn comes from UCC § 9-203(b)(2). Article 9 was amended to include this wording in order to facilitate securitisation. They include limited rights in collateral short of full ownership: see Note 6 UCC § 9-203 Official Commentary.

39 Duggan and Brown, above n 6, [10.67]–[10.81]. See also *AustPPSA* s 10 (definition of financial property).

40 *NZPPSA* s 95; *SaskPPSA* s 31; UCC § 9-332(b).

41 *AustPPSA* s 70(2).

security agreement?[42] Where the acquirer is not in the business the test is higher as it requires an acquisition without actual or constructive knowledge of the security interest.[43]

A consensual transaction would include both a buyer and a secured party. Presumably these rules are designed to ensure that the default priority rules do not come into conflict with the general law, ie the holder in due course rules under the *Cheques Act 1986* (Cth) and *Bills of Exchange Act 1909* (Cth).[44]

The example given at paragraph 2.161 of the Replacement Explanatory Memorandum on the *Personal Properties Securities Bill* 2009 (Cth) appears to be incorrect as it presupposes that the bank acquires an interest in the cheque.[45] In reality, the bank in the example is simply a collecting bank. The bank would be an acquirer (holder) if it gave its customer immediate credit for the face value of the cheque and then collected the cheque on its own behalf and not as agent for its customer.[46] Similarly, a security interest in currency (money[47]) is lost if a holder of currency acquires currency with no actual or constructive knowledge of the security interest. This is dealt with in *AustPPSA* s 48.

The *PPSA*s deal specifically with the priority of the recipient of debtor-initiated payment (a general unsecured creditor) by providing rules that immunise a general unsecured creditor from any claim that a security party might have who seeks priority on the basis that the relevant payment represents proceeds of collateral that was secured by the security party's perfected security agreement.

AustPPSA s 69 protects a creditor who takes payment of a debt either:

(a) in money by an electronic funds transfer; or
(b) by contemporaneous authorisation or by a negotiable instrument.

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42 *AustPPSA* s 70(2)(b)(i). Speculation is not knowledge: *Belarus Equipment of Canada Ltd v C & M Equipment (Brooks) Ltd* (1995) 24 Alta LR (3d) 125, [128] (Alberta Court of Queen's Bench) ('*Belarus*').

43 *AustPPSA* s 70(2)(b)(ii). Duggan and Brown, above n 6, [10.70]; *Belarus* (1995) 24 Alta LR (3d) 125, [118]; *CFI Trust v Royal Bank of Canada* 2013 BCSC 1715, [203] ('*CFI Trust*').

44 Note that *AustPPSA* s 256 provides that if there is conflict, the other Act prevails over the *AustPPSA*.

45 *Replacement Explanatory Memorandum on the Personal Property Securities Bill 2009* (Cth), [2.161].

46 *Belarus* (1995) 24 Alta LR (3d) 125, [42]–[45], quoting Lord Macnaghten and Lord Lindley in *Capital & Counties Bank Ltd v Gordon* [1903] AC 240, 244–245.

47 Money is a personal chattel in possession but once paid into a bank account it is replaced by a chose in action. See generally Bridge et al, above n 14, [1-016]–[1-020]; Charles Proctor, *Mann on the Legal Aspect of Money* (Oxford University Press, 6th ed, 2005), [1.28 – 1.31]; David Fox, *Property Rights in Money* (Oxford University Press, 2008), [1.59 – 1.110].

For convenience *AustPPSA* s 69 provides:

> 69 Priority of creditor who receives payment of debt
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> (1) The interest of a creditor who receives payment of a debt owing by a debtor through a payment covered by subsection (3) has priority over a security interest (whether perfected or unperfected) in:
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> (a) the funds paid; and
>
> (b) the intangible that was the source of the payment; and
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> (c) a negotiable instrument used to effect the payment.
>
> Example: A bank account from which the funds were paid is an example of an intangible that was the source of the payment.
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> (2) Subsection (1) does not apply if, at the time of the payment, the creditor had actual knowledge that the payment was made in breach of the security agreement that provides for the security interest.
>
> (3) Payments made by a debtor are covered by this subsection if they are made through the use of:
>
> (a) an electronic funds transfer; or
>
> (b) a debit, transfer order, authorisation, or similar written payment mechanism executed by the debtor when the payment was made; or
>
> (c) a negotiable instrument.

The function of *AustPPSA* s 69 is to allow the debtor the freedom to pay his or her unsecured creditors but this freedom is restricted to the means set out in subsection (3). In some respects this freedom preserves negotiability while in others it reflects the need to preserve the payment system generally. If it were otherwise, the section and the licence to sell inventory would eviscerate the secured party's security interest.[48]

An example of how AustPSSA s 69 is intended to work is as follows:

> SP under a general security agreement holds a security interest in all of Debtor's present and after-acquired personal property that has been perfected by registration of a financing statement. Debtor buys two new Apple computers on invoice from S. In accordance with its usual practice, Debtor's account department pays the invoiced amount by BPAY from its trading account.[49]

Debtor holds its bank account with National Australia Bank ('NAB'). SP's security agreement will cover the NAB account. Any funds paid into that account by Debtor will, in the ordinary course, be the proceeds of the sale of inventory that are part of the all present and after-acquired collateral covered by the security agreement. Any credit balance in the NAB account is part of SP's security, as are any cheques or cash deposited to the account. These items will be proceeds of the inventory sold,

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48 *Sparrow* [1997] 1 SCR 411, [97] (Iaccobucci J).

49 This example is a modification of the example in Duggan and Brown, above n 6, [10.67].

as well as being original collateral secured by the after-acquired property clause. If Debtor were to default, SP would be entitled to any credit balance in the account. This would also include any cheques paid to third parties that had not been paid when SP appointed a receiver or otherwise enforced his security interest.

The position may be different in the case where Debtor's account with the bank is in debit.[50] There is no 'balance owing' to the debtor to which a proceeds claim could attach. This is because the requirement in *AustPPSA* s 31(3) that personal property is proceeds only if the grantor has rights in the proceeds or the grantor has rights to transfer proceeds to the secured party.[51]

Ordinarily, unless *AustPPSA* s 32(1) applies where SP expressly or impliedly authorised the dealing enabling Debtor to buy the Apple computers, S would take the BPAY payment subject to the security interest. This is because the definition of proceeds includes cheques (a negotiable instrument) and cash (financial property) under *AustPPSA* s 31(1)(c). A BPAY payment is usually a transfer from a bank account rather than a credit card account but *AustPPSA* s 69 is not restricted in this way by use of the term 'funds'. If *AustPPSA* s 32(1) does not apply (SP did not authorise the use of the proceeds), S has priority because of *AustPPSA* s 69 provided that S did not know that the payment was in breach of the security agreement.

The *NZPPSA* provision is worded differently. Section 95 of the *NZPPSA* provides:

> (1) A creditor who receives payment of a debt owing by a debtor through a debtor-initiated payment has priority over a security interest in-
> (a) the funds paid;
> (b) the intangible that was the source of the payment:
> (c) a negotiable instrument used to effect payment.
> (2) Subsection (1) applies whether or not the creditor had knowledge of the security interest at the time of payment.
> (3) In sub-section (1), a debtor-initiated payment means a payment made by a debtor through the use of-
> (a) a negotiable instrument; or
> (b) an electronic transfer; or
> (c) a debit, transfer order, an authorisation, or a similar written payment mechanism executed by the debtor when the payment was made.

50 Linda Widdup, in *Personal Property Securities Act: A Conceptual Approach* (LexisNexis, 3rd ed, 2012) [18.40] suggests that there was no proceeds claim in *Flexi-Coil* because the funds were deposited into an overdrawn account. This statement is clearly correct.

51 See also *CFI Trust v Royal Bank of Canada* 2013 BCSC 1715, [185]. This is because if there is a debit balance no property right arises because the customer is the debtor of the bank. If there is a credit balance the bank is the debtor of the customer.

This section replicates the current Saskatchewan provision, s 31(2), which was amended to include payments by electronic funds transfer following the *Flexi-Coil* decision.[52]

Under the Saskatchewan provision[53] and *NZPPSA* s 95, S would take the payment free of the security interest even if S knew of the security interest.[54] Under *AustPPSA* s 69, S would take free of SP's security interest unless S had actual knowledge that the payment was made in breach of debtor's security agreement with SP.[55] Ronald Cuming and Roderick Wood assert that this provision:

> was designed to deal with situations where a broadly based security interest in personal property has been given by the debtor. The debtor's property may include instruments, securities, or negotiable documents or title. In the absence of this special provision, no one who was aware of the existence of such a security interest could deal with the debtor in the ordinary course of business without the consent of the secured party. This would paralyse the business of the debtor.[56]

AustPPSA s 69 refers to both unperfected and perfected security interests. Unperfected ones are more likely to be defeated by third parties on the insolvency of the debtor. Where the security interest is perfected by registration, defeat is less likely as it will generally prevail over the interests of third parties, including liquidators, administrators and trustees.[57] No doubt the reference to 'unperfected' is to provide certainty of the validity of an unperfected security interest against unsecured creditors generally.[58] As a result both unperfected and perfected secured parties will have the benefit of *AustPPSA* s 31 and will be able to follow or trace his or her collateral or its proceeds. Despite this, the *PPSA*s strip away the rights of secured parties in order to protect the interests of third parties with the buyer transferee or cut-off rules and the payment of unsecured debts. It will not be possible to follow the proceeds if *AustPPSA* s 32(1)(a) applies or if *AustPPSA* s 69 applies, or if the debtor does not acquire an interest in the proceeds (s 31(3)(a)(i)) or a right to transfer rights in them (s 31(3)(a)(ii).[59] *AustPPSA* s 69 will not apply to a transaction involving the

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52 *SaskPPSA* 31(3)(a) now includes 'an instrument or an electronic funds transfer'. Note that with the exception of Ontario all the Canadian statutes have similar provisions. Ontario provides that transfers of negotiable instruments and money are to be determined without regard to the Ontario *PPSA*: *Personal Property Security Act*, RSO 1990, c P-10, s 29.

53 *The Personal Property Security Act*, SS 1993 c P-6.2, s 31 ('*SaskPPSA*').

54 But see *Stiassny* [2013] 1 NZLR 453 in the Supreme Court of New Zealand, [57] (Blanchard J).

55 Neither *NZPPSA* s 95 nor *SaskPPSA* s 31 contain a knowledge requirement. Both provisions provide that the creditor takes free of the security interest whether or not he or she has knowledge of any security interest.

56 Cuming and Wood, above n 23, 252. See also *Belarus* (1995) 24 Alta LR (3d) 125, [120]–[121].

57 *AustPPSA* ss 267–267A; *Corporations Act 2001* (Cth) s 588FL, subject to s 588FN.

58 *AustPPSA* ss 18(1), 20(1); *NZPPSA* ss 35–36, *SaskPPSA* s 10.

59 See above n 37.

payment for personal property paid for at the time of acquisition because the transaction is a sale not the payment of a debt.[60]

VI The Cases

The Courts in some of the Canadian provinces have considered the various debtor-initiated payments provisions and have taken differing interpretative approaches. The approach of the New Zealand courts differs even though the New Zealand provision is taken directly from the Saskatchewan *PPSA* ('*SaskPPSA*') with minor stylistic changes.

Flexi-Coil Decision

Flexi-Coil illustrates how the Saskatchewan equivalent to *AustPPSA* s 69 operates.[61] In *Flexi-Coil* Churchill dealt in farm equipment. Flexi-Coil provided inventory finance to it. Flexi-Coil's security interest was perfected by registration. Churchill banked with Kindersley Credit Union ('Kindersley') where it had an overdraft facility that was almost always in debit. Churchill sold certain inventory and paid the proceeds of $86,659 to its account with Kindersley. Some were cheques but $28,249 was paid into the overdraft account by electronic funds transfer.

Flexi-Coil claimed the $86,659 as proceeds of the inventory. It was common ground that Flexi-Coil held a security interest in the proceeds but that this was destroyed at the point when Kindersley received the moneys into the Churchill account with it. This was because the account was a line of credit account and was never in positive balance. The Court said at [39]:

> [T]here was never a point at which Churchill could have called for the proceeds of the cheque to be paid to him. The account was never in positive balance. . . . Since it was in negative balance, the result was the netting of two amounts. When an account is in overdraft . . . no property right arises. The customer is the debtor of the deposit taking institution.

As a consequence of this finding, the Court of Appeal accepted Kindersley's argument that it was protected by *SaskPPSA* s 31(2). This section protects a creditor who receives payment of a debt either in money or by an instrument drawn by the debtor even where the creditor is aware of the existence of a security interest in the money or the instrument.[62]

The Court of Appeal took the view that Kindersley gave value to Churchill when the cheques were deposited to the overdraft account without notice of Flexi-Coil's

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60 The other transferee or cut-off rules in Part 2.5 of *AustPPSA* and their equivalents in the other *PPSA*s will apply to a sale or lease transaction.

61 *SaskPPSA* s 31.

62 Instrument has a similar meaning to negotiable instrument in *AustPPSA* s 10.

proceeds claim. Value was either credit on which Churchill could draw or a reduction in the overdraft account balance. The giving of value made Kindersley a purchaser for value without notice within the meaning of *SaskPPSA* s 31(3). This provision is now *SaskPPSA* s 31(3)(a). The Court of Appeal also decided, rejecting Flexi-Coil's argument, that protection afforded by the section, which only applied to an instrument or a security, was capable of applying to credit transfers. Jackson JA for the Court of Appeal said that:

> when the *PPSA* was drafted credit transfers were relatively new … The goal of these sections is to leave money and cheques largely free from security interests to preserve the integrity of the payment system in Canada which now includes credit transfers. … Accordingly, it is my opinion that the credit transfers and the cheques should be treated alike judicially.[63]

CFI Trust v Royal Bank of Canada 2013 BCSC 1715 (18 September 2013)

This is a first instance decision of Myers J of the Supreme Court of British Columbia. The Court declined to follow the decision in *Flexi-Coil*. CFI provided financing to Totem Ford ('Totem'). Motor vehicles were leased by Totem to customers. Totem permitted 242 customers to terminate their finance contracts with it early and received from its customers early termination fees totalling $5.97 million. Totem failed to repay those funds to CFI and instead paid the early termination fees into its operating account with the Royal Bank of Canada ('RBC'). RBC debited Totem's operating account to reduce an operating line of credit whenever the line of credit was in a negative balance. RBC financed Totem's floor plan and held a registered general security agreement. CFI also had an earlier registered security agreement but had entered into a priority agreement with RBC.

There were two issues before Myers J. First, CFI claimed the early termination fees as proceeds under its security agreement. Secondly, it argued that the funds were trust funds and RBC was liable to account to it in knowing receipt and unjust enrichment. In either case, CFI claimed it was entitled to trace the early termination fees as proceeds. Myers J did not accept CFI's claims. The unjust enrichment failed because RBC was a bona fide purchaser for value. The claim based on s 31(3) of the *Personal Property Security Act* RSBC 1996 ('*BCPPSA*') (*AustPPSA* s 69 equivalent) partly failed. Myers J found that RBC had priority in respect of lease payments because of the existence of a priority agreement and, also, because the payments were received by cheque. RBC was not accorded priority in respect of payments received by electronic funds transfer. The case is interesting because of the *BCPPSA* s 31(3) issue. *BCPPSA* s 31(3) is equivalent to the Saskatchewan provision considered in *Flexi-Coil*.

In the course of his analysis Myers J stated that *Flexi-Coil* focused on the issue of the account being in negative balance.[64] He said that in *Flexi-Coil* when the account

63 *Flexi-Coil* 107 DLR (4th) 129, [50].

64 *CFI Trust* 2013 BCSC 1715, [185].

is an overdraft account, no property right (proceeds claim) arises because the customer is the debtor of the bank but when the account is in credit, cheques paid in are proceeds because the bank is in a debtor relationship with the account holder.

Myers J found that because of the RBC system, Totem's account was never in a negative balance and could never be in negative balance unless Totem impermissibly attempted to exceed its loan limits.[65] Myers J found that RBC had priority for the cheques despite its knowledge of the security agreement in favour of CFI. In relation to the payments to RBC by electronic funds transfer ('EFT'), Myers J declined to follow *Flexi-Coil* and approached the question on the basis of statutory interpretation. Because the definition of instrument did not include the word 'account' Myers J concluded that an EFT was not an instrument for the purposes of *BCPPSA* s 31(3) and it was up to the legislature to fill the gap.[66]

The Stiassny Decision in the NZ Court of Appeal

The case is of interest to unsecured creditors, competing secured parties, receivers, administrators and liquidators. The decision concerned a dispute between the Commissioner of Inland Revenue and the receivers and managers of two partners in a partnership called Central North Island Forest Partnership ('CNIFP') involving The Forestry Corporation of New Zealand ('FCNZ') and CITIC New Zealand Limited ('CITIC') in relation to a payment by cheque in respect of a GST liability. The receivers and managers had been appointed by the Bank of New Zealand ('BNZ') to each of the individual members of the partnership and not to the partnership itself. *Commissioner of Inland Revenue v Stiassny*[67] involved a strike out action by the Commissioner in relation to a recovery action by the receivers of a payment of a GST[68] debt of NZ$127.5m mistakenly made by them following the sale of substantial forestry assets in 2003. CITIC traded in partnership in the name of CNIFP. A syndicate of banks had provided funding to CNIFP. The syndicate held security over the individual assets of the two partners FCNZ and CITIC. BNZ (one of the syndicate) appointed Stiassny and Graham as receivers and managers of the collateral owned by FCNZ and CITIC but not to the partnership itself. Effective 26 February 2001, FCNZ and CITIC appointed one of the two receivers as their representative to CNIFP's board.

In October 2003 CNIFP sold all of its assets for US$621m plus GST of NZ$127.5m. The sale proceeds were insufficient to repay the secured debts and the GST. The deed evidencing the sale provided for the sale proceeds to be deposited to the CNIFP bank account. The receivers were concerned that they might be personally liable for the GST and therefore drew a cheque on their receivers account styled 'For Central North Island Forestry partnership (Receivers A/C)' for the GST amount and paid it to the Commissioner. The receivers then sought to recover the payment as they had paid it in the mistaken belief that they were personally liable for the GST.

65 Ibid [187].

66 *CFI Trust* 2013 BCSC 1715, [212]–[217].

67 [2013] 1 NZLR 140.

68 Payable under the *Goods and Services Tax Act 1985* (NZ) ('*GST Act*').

In the High Court,[69] Allan J found that the receivers were not personally liable for the GST. He further held that as the payment was made by CNIFP from its own funds by negotiable instrument, *NZPPSA* s 95 had the effect of giving the Commissioner priority ahead of the secured creditors. A third finding was that *NZPPSA* s 95 did not preclude an in personam claim against the Commissioner for the recovery of the GST. These three findings were the subject of an appeal to the Court of Appeal.

The Court of Appeal found that the receiver was not personally liable as the activity in question related to CNIFP and not the two entities over which they had been appointed receivers.[70] In other words CNIFP was not the incapacitated entity referred to in s 58 of the *GST Act*. Therefore the receivers could not be agents for CNIFP for GST purposes but they were agents for the chargors under the terms of their appointment by BNZ. The deed of charge contained the usual provision that the receiver was agent of the chargor.

The central question was whether *NZPPSA* s 95 conferred priority on the Commissioner ahead of the secured creditors. The Court of Appeal agreed with Allan J that the purpose and effect of *NZPPSA* s 95 was:

> [T]o facilitate ordinary trade and commerce by ensuring that a creditor who receives payment of a debt in the manner stipulated by s 95(3) takes priority over any security interests in the funds so paid, the intangibles that were the source of the payment, and the negotiable instrument itself. Such priority arises whether or not the creditor had knowledge of the security interest at the time of payment . . .[71]

In analysing the position under *NZPPSA* s 95, the Court of Appeal said that the legal ownership of the proceeds of sale was in CNIFP subject to the security interest of the secured creditors. But relying on *NZPPSA* s 24, which provides that the *PPSA* does not rely on notions of title, the Court of Appeal said this did not matter so long as the debtor-initiated payment to the creditor is accorded priority by force of *NZPPSA* s 95 over a security interest in the funds paid.[72] The bank account of CNIFP was the intangible and source of the payment and the negotiable instrument was the cheque used to effect payment.[73] If title to the payment was relevant, then the purpose of *NZPPSA* s 95 would be defeated.[74] Thus if CNIFP itself made the payment in the manner effected, then *NZPPSA* s 95 would operate to give priority to the Commissioner.

The Court of Appeal also referred to the trial judge's comments that 'Secured parties should not be given the power to prevent debtors from paying other creditors out of

69 *Stiassny v Commissioner of Inland Revenue* [2010] NZHC 2351.

70 *Commissioner of Inland Revenue v Stiassny* [2013] 1 NZLR 140.

71 Ibid [62].

72 Ibid [59].

73 Ibid.

74 Ibid [60].

liquid assets held by them. If this were allowed, great disruption in commercial activity would result.'[75] The section and its effect is equivalent to 'the power of a debtor under prior law to pay it creditors where the debtor had given an uncrystallised floating charge.'

The Court of Appeal further said (agreeing with the trial judge) that 'issues as to whether the security interests had crystallised and whether the payment was made in the ordinary course of business are not relevant to the operation of s 95' (*AustPPSA* s 69).[76] As pointed out above, the justification for these provisions is the policy expressed in *Flexi-Coil*.

The Court of Appeal then went on to consider the question: does *NZPPSA* s 95 apply where a receiver has been appointed? It was argued that receivers were appointed to FCNZ and CITIC and that the receivers had control of the normal business of CNIFP. On this basis the payment was not debtor-initiated but rather a payment initiated by a creditor as an act of enforcement of its security interest. This argument was rejected on the basis that while the receivers were in control of the FCNZ and CITIC ('CNIFP'), they were at all times agents for the partnership member companies. The payment was from funds owned by CNIFP with the consent of BNZ on behalf of the syndicate members. The fact that the receivers thought they might be personally liable for the GST made no difference. Also, even though the Commissioner had notice of the security itself at the time it received the GST payment this did not affect the priority afforded to the Commissioner in respect of a debtor-initiated payment because of *NZPPSA* s 95(2).[77]

The Court of Appeal's decision confirms the position that *NZPPSA* s 95 deals with priority of payments that are debtor-initiated and does not prevent in personam claims, such as a claim for a payment made under mistake. Importantly, *NZPPSA* s 95 operates to protect a creditor whether he or she is secured or unsecured and whether or not he or she has notice of the security interest granted by the debtor in favour of a third party.

Notwithstanding the Court of Appeal's view, *NZPPSA* s 95 had no application on the facts because the payment was made from the moneys belonging to CNIFP and it was made with the consent of the secured party banks. Further, it appears that the syndicate of banks did not hold security over the assets of the partnership that included the partnership account; rather they held security over the interests of each individual member in the partnership. This point seems to have eluded counsel who acted in the appeal.[78] Despite the reach of *NZPPSA* s 95,

75 Ibid [36].

76 Ibid [66], [69].

77 Ibid [69].

78 Blanchard J at [2] referred to this as a 'potentially important issue' which was not argued in the Supreme Court appeal. The effect of the security being over the aliquot interest of each member of the partnership meant that the secured parties only had a right to whatever was owed to the individual members on the dissolution of the

a debtor-initiated payment is subject to the preferential claims regime on the insolvency of the debtor.[79]

Stiassny v Commissioner of Inland Revenue in the NZ Supreme Court[80]

The Supreme Court dismissed the receivers' appeal in relation to the debtor-initiated payment of the GST essentially on the same basis as the Court of Appeal. The decision of the Court was given by Blanchard J who began by stating that '[a]ny payment made by or on behalf of the debtor from the proceeds of sale of the collateral is a debtor-initiated payment for the purposes of s 95.'[81] Blanchard J went on to endorse the policy reasons for the existence of *NZPPSA* s 95 and said that if a secured creditor could reclaim payments made by a debtor, it would be difficult for the debtor to obtain credit.[82]

NZPPSA s 95 can therefore be seen as operating in circumstances where the partnership was insolvent as there was nothing in the section that disqualifies a payment made during an insolvency, nor was there a requirement that the payment be made in the ordinary course of business. Despite these statements, Blanchard J said that as a practical matter payments made out of the ordinary order in an insolvency would not be covered by the section without good reason.[83]

The receiver argued that the Commissioner could not rely on *NZPPSA* s 95 because he had actual knowledge or notice of the terms of the security agreements as well as notice of the competing claims of BNZ and CNI. Knowledge of the existence of the security agreement is not sufficient to remove the protection of the section. Blanchard J said that this:

> must be taken to include also any knowledge the creditor had of the terms of the competing security interest. But the protection of that provision would not extend to a creditor with actual knowledge or notice at the time of receipt that a payment is being received in breach of the security agreement. (A creditor could in fact have gained knowledge or notice of a breach without necessarily becoming aware of the detailed terms of the security agreement.)[84]

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partnership. This meant that the secured parties' security was essentially illusory as they were in effect secured shareholders or unitholders/beneficiaries in the case of a trust. See *United Builders Pty Ltd v Mutual Acceptance Ltd* (1980) 144 CLR 673, 679 (Stephen J). A charge taken by a lender over the assets of individual members of a partnership rather than the partnership assets themselves was fatal in *Bailey v Manos Breeders Farms Pty Ltd* South Australian Supreme Court (Unreported, Full Court Supreme Court of South Australia, 4 April 1991); BC910048.

79 See comments of Blanchard J in *Stiassny* at [54].

80 *Stiassny v Commissioner of Inland Revenue* [2013] 1 NZLR 453 ('*Stiassny No 2*').

81 *Stiassny No 2* [2013] 1 NZLR 453, [52]. A payment by an agent is not 'debtor initiated' within the section. See below under XII Receivers.

82 Ibid [53].

83 Ibid [54].

84 Ibid [57].

Blanchard J went on to say that the Australian provision states expressly that the subsection does not immunise the creditor against knowledge of a breach and that in the Court's view *NZPPSA* s 95(2) implicitly has the same limitation. Clearly this is incorrect as *NZPPSA* s 95 states that the section "*applies whether or not the creditor had knowledge of the security interest at the time of the payment*".

The Court said by way of *obiter dictum* that the test of whether a creditor had knowledge was an objective one. The question is what did the Commissioner objectively know at the time of receipt? The Court found that the Commissioner knew nothing more than that the BNZ and CNI had competing claims to the GST payment.[85] No inference was to be made that this meant the Commissioner knew it was a breach of the terms of the security agreements at the time of the payment. This was not enough to disentitle the Commissioner to rely on the protection afforded by *NZPPSA* s 95.

Blanchard J said, by way of an obiter dictum, with respect to knowledge that 'the sense of the section is consistent with s 53 which provides for a buyer or a lessee of goods sold in the ordinary course of business to take them free of a security interest over them unless the buyer or lessee knows that the sale or lease constitutes a breach of the security interest'.[86]

The policy in relation to the transferee or cut off rules is different to the policy underlying the payment of a debt. The reason why a buyer or lessee takes free is because the inventory financier expects the goods to be sold in the ordinary course of the debtor's business. In the interests of commercial certainty and the flow of commerce, a retail buyer or lessee of inventory should not have to search the register as it would have the effect of impeding commerce. A buyer or lessee would expect that a bank or other financier has financed the floor plan but he or she expects to buy free of that security interest. This is not the case if he or she knows that the sale is forbidden.[87] Grant Gilmore suggests that the reason for the rule is that a secured party expects that the retailer will sell the personal property subject to the security interest and the loan or part or the loan will be repaid from the proceeds of sale.[88]

Despite the clear wording in *NZPPSA* s 95(2), it is plainly not open to a court to interpret a section of legislation by adding words (where the wording of the section is to the contrary) by reference to what is contained in another section of the same legislation or in light of what is contained in the same or similar legislation of another jurisdiction.

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85 Ibid [58].

86 Ibid [57].

87 Cuming, Walsh and Wood, above n 6, 385. See generally Clark and Clark, above n 26, [3.04].

88 Grant Gilmore, *Security Interests in Personal Property* (Little, Brown and Company, 1965) vol 2, 677.

VII Protected Transactions: Australian And New Zealand Contrasted

This part considers whether or not there is any substantial difference in interpretation of the *AustPPSA* and *NZPPSA* in light of the stylistic differences in drafting between the provisions. *AustPPSA* s 69 is drafted differently to *NZPPSA* s 95. It differs in three respects:

(1) It does not use the expression 'debtor-initiated payment'. It refers to a payment made by a debtor.
(2) It qualifies security interest with the words '(whether perfected or unperfected)'; [89] and
(3) Subsection (2) provides that 'subsection (1) does not apply if, at the time of the payment, the creditor had actual knowledge that the payment was made in breach of the security agreement that provides for the security interest.'

However, apart from the question of a no knowledge requirement in *NZPPSA* s 95(2), the New Zealand and Australian provisions are essentially the same: both deal with payment by a debtor by way of instrument or electronic funds transfer or other debit order, authorisation or similar written payment mechanism, at the time payment is made. The Australian, New Zealand and Saskatchewan provisions, only sanction payments by negotiable instrument, electronic funds transfer or debit authorities initiated (executed) at the time of the payment. Logically, therefore, they exclude automatic debt authorities of the type usually employed by creditors in Australia and New Zealand.[90]

The limitation in *AustPPSA* s 69(3)(b) to a debit, transfer order, authorisation or similar written payment mechanism executed by the debtor when the payment is made is designed to prevent abuse. It would eviscerate the secured party's security interest.[91]

The upshot of this limitation appears to be that a debtor cannot consent in advance to deductions from an account by way of automatic debit, automated BPAY payments (whether from credit accounts or credit card accounts) and letters of credit. Further post-dated cheques, bills of exchange payable to a future date, purchase of a bank cheque to pay a creditor or the like would all seem to be outside the scope of the sections. A cheque drawn by a third party payable to the debtor and endorsed to a creditor also will not qualify as a debtor-initiated payment as the drawer is the third party not the debtor.[92]

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89 An unregistered security interest will not affect the payment except on the insolvency of the debtor.

90 See below in relation to the Manitoba provisions.

91 *Sparrow* [1997] 1 SCR 411 (Iacobucci J).

92 Cuming, Walsh and Wood, above n 6, 407; Gedye, Cuming and Wood, above n 19, [95.1].

Similarly, a set off provision or right to combine accounts contained in a facility agreement or bank authority or otherwise would not be permitted if pre-arranged.[93] But it could be if a set off letter was signed at the time of payment. This is because it would be within the section as 'an authorisation . . . executed at the time of when the payment was made'. Again this highlights the policy of the *PPSA*s to ensure that a debtor has the ability to pay his or her creditors. If he or she is unable to do so, he or she will cease to be able to carry on business. He or she will not be able to obtain other goods, nor will he or she be able to obtain secured or unsecured credit.

If one allows automatic debit authorities, one difficulty is that banks can defeat the proceeds interests of inventory financiers by requiring them to bank all moneys, whether by cheque or cash, from the sale of inventory into trading accounts with them that are generally in debit balance. The bank is then able to sweep those proceeds in reduction of the debit balance or against another obligation owed to the bank, such as under a lease purchase agreement or term loan facility[94]. In *Flexi-Coil,* Jackson JA said that this requirement 'would significantly affect the priority given to inventory suppliers . . . This was of concern to the Court, but since the Court did not have before it any evidence of such dealings, this issue is best left to another day without further comment'.[95] This is of greater concern in Australia where an ADI is able to take a security interest in the bank account of its customer and perfect by control.

VIII Knowledge

The New Zealand provision, consistently with the Canadian *PPSA* statutes, provides that knowledge of a security interest given by the debtor in favour of a third party does not affect the status of the payment, but according to the NZ Supreme Court in *Stiassny*, actual knowledge that the payment when received was in breach of the security agreement will. *AustPPSA* s 69(2) is at odds with the New Zealand and Canadian provisions. It provides that the payment will not be 'immunised'[96] if the recipient had actual knowledge that the payment was made in breach of the security agreement. The reason is mystifying but it is thought that the Attorney-General's Department failed to understand the policy difference between the purchaser of an instrument in the ordinary course of business and the policy behind the need to protect creditors of a debtor.[97]

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93 Caldwell, above n 11, 172.

94 Effectively this is what occurred in *CFI Trust* as under the operating loan system revolving multiples of $10,000 were automatically transferred at the end of each business day to pay down the loan so that the account from which payments were made was never in a negative balance.

95 *Flexi-Coil* (1993) 107 DLR (4th) 129, [52].

96 [2013] 1 NZLR 453 (Blanchard J). See also discussion above.

97 The *Replacement Explanatory Memorandum on the Personal Property Securities Bill 2009* (Cth), does not provide any reason for this policy choice other than to state that what is contained in s 69(2): [2.158].

If the integrity of the payment system and business efficacy is to be preserved, knowledge should not matter, subject to questions of preferential payment on the insolvency of the debtor. The knowledge requirement is also at odds with Article 9 of the UCC. UCC Article 9 is much simpler in its terms: a transferee of money or of funds from a deposit account takes the funds free of a security interest or the security interest in the deposit account unless the transferee acts in collusion with the debtor in violating the rights of the secured party.[98] The collusion test is seen as more protective of transferee unsecured creditors who receive payment of a debt from a bank account. Unless collusion occurs which has the effect of violating a secured party's claim to proceeds deposited to the bank account the general creditor payee prevails. The collusion test makes it more difficult for a secured party to challenge the debtor payment that would otherwise be the case if the test was simply one which required proof of a payment made with knowledge that the payment violated the rights of a secured party under the security agreement.

As discussed above, the Supreme Court in *Stiassny* provides some guidance on the meaning of 'knowledge of a security interest' and 'actual knowledge that the payment was made in breach of the security agreement'. This guidance is limited to the formulation of an objective test of what the recipient creditor understood at the time of receipt of the payment and no more.

Further guidance can be found in some of the Canadian cases, notably, *Belarus* and *CFI Trust*. Notice of the existence of a security interest will not be sufficient to remove protection as the test is too low. In *Belarus* (Alberta), Master Funduk stated that actual knowledge is required. Actual knowledge is not defined in any of the *PPSA*s. Where there is no statutory definition of actual knowledge the common law test will apply.[99] Cuming and Wood say that mere knowledge of the existence of a security interest would paralyse a business as no one could deal with the debtor in the ordinary course of business without the consent of the secured party.[100]

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98 UCC § 9-332(a) and (b). A classic example of a buyer who had actual knowledge that the sale was a breach of the terms of the security agreement occurred in *Quinn v Scheu* 675 P2d 1078, 38 UCC Rep 367 (Oregon CA 1984). In this case the court found that a holder of a perfected security interest in respect of a printer's inventory of books defeated a buyer in due course. This was because the buyer was an author for whom the printer produced books under an earlier contract in circumstances where the secured party sent a notice to that buyer to pay the secured party who was an assignee of printer's accounts. Patently, collusion may consist of an act where a buyer was also intending to acquire the business. The same would likely obtain where a special relationship existed between a employee of the seller and a buyer. See Clarke, above n 26, 3.04(1). The receipt of the notice of assignment by Quinn was knowledge imputed to his partner-father which was seen as being adequate as a matter of law to inform the plaintiff that payment to anyone other Heller would violate Heller's security agreement.

99 Duggan and Brown, above n 6, [10.19]; Cuming, Walsh and Wood, above n 6, 55–59.

100 Cuming and Wood, above n 23, 236, Caldwell, above n 11, 186.

The expression with 'actual knowledge that the payment it was in breach of the terms of the security agreement', appears to mean that the person relying on the section must in fact know the underlying transaction to each cheque before it can be said he or she has actual knowledge.[101]

In *Belarus,* Master Funduk said that:

> Certainly, a banker might speculate about what a cheque is for and he might even be on the mark in his speculation. But that is not what subs. (4.1) is about. Speculation is not knowledge. He must know that the cheque is the sale proceeds of collateral that is subject to a security interest. Nothing less will do.[102]

Section 4.1 states that a person 'has knowledge only if he acquired his interest with knowledge that the transaction violated the terms of the security agreement creating or providing for the security interest.'[103]

These statements on the meaning of knowledge in *Belarus* were expressly adopted by Myers J in *CFI Trust.* Myers J said:

> I agree with Belarus. Knowledge of the existence of a security agreement with a bank's customer is not enough to disentitle the bank from relying on the protection afforded by s 31(3). There must be knowledge that the transaction violates the terms of the relevant security agreement.[104]

While the statements assist with an understanding of the requirement of knowledge, they do not really assist an unsecured creditor or purchaser in relation to other transactions covered by these special priority rules designed to protect unsecured creditors or buyers and lessees. The differing requirements discriminate between the types of transactions rather than being a uniform requirement. Part of this problem can be explained by the deliberate use of the words 'personal property' in place of 'goods' in most of the transferee rules in Part 2.5 of the *AustPPSA*. The use of the term 'personal property' means that there is a substantial overlap between the differing provisions. For convenience, the following table illustrates the inconsistencies.

101 *Belarus* (1995) 24 Alta LR (3d) 125, [128].

102 Ibid.

103 Ibid [27].

104 *CFI Trust* 2013 BCSC 1715, [206].

Knowledge requirement table

Section	Knowledge requirement
43 — unperfected SIs	None
44 — incorrect or missing serial number	None
45(1) — motor vehicles — incorrect or missing serial number	Actual or constructive knowledge of the security interest
45(3) — prescribed persons	Actual or constructive knowledge of breach of security agreement[105]
46 — ordinary course of business	Actual knowledge of breach of the security agreement
47 — consumer transactions	Actual or constructive knowledge of breach of security agreement
48 — currency	Actual or constructive knowledge of the security interest
49 — investment instruments or intermediated securities in ordinary course of trading	None
50 — investment instruments	Actual or constructive knowledge of breach of security agreement
51 — intermediated securities	Actual or constructive knowledge of breach of security agreement
52 — temporary perfected security interests	Actual knowledge of breach of the security agreement

IX Debtor-Initiated Or Not?

The *PPSA* requires that the transfer or payment is debtor-initiated so that if the debtor uses its own funds to obtain a bank cheque that is then used to pay a creditor the bank cheque will not qualify as a debtor-initiated payment.[106] The payment would be proceeds under *AustPPSA* s 31 (*NZPPSA* s 16) and therefore traceable and

105 This requirement is correct policy. In the case of unperfected security interests (AustPPSA s 43), the absence of a knowledge requirement is designed to encourage secured parties to perfect by registering financing statements. In the case of s 44, the rule is designed to encourage the inclusion of a serial number in the financing statement.

106 Note 3 to UCC § 9-332 official commentary.

recoverable by the secured party whose security interest extends to the ADI account of the debtor. The reason for this is that the payment is by means of the bank cheque drawn by the bank, not a cheque drawn by the debtor. The bank cheque is proceeds of the debtor's account.[107]

Although there is a general test for knowledge in the *PPSA*s for the purposes of the priority and transfer rules in particular, it has no place in circumstances where the provision itself is intended to replicate the existing law. In relation to cheques and other negotiable instruments a purchaser (holder) is one who takes free of equities. A holder for value and without notice of defects in the transferee's title takes free of equities.[108] What this means is that it is possible in the ordinary course of transferring rights in a negotiable instrument to pass a better title to the holder or transferee than the one held by the transferor. A bank cannot be a holder where it collects a cheque as agent for the payee.

The proper place for the requirement replicated in *AustPPSA* s 69(2) is s 70 (*NZPPSA* s 96). *AustPPSA* 48 deals with currency (money) (*NZPPSA* s 94). The New Zealand provision replicates s 31(1) of the Saskatchewan legislation. A modification of the example given at the end of *NZPPSA* s 94 is the use of money to buy a computer that represents the proceeds of the sale of cars subject to a security interest in inventory and their cash proceeds. The vendor of the computer takes-free even though the cash is proceeds and would be subject to a perfected security interest. The purpose of this provision is to ensure that the rights of the holder for value of the money (the vendor of the computer) are not interfered with by the *PPSA*.[109] The problem with *AustPPSA* s 48 is that it confuses the policy goal, as it fails to provide that the holder acquires the currency whether or not he or she had knowledge of the security interest.[110]

Despite the above comments, our present inquiry does not relate to the acquisition of an instrument or currency in the ordinary course of business. The purpose to which *AustPPSA* s 69 is directed is the payment of unsecured creditors generally. This point seems to have eluded the draftsperson when *AustPPSA* s 69(2) was drafted.

X Excluded Transactions

As Cuming, Walsh and Wood point out the excluded transaction provision exists to enable a debtor to pay his or her debts and the creditor will take free of the security

107 Cuming, Walsh and Wood, above n 6, 407.

108 Cuming, Walsh and Wood, above n 6, 382. See also E P Ellinger, E Lomnicka and C Hare, *Ellinger's Modern Banking Law* (Oxford University Press, 4th ed, 2006), 353; Alan Tyree, *Banking Law in Australia* (LexisNexis, 6th ed, 2008), [4.10].

109 Cuming and Wood, above n 23, 243.

110 This can be partly attributed to the failure of the draftsperson to differentiate between a holder who takes money if the holder (1) acquired the money without knowledge of the security interest or (2) is a holder for value where knowledge does not matter. See *NZPPSA* s 94 and *SaskPPSA* s 31(1).

interest so long as the transaction is one by the debtor, whether or not the creditor is aware of a security interest or that the payment might be in breach of it.[111] 'The provision has the effect of empowering a debtor to use a negotiable instrument to pay debts, even though, as property of the debtor, the instrument is subject to the security interest.'[112]

The section seems to be limited in its ambit. It will not apply to the following:[113]

(a) an automatic debit that is not made at the time of the payment, thus excluding debit authorities signed at the time of a loan facility as the required method of payment by the lender bank;
(b) a cheque payable to the debtor that is subsequently endorsed to the creditor;
(c) a bank account upon which is cheque is drawn by the debtor;
(d) an instrument not paid at the time a secured party enforces in respect of the account (a cheque is conditional payment until paid).

XI Manitoba Provisions

According to Cuming and Wood[114] the Manitoba *PPSA* was amended to include a number of additional excluded transactions designed to enable a bank to debit a customer's account in disregard of a security interest that another secured party might have in that account. Despite the obvious exclusions, the Manitoba *PPSA*[115] sets out a number of transactions that qualify as statutory protected 'debtor-initiated' transactions where a third party secured party holds a security interest in the account. These include:

(a) a payment between accounts in the same financial institution, initiated by the debtor at the time the debt is payable or thereafter. This would include a payment from a deposit account to repay a term loan facility or other credit transaction;
(b) the repayment of an overdraft account by specific authorisation where demand has been made;
(c) payment effected through a post-dated cheque.

A payment via post-dated cheque will be subject to the same limitation where the security interest in the account is enforced before the date for presentment and actual payment. It is also subject to the written authorisation signed by the debtor specifying the amounts and the times or intervals of the payments, or the authorised

111 Cuming, Walsh and Wood, above n 6, 408.

112 Ibid, 407.

113 Ibid, 384.

114 Cuming and Wood, above n 23, 245.

115 *Manitoba Personal Property Security Act* 2012 CCSM c. P35, s 31(3).

debit being paid from a credit balance that exceeds the amount of the debit.[116] In respect of the last point, the view of Cuming and Wood is that it will apply to a revolving loan arrangement under which the agreement between the 'depositor and the deposit-taking institution provides that when the amount in the account drops below a certain amount the institution will credit the account so as to bring it up to that amount, but if through deposit credits in the account exceeds the amount, the excess will be taken by the deposit-taking institution in payment of the debt owing to it under the arrangement.' [117] Debits authorised by an ADI as agent of the debtor are excluded from the special priority given by Manitoba *PPSA* s 31(2).

A troubling aspect of *AustPPSA* s 69 for banks is that absent equivalent provisions to the Manitoba provisions permitting payments by automatic debit, any expansive reading of *AustPPSA* s 69(3)(a) would be tantamount to allowing a banker's set off.[118] In the *Transamerica Commercial Finance Corp Canada v Royal Bank of Canada* case,[119] the RBC, that held a security interest from its account holder, applied receipts to its customer's current account in reduction of the customer's loan debt to it. Some of those moneys were purchase money security interest ('PMSI') proceeds of inventory that had been deposited to the customer's current account with the bank. The Saskatchewan Court of Appeal found there was no evidence that the bank was the recipient of money that was deposited to the current account (the proceeds of inventory were paid to the debtor's account with it), nor did the bank receive an instrument drawn and delivered by the debtor to it. Consequently, the equivalent to *AustPPSA* s 69 (*NZPPSA* s 95) did not apply. The PMSI financier had priority for the proceeds as it could trace the inventory to the proceeds paid into the bank account.

Jacob Zeigel and David Denomme point out that had the Court of Appeal given an expansive reading of the section, effectively permitting set off, this would seriously undermine the purchase money financier's claim to proceeds.[120] As discussed below, this issue may not arise in Australia where an ADI has control of the relevant accounts with it. An ADI's super priority because of *AustPPSA* s 57 will trump a security interest (which includes a PMSI) perfected by any other means.[121]

116 This provision would sanction automatic debit authorities.

117 Cuming and Wood, above n 23, 245.

118 According to RCC Cuming, 'Security Interests in Accounts and the Right of Set-Off' (1990) 6 *Banking and Finance Law Review* 299 at 310, the case law in the USA appears to support the position that set-off cannot be exercised so as to defeat a security interest in proceeds except where there the account is original collateral.

119 (1990) 70 DLR (4th) 627, 636.

120 Jacob D Ziegel and David L Denomme, *The Ontario Personal Property Security Act Commentary and Analysis* (Butterworths, 2nd ed, 2000) § 25.4.8.3.

121 One solution for the inventory financier might be to enter into a blocked account agreement with the ADI to ensure that the inventory financier gets the sale proceeds of his or her inventory in priority to any claim by the ADI.

Although the additional Manitoba provisions do not exist in the New Zealand or Australian legislation, it is possible that an Australian court faced with a factual situation involving any one of these scenarios might interpret *AustPPSA* s 69 as protective of one of those types of additional debtor payments. This would replicate the approach taken in *Flexi-Coil*.

XII Interaction Between The Debtor Payment Provisions And The Perfection By Control Rules

There is a significant interaction between the debtor-initiated payment provisions and the perfection by control rules. The debtor-initiated provisions, except in the case of Manitoba, were designed to prevent a bank from obtaining priority over an inventory supplier by use of automated debt authorities or other pre-authorised transfer orders used by banks to sweep funds from debtor trading accounts to debtor loan accounts with the bank.[122]

In Australia, in particular, as well as in America by virtue of Article 9, perfection by control of a bank account is permitted. An ADI under the *AustPPSA* is able to take a security interest in the deposit account[123] and perfect it by control.[124] Potentially, this gives a bank a super priority over the PMSI claim of the inventory supplier even though the bank may have actual notice of the PMSI security interest. For policy reasons, and to ensure a level playing field, the current position is untenable as it gives the bank a super priority because of its status as an ADI. Absent this special status a bank will not be able to assert any set off rights if it has actual notice of a competing secured party's inventory security interest or security interest over the debtor's bank account. If it controls the ADI account of its debtor it has priority simply because of its status as an ADI. The New Zealand, Saskatchewan and Manitoba *PPSA*s do not presently provide for perfection by control of bank accounts and therefore banks in these jurisdictions do not enjoy this privileged position.

As a result of the ability of an ADI to take security over a bank account of its debtor, it will be in a superior position and be able to defeat any debtor-initiated payment. An ADI security interest is automatically perfected by control under *AustPPSA* s 25. This security interest will have priority over any other security interest in the ADI account under *AustPPSA* s 75. The ADI will also have priority because of *AustPPSA* ss 21(2) and 57.

If the debtor has granted a security interest in his account to his ADI, the ADI will necessarily have priority over any proceeds deposited to the account by its debtor.[125]

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122 This limitation should remain but is effectively cancelled out because of the super priority given to banks that are able to control ADI accounts.

123 *AustPPSA* s 12(4)(b).

124 *AustPPSA* ss 57(1), 21(2)(c)(i), 25.

125 Roderick J Wood, 'Acquisition Financing of Inventory: Explaining the Diversity' (2013) 13 *Oxford University Commonwealth Law Journal* 49.

An ADI will therefore be able to defeat a creditor who receives a debtor-initiated payment by enforcing its ADI security interest or by set off, unless it has actual notice of competing secured party's interest in the account and/or its proceeds. An ADI will also be able to defeat a garnishee order or an ATO garnishee notice because the interest is a fixed statutory interest not a floating charge interest.[126] As a result of the ADI control account security interest and set off, a creditor will not be protected by s 69 until actual payment of his or her debt.

A feature of s 25 is that an ADI has control simply by being an ADI.[127] This is to be contrasted with the Article 9 provision which provides that control occurs automatically if a debtor has granted a security interest in favour of the bank which covers the account.[128] Under the UCC § 9-340(a) a bank's right of set off has priority over a security interest held by another secured party. The position is different if the third party secured party has a control agreement with the bank in respect of the debtor's deposit account.[129] Here a secured party obtains priority for proceeds of accounts deposited into a bank account.[130]

XII Receivers

In *Stiassny*, both the New Zealand Court of Appeal and the Supreme Court decided that the payment initiated by a receiver as agent for the debtor was covered by *NZPPSA* s 95. The better view is that this is not correct. An authorisation by an agent is not the same. If the same facts came before an Australian court it is likely that the result would be different. First, the definition of 'debtor'[131] in *AustPPSA* s 10 does not include a receiver or agent of the debtor. Secondly, a payment by a receiver

126 Cf *Commissioner of Taxation v Park* [2012] FCAFC 122.

127 The requirements of control in *AustPPSA* ss 341 and 341A only apply in respect of circulating assets. See Duggan and Brown, above n 6, 5.23–5.24. It is implicit in *AustPPSA* s 25 that the ADI's customer must have granted a security interest to the ADI which covers ADI accounts. Despite this, *AustPPSA* s 25 should be amended to require a control account agreement to gain priority under s 75 over another secured party who has perfected by registration of a financing statement. The control account requirements in ss 341 and 341A should be moved to s 25.

128 UCC § 9-104. According to the Official Commentary, Note 3, all actual and potential creditors of the debtor are always on notice that the bank with which the debtor's deposit account is maintained may assert a claim against the deposit account. A secured party which is not a bank must enter into a control account agreement with the bank or become the bank's customer.

129 UCC § 9-340(c).

130 Clarke, above n 26, [3.11[1]]. As to the Australian position, see Rory Derham, *Derham on the Law of Set-off* (Oxford University Press, 4th ed, 2010) [17.58]–[17.59]. See also *AustPPSA* s 80 in relation to transfers of accounts and the right of set off.

131 The position is the same in respect of the term 'grantor' in s 10. *AustPPSA* uses the term 'grantor' idiosyncratically in place of 'debtor', which in itself causes confusion. The term 'grantor' is not used any of the other *PPSA*s.

is not a payment by the debtor as a matter of general law.[132] This is so despite the fact that, generally, the debenture charge or general security agreement will provide that a receiver or receiver and manager is agent of the debtor/grantor. After liquidation it will provide that the receiver is agent of the chargeholder or secured party because upon the making of the winding up order the agency ceases.[133]

During the course of a receivership, a receiver will open an account of his own with the ADI and bank all moneys received by him or her during the receivership to that account. The account established by a receiver will necessarily be the receiver's account and any cheques and other debits made to the account can only be made by the receiver. As a consequence, any payments made by the receiver from that account can only be characterised as payments by the receiver,[134] not the debtor. If made by a receiver, the payment would, in any event, be made with consent of the secured party and would therefore operate as a release. *NZPPSA* s 95 and *AustPPSA* s 69 could only apply if the security interest had not been enforced.

There is a further difficulty with the *Staissny* decisions: the receivers were receivers of FCNZ and CITIC, not CNIFP. Consequently, they were not agents of CNIFP. The Court of Appeal and the Supreme Court found that as the sale proceeds belonged to CNIFP, not FCNZ or CITIC, they were subject to the security granted by CNIFP.[135] The moneys were paid to the Commissioner from the partnership bank account in the name of the receivers. The receivers were agents of the two members of the CNIFP partnership. FCNZ and CITIC had appointed one of the receivers to the management board of CNIFP. Even if you accept that the payment was made from the sale proceeds belonging to CNIFP, the payments were made from an account of the receivers by the receivers not by the partnership itself.

The statement by Blanchard J that any payment made by or on behalf of the debtor from the proceeds of sale of the collateral is a debtor-initiated payment for the purposes of s 95 cannot be correct.[136] On this basis, if a case came before a Court here in Australia that considered the same fact situation as in *Stiassny*, *AustPPSA* s 69 may not be engaged if the characterisation of the account is as decided by the High Court in *Sheahan*.[137]

This is because in *Sheahan*, the High Court said that it was important to have regard to the source of the funds. Because the account was in the receivers name any payments from it could only be characterised as payments by the receiver and

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132 In *Sheahan v Carrier Air Conditioning Pty Ltd* (1997) 189 CLR 407, Dawson, Gaudron and Gummow JJ said (at 435) if the payments were from an account maintained by a receiver then it was correct to characterise them as payments made by the receiver. Brennan CJ agreed (at 421).

133 *Sheahan v Carrier Air Conditioning Pty Ltd* (1997) 189 CLR 407.

134 Ibid 435.

135 *Stiassny* [2013] 1 NZLR 140, [58]; *Stiassny No 2* [2013] 1 NZLR 453, [48].

136 *Stiassny No 2* [2013] 1 NZLR 453, [52].

137 Ibid.

no one else.[138] This is so despite the fact that the proceeds technically remained the property of CNIFP.[139] Nevertheless the payment to the Commissioner was made with the consent of BNZ on behalf of the secured creditors. Section 95, therefore, was not engaged as the payment was made with consent of the secured parties and hence operated as a release.

Apart from this, it is bewildering that counsel in *Stiassny* all the way through the various courts failed to analysis the legal position correctly. If the security taken by the BNZ and CNI was only over the aliquot share of each individual member of the partnership,[140] the secured parties did not have security over the partnership assets themselves that included the proceeds of sale in the bank account and as a consequence had no entitlement to the partnership moneys as secured creditors. Further, if the receivers were invalidly appointed they had no legal right or entitlement to make the GST payment to the Commissioner.

XIII CONCLUSION

One characteristic of the *PPSA* is its treatment of the priority rules. They generally provide clarity, predictability and certainty when contrasted with what was a foggy state of affairs under the prior law. But the poor drafting and policy choices in the *AustPPSA* sections considered in this article do not meet these requirements of clarity, certainty and predictability. Unsecured creditors appear to be in a slightly better position than they were under pre-*PPSA* law once payment by one of the methods stipulated has been made. However, this position is seriously undermined by the position given to ADI's by the *AustPPSA* through the ability to take a security interest in an ADI account kept with them that is automatically perfected by control.

We await with interest the likely outcome of the agitation of s 69 before an Australian court. In the meantime, it is hoped that the review incorporated in the *AustPPSA* by s 343 will bring some sense to the uninformed drafting by a view of the various knowledge requirements referred to above and repeal of s 69(2).[141] Knowledge of a security interest or a payment received with knowledge that it is in breach of the terms of the security agreement should not matter for the policy reasons stated above. The *SaskPPSA* s 31(2) has the balance right but this is not assisted by the decision of

138 Ibid 435 (Dawson, Gaudron and Gummow JJ).

139 [2012] 1 NZLR 140, [41]. See above n 72, where it was observed by the Court of Appeal, relying on *NZPPSA* s 24, that title did not matter.

140 See above n 78.

141 The review of the *AustPPSA* is to be undertaken and completed within three years after the registration commencement time (30 January 2012).

Stiassny in the New Zealand Supreme Court. The special priority rule should be the same as UCC § 9-332(b): 'A transferee of funds from a deposit account takes free of a security interest in the deposit account unless the transferee [creditor] acts in collusion[142] with the debtor in violating the rights of the security party.'

142 See *Banner Bank v First Community Bank* 854 F.Supp. 2d 846 (D.Mont. 2012). In this case where a debtor company's principals enabled a fraud on a first creditor where a second creditor knew that the debtor was bypassing the first secured party creditor's security interest by keeping the creditor completely in the dark about a potential bank conflict over the debtor's assets or about the possibility that the debtor might want to sell the encumbered assets. Cf *Keybank NA v Ruiz Food Products Inc* 59 UCC Rep. 2d 870 (D. Ida 2005); *Kentucky Highlands Inv Corp v Bank of Corbin* 60 UCC Rep. 2d 1307 (Ky Ct App 2006) where collusion was not found on the facts.