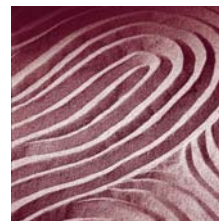
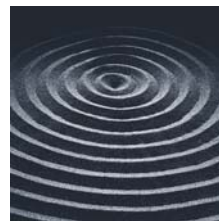


# MILLER THOMSON LLP

Barristers & Solicitors  
Patent & Trade-Mark Agents

Scotia Plaza  
40 King St. West, Suite 5800  
P.O. Box 1011  
Toronto, ON Canada  
M5H 3S1  
Tel. 416.595.8500  
Fax.416.595.8695  
www.millerthomson.com



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## PENDING AMENDMENTS TO THE ONTARIO PPSA

Jennifer E. Babe  
Miller Thomson LLP

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1. **Where Did These PPSA Changes Come From:**

There has been a long path to get to these Ontario Personal Property Security Act (“PPSA”) changes coming into effect on August first. A synopsis of the path follows:

1989: The PPSA, S. O. 1989 is enacted, updating the prior statute.

May 26, 1993: The Personal Property Security Law Committee of the Business Section of the Ontario Bar Association (the “PPSL Committee”) provided its submission to the Ontario government recommending changes to the 1989 PPSA (the “1993 Submission”).

Oct. 21, 1998: Submission by the PPSL Committee to the Minister recommending again the changes from the 1993 Submission which had not been enacted and providing additional specific reforms, for a total of 36 areas for reform.

2004: The secured transactions working group of the Commercial Law Strategy of the Uniform Law Conference of Canada (“ULCC”) studied five areas and recommended changes to increase uniformity among all 12 PPSA statutes and the Quebec Civil Code. These five areas are:

- (i) Conflicts of law;
- (ii) Proceeds arising from inventory v. receivables security;
- (iii) Anti Assignment clauses for financing receivables;
- (iv) Priority between *Bank Act* security and provincial security;
- (v) Security interest in licences.

see : [www.ulcc.ca/2003](http://www.ulcc.ca/2003) proceedings and a further report in the 2004 proceedings.

- 2004: The joint working group of the ULCC and the Securities Law Administrators produce the *Uniform Securities Transfer Act*, the result of about a decade of work (the “USTA”). see [www.ulcc.ca/2004](http://www.ulcc.ca/2004) proceedings.
- 2006: A working group from across Canada helps to draft the consequent PPSA amendments needed to enable the USTA, providing sample text for both the Alberta PPSA and the Ontario PPSA.
- Feb. 13, 2006: PPSL Committee requests that the Minister move forward on the 36 recommendations from 1998.
- April 28, 2006: PPSL Committee recommends to the Minister additional PPSA reforms to deal with the check box classification of collateral, rights to proceeds of inventory as against receivable financiers, conflict of law rules, and a permanent advisory committee to assist the Ministry to modernize the PPSA and keep it modern.
- May 8, 2006: The *Securities Transfer Act, 2006* (the “STA”) incorporating the consequent PPSA, OBCA and *Executions Act* changes, receives Royal Assent and is proclaimed into force January 1, 2007.
- May 19, 2006: PPSL Committee makes further recommendations to the Minister on the conflict of law rules. Many hours of discussions and comments were provided before the release of this submission.
- Aug. 1, 2007: With several exceptions, the majority of Schedule E to *An Act to modernize various Acts administered or affecting the Ministry of Government Services, 2006* (“Bill 152”) will go into effect.

References to the ULCC website is given as these materials provide an excellent analysis of the legal problems and the reasons for reform. Copies of the PPSL Committee’s submissions are attached to John Cameron’s paper on the STA delivered on February 6, 2007 at the OBA’s Mid Winter Institute session on The Ultimate Review of Key Issues in Business Law. The OBA has been asked to post these PPSL Committee submissions on

the Business Section's portion of OBA website, as they too provide excellent analysis of these legal issues.

## 2. **What Changes Does Bill 152 Make to the PPSA:**

John Cameron's paper today on the STA addresses the PPSA changes that came into effect January 1, 2007 to enable the STA. Comments on these STA changes to the PPSA are not duplicated here.

Ontario's PPSA is the oldest in Canada. The more recent PPSA statutes in Western Canada and Atlantic Canada have a great degree of uniformity in their content. The 2004 ULCC recommendations on five key areas focus on some of these differences.

Bill 152 helps bring Ontario's PPSA more in line with the other 11 PPSA statutes in effect in Canada and the Quebec Civil Code. To a large extent Bill 152 is "catch up" legislation moving Ontario ahead to match the Western and Atlantic PPSAs, and gives effect to more, but not all, of the PPSL Committee's recommendations in the 1993, 1998, and subsequent Submissions.

## 3. **Changes to the Registration System:**

### (a) **Elimination of Paper Registration Forms**

- see new definitions of "financing statement" and "financing change statement".
- see Part IV where there are revisions for the deletion of "branch offices" and "branch registrars", as only the central electronic registry is now needed.
- see Ontario Regulation 56/07 which on August 1, 2007 repeals Ontario Regulation 912, the general PPSA regulation.
- New Ministerial Orders have been prepared pursuant to section 73.1 of the PPSA and should be published in mid June 2007 and will go into effect August 1, 2007.
- We are told these new Orders will largely duplicate Regulation 912, but will delete the paper registration forms and processes.

(b) **To Come : Elimination of the “Check the Box” Collateral Description**

- Ontario had the first PPSA registry, created at a time when computer memory was expensive; hence the adoption of the Spartan “check the box” collateral description to save memory and cost.
- All other Canadian jurisdictions use a word description to describe the collateral claimed; Ontario is planning to move to follow the others.
- This change requires the government’s PPSA computer system to be altered and we are told that this infrastructure work may take at least two years.
- When it happens the change will come as a Ministerial Order under section 73.1 of the PPSA, amending the required content of a financing statement or financing change statement.

4. **More Changed Definitions:**

(a) **“debtor”**

- see section 1.
- This revised definition now allows a person who does not owe payment or performance of an obligation to the secured party, but does own or has rights to collateral, to provide a security interest to the secured party in that collateral as a “debtor”.
- This definition is found in other jurisdictions of Canada and is also a concept from the United States and will facilitate cross border deals.
- For example a shareholder could pledge his or her shares but not have granted any payment covenant, indemnity or guarantee with the secured party.
- Given that indemnities, guarantees and co-borrower obligations give secured parties additional rights than those provided to secured parties under Part V of the

PPSA, secured parties will likely continue to want the “debtor” to also enter into a guarantee, indemnity or like covenant with the secured party.

(b) **“motor vehicle”**

- This definition has not changed, but has been carried forward from repealed Regulation 912 into Regulation 56/07.

5. **Leases for a Term of More Than One Year**

- See also the revised definitions of “security interest” and “purchase-money security interest” which are expanded to now include “a lease for a term of more than one year”.
- See the new section 1 definition of “lease for a term of more than one year” which includes:
  - (a) A lease for an indefinite term even if one or more of the parties can terminate it inside one year;
  - (b) A lease for a term of one year or less if the lessee with the consent of the lessor retains uninterrupted possession for more than one year, but only when the possession does exceed one year; and
  - (c) The lease for one year or less if the lease is renewable for a total term in excess of one year; but does include
  - (d) A lease of goods by a lessor who does not regularly engage in the business of leasing goods; or
  - (e) A lease of household furnishings or appliances as part of a lease of land and incidental to the use and enjoyment of the land.
- See section 2 which provides that the PPSA applies to leases for a term of more than one year.

- See new section 57.1 which provides that Part V of the PPSA on remedies and enforcement, only applies to a security interest if it secures payment or performance of an obligation.
- All other PPSA statutes in Canada and the Quebec Civil Code apply the lease for a term of more than one year lease provision.
- Now all Ontario leases of chattels that fit this definition, should be perfected in time to achieve purchase-money security interest (“PMSI”) priority status.
- This pushes the determination of the characterization of a lease as a “true lease” as opposed to a “financing lease” or “disguised time purchase” until default by the lessee and enforcement.
- see: DaimlerChrysler Services Canada Inc. v. Cameron [2007] B.C.J. No. 456, British Columbia Court of Appeal, Prowse, Low and Kirkpatrick JJ.A., March 8, 2007.

The issue before the Court was whether the vehicle lease between the parties was a true lease or a security agreement to which Part 5 of the Personal Property Security Act (B.C.) applied. While many features of the document bore the hallmark of a true lease, the Chambers found that the default clause supported the finding that the transaction was a security lease. The default clause secured the payment of the lease payments and the option price and that the lessor knew it would receive the vehicle's full value and the full benefit of the lease payments in the event of default.

The appeal was allowed. The transaction was a true lease. The default provisions did not create a separate security. They simply represent the calculation of the amounts owing by the lessee upon a breach of the agreement. The chambers judge erred in her characterization of the lease by placing undue emphasis on the default provisions of the lease and, accordingly, by failing to accord proper weight to the option purchase price. The impugned transaction was a true lease that came within the definition of s. 2 and, therefore, was excluded from Part 5 of the PPSA

- By new section 57.1 of Part V will not apply to true leases, but govern enforcement of only those leases that secure payment or performance of an obligation.

## 6. **Errors in the Security Agreement**

- Existing section 11(2)(a) provides that a security interest attaches to the collateral when a debtor signs a security agreement that contains a description of the collateral sufficient to enable it to be identified.
- Sections 9(2) on defects or errors in the security agreement and 9(3) on omissions of collateral descriptions are being repealed as they conflict with the section 11(2)(a) requirements.
- Secured parties need to ensure the security agreement has a good collateral description to achieve attachment, and which description will also be the key to a word description of the collateral in the financing statement when Ontario drops the “check the box” system.

## 7. **Sales and Leases in the Ordinary Course of Business**

- Ontario’s old *Bills of Sale Act* was repealed in 1989.
- It required registration of a bill of sale where title passed to the buyer, but the goods remained in the vendor’s possession.
- This registration requirement was after forgotten and among other situations, caused losses to consumers when several boat makers failed, causing the unregistered purchasers to lose their goods still in the possession of the insolvent vendor, to the vendor’s secured creditors.
- After repeal in 1989, there was a gap in how to protect buyers in these situations.
- Sections 28(1.1), (1.2) and (1.3) expand section 28(1) to specifically extend protection to buyers in situations where the buyer has not taken possession or title has not passed or the vendor took a security interest in the goods, as long as the



goods are identifiable in the contract of sale or the goods have been identified or marked as allocated to the buyer.

- Subsections 2.1, 2.2 and 2.3 expand the same protections to protect the rights of the lessee under a lease.

## 8. **PMSI Notices**

- As outlined in the ULCC papers from 2003 and 2004 there are three different ways priority as between proceeds generated by sale of inventory secured to a PMSI inventory secured party, have priority as against the receivables of the same debtor financed to a second secured party.
- Given that the PMSI rights of a financier or lessor of inventory also extends to the proceeds generated by that inventory, Ontario has moved to expand the requirement to send PMSI notices to prior registered PPSA creditors of the debtor who have claimed an interest in either or both the inventory or the receivables of that debtor.
- Ontario is now matching the requirements in the Atlantic Canada PPSA statutes.

## 9. **Anti Assignment Clauses and Receivables and Chattel Paper Financing**

- See new section 40(1) with a new definition “account debtor” and sections 40(1.1), 40(2), 40(3) and 40(4).
- These changes validate a security interest granted by an account and chattel paper holder, to enable it to raise funds, despite an anti assignment clause.
- Section 40(4) now allows a secured creditor to obtain security over specified accounts of its debtor even though the contract between the debtor and its account debtor prohibits assignment. Anti assignment clauses cannot be upheld as against the assignee secured creditor.

- Section 40(1.1) provides that the account debtor retains all of its rights and remedies (including set off) that it had against the assignor, as against the assignee secured creditor of the assignor.
- Section 40(2) preserves the same rules that exist in section 53 of the *Conveyancing and Law of Property Act* that the account debtor may pay the assignor until such time as the account debtor has received notice reasonably identifying that the receivable or chattel paper has been assigned. The account debtor is entitled to obtain proof that the assignment has been made before the account debtor is obliged to pay the assignee.
- Note that the provisions in new section 40(4) apply to an assignment of “the whole of the account or chattel paper” and not partial assignments.
- By contrast the UNCITRAL convention on the assignment of international receivables which Canada is expected to ratify, deals with partial assignments. Any disconnect between Canada’s adoption of the convention and this provision will have to be dealt with in future.

## 10. **Mandatory Full and Partial Discharges**

- Section 56 of the statute has been updated with respect to the filing of financing change statements when the obligations of the debtor have been performed or with respect to partial discharges when it has been agreed to release at least part of the collateral or where a registration has been made but no security interest granted.
- A new provision in section 56(1) provides that where the scope of the collateral claimed in a financing statement is broader than the collateral actually granted under the security agreement, the debtor named in the financing statement may deliver written notice to the secured party demanding that a financing change statement be filed to accurately describe the collateral covered by the security agreement.

- Revised section 56(4) makes the secured party liable to pay \$500 to the debtor or other person entitled to make a demand, plus any damages resulting from the failure, where the secured party without reasonable excuse, fails to provide the required financing change statement or discharge or partial discharge under the prior sections.

## 11. **Changes in Enforcement**

### (a) **Exemptions from seizure and enforcement**

- New section 62(2) provides that any collateral under a security agreement, other than a security agreement perfected by possession or which has PMSI status, that would otherwise be exempt from seizure under the *Executions Act*, are also exempt from the rights of the secured party under subsection 62(1), being rights to repossess.
- It is extremely important that all financiers and lessors, and particularly those engaged in time purchases or financing of motor vehicles with consumers, ensure that they have PMSI priority for all leases and conditional sales.
- It also means the use of chattel mortgages, where a secured party is unable to fall inside the definition of a PMSI, come with an additional risk to the lender where the collateral may be exempt goods. For example a credit union taking a chattel mortgage on my family used vehicle to secure my loan.
- In adopting this exemption provision Ontario is matching a number of the other PPSA statutes.

### (b) **Objections to a notice to retain the collateral in satisfaction of the debt**

- See section 65(3) which provides that the time period within which a person who receives a section 65(2) notice of intention to retain the collateral in satisfaction of the debt, now has 15 days after service of the notice to object, and no longer 30 days.

- This now matches the same 15 day period with respect to objecting to notices of sale.
- New section 65(3.1) allows a person entitled to notice under section 65(1) to apply to a court to extend the 15 day period.

(c) **Enforcement of interests in personalty and realty together**

- Section 67(1)(g) has been added to provide the Court power to make orders as to notice, redemption, accounting for surpluses and other matters to enable a secured party to enforce any of its rights and remedies against both real and personal property security. For example, a trust deed charging a hotel and its contents.
- This allows a process for the secured party to deal with conflicting foreclosure and notice of sale notice provisions found in mortgage enforcement legislation and the PPSA, as well as different statutory duties of accounting relative to surpluses.

12. **Service of Notices**

- Section 68 has been updated to allow for fax and other electronic means of delivery of notices which are required to be served under the PPSA, as well as notices to be served by personal delivery such as a courier service.
- A reminder that section 68(4) was amended earlier in 2006 to drop from the deemed receipt of notices provision the exclusion for PMSI notices. PMSI notices now are deemed to be received in the same manner as any other form of notice delivered under the Act.

13. **Conflicts of Laws : to Come**

- The new provisions in Bill 152 dealing with conflicts of laws rules are not being proclaimed at this time.
- Currently the existing conflicts of law rules in section 7(1) use the location of the debtor at the time the security interest attaches to determine the validity,

perfection and priority of security interests in intangibles, mobile goods and a nonpossessory security interest in instruments, negotiable documents of title, money and chattel paper.

- For some corporate debtors with multiple offices and for foreign corporations, it has been very difficult to determine the “location of the debtor” by reference to its “chief executive office”: where the executives meet may not be an easy or obvious fact.
- The Bill 152 provisions when proclaimed, will use the jurisdiction of incorporation and the registered head office of a corporation to provide a definitive and easily determinable rule in making this decision.
- The existing PPSA does not provide rules to determining the location of general partnerships, limited partnerships and trusts. Bill 152 does and simplifies that determination.
- A key aspect to uniformity among the PPSA jurisdictions is to have uniformity in the conflict of law rules. Absent uniformity, we go back to conflicts of law from law school and deal with question of renvoi.
- Ontario at this time has not enacted these new conflict of law rules and will wait until other jurisdictions in Canada are prepared to make like amendments.
- At the ULCC meeting to be held in Charlottetown in September 2007, Professor Ronald Cumming will be providing his paper on certain PPSA amendment ideas to that body.
- While his paper is not generally available at this time, he is recommending that these Ontario new rules for conflicts of laws be adopted across Canada.

14. **What Changes Were Not Made By Bill 152 from the 1998 Submissions?**

- (a) Application of PPSA to licences - section 2. Some guidance may come from the Supreme Court of Canada where it basis the appeal for the Nova Scotia Court of Appeal on the nature of filing licences.

See: Royal Bank v. Saulnier [2006] S.C.C.A. No. 351 (S.C.C.), on appeal from [2006] N.S.J. No. 307, as altered by N.S.J. No. 387 (N.S.C.A.), on appeal from (2006) 17 C.B.R. (5<sup>th</sup>) 182 (N.S.S.C.)

At trial, the court held that the bank's general security agreement from the fisherman, now bankrupt, attached to his fishing licences, as they were personal property. The court held that the licences were property in his estate as the fair and correct approach was to characterize federal fishing licences as property given:

fishermen sold licences, especially lobster licences, for large amounts of money;

they were a bundle of rights constituting marketable property; and

to ignore commercial reality would result in inequitably denying the creditors access to something of significant value in the hands of the bankrupt.

The Nova Scotia Court of Appeal altered the trial court decision by finding that the licences were not an asset in the estate, but the income earned from the licences were part of the estate. The Court held that the licences were not property but that Mr. Saulnier had rights in relation to the licences, such as the income and the right to apply for renewals and the right to have them reissued to a designated third party.

The Supreme Court of Canada has granted leave to appeal

- (b) Use of PPSA registry for executions - section 41(1);
- (c) Classification of collateral - section 46(3);
- (d) Dropping the need for sending a copy of registration to debtor - section 46(6);
- (e) *Commercial Tenancies Act* – harmonize the CTA based on title concepts [leases, chattel mortgages, conditional sales] with the PPSA and except goods subject to purchase-money security interests from distraint by landlords;

- (f) Reform of other parts of the Act to deal with agricultural property, “crops”; the overlap between Bank Act and provincial PPSA security; the UNCITRAL convention on international receivables; and other improvements;
- (g) Create a process for ongoing PPSA reform – continual updates and an ongoing process.

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