



Changes in Law Fix Unintended Problem: Give Lenders More Certainty, Borrowers More Credit Opportunities

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Originally published in *Blaneys on Business* (December 2010) - [Read the entire newsletter](#)



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Greater certainty for business lenders and, as a result, a greater number of financing opportunities for business borrowers, flow from recent amendments to Ontario's *Personal Property Security Act* (PPSA) that have been just implemented to fix an inadvertent error in 2007 changes to the statute.

The new amendments to the PPSA, the Ontario legislation governing secured lenders' rights to collateral pledged to them by borrowers, are contained in the Ontario Legislature's Bill 68, which took effect October 25, 2010.

Ontario's PPSA, the oldest of the personal property security statutes in Canada, establishes what is now a unique "check-the-box" system that allows a lender to register with the Ontario government his claim to an asset or assets that have been pledged as security for a loan. This claim is registered when the lender files a "Financing statement/claim of lien" with the province.

The financing statement requires that the lender chose a collateral "category". Each category embraces a wide range of assets. Equipment, for example, can encompass everything from a laptop computer to a 12-wheel tractor trailer. If the lender simply checked the equipment box, only he would know which specific piece or pieces of equipment in the borrower's business had been pledged as collateral for that particular loan. If the lender took security over all of the borrower's assets, he would choose all the categories.

Prior to August 1, 2007, subsection 46(3) of the PPSA provided that if a lender inserted a description of the collateral over which it was taking a security interest, the financing statement was then limited to that collateral and could not be used by the lender in a subsequent loan for another security interest in any of the borrower's other collateral.

If the lender did not specify in the financing statement which particular asset he was taking as collateral, however, subsection 45(4) of the Act allowed that single financing statement to cover one or more security agreements between the lender and the borrower. So, one agreement might cover a laptop; a second — still captured by the checked-off equipment box in the first financing statement — might cover a big rig, and so on.

If the business asked for a third loan — from somebody else — there was no way that the prospective new lender could tell, simply by reviewing the financing statement, how many security agreements might be behind the check mark and whether he had a clear claim to whatever he was being asked to finance.

If the new lender wanted to ensure that he had a clear claim to the asset that was being pledged to him, he had to contact the first lender, as identified on the financing statement, and ask that lender to waive any priority he might have on the new item in question.

This, obviously, could be time-consuming for the new lender. In addition, a savvy borrower might object to a broad filing that didn't limit the registration to the specific collateral in question.

Accordingly, those secured parties who did not take all of the borrower's assets as pledged collateral, chose to describe the specific collateral covered by their existing security agreement.

The PPSA amendments, which were instituted in August, 2007 were part of a process that is intended, ultimately, to streamline, simplify and clarify the administration of the PPSA and harmonize it with regimes in the other provinces and territories. (Previously, the legislative authorities had acknowledged that the time had come to do away with the check-the-box system. It had been created when computers had much less memory and had been designed to accommodate registrations without taxing that limited memory. In the subsequent years, all other jurisdictions had taken advantage of advancing technology and had enacted PPSAs that did not need nor have 'check-the-box'.)

As part of eliminating 'check-the-box' and moving toward a more transparent Ontario system, the repeal of subsection 46(3) was made part of the amendments. Unfortunately, there were to be many delays in the development of software updates to the registration system. Subsection 46(3) was repealed nonetheless, but the repeal turned out to be premature.

The result was that, even where a secured party inserted a description of the collateral over which it was claiming a security interest, subsequent secured parties could not rely on that description because the legislative authority allowing for it no longer existed.

Therefore, even those creditors who sought to limit their financing statements were still bombarded with waiver and subordination requests.

At long last, however, with the passing of Bill 68, subsection 46(3) of the PPSA has now been reinstated and "new" lenders can now rely on the collateral descriptions provided by those secured parties ahead of them.

However, the Bill went even further than the prior subsection 46(3). A new subsection, 46(2.3), was instituted to provide that if a secured party did not insert a collateral description then it was open to the debtor to deliver a notice to the secured party demanding such a description, and the lender was obliged to file an amendment to his financing statement to provide such a description.

This obviously makes sense in the context of the eventual elimination of the check-the-box system because secured parties soon will not be permitted to simply check a box. A full collateral description will be required

This means that the public record will now state clearly, in every instance, which lender has priority over which specific asset, or will indicate which lenders have security over all of the borrower's assets. Prospective new lenders will know what is safe to them to lend against, and what is not and where it will be necessary to seek a waiver from an existing lender. Therefore, there will be reduced uncertainty regarding the priority over a piece of collateral and fewer delays or rejected credits because an earlier lender refuses to give a waiver.

In addition to this significant change, Bill 68 also extended the time frame in which a lender can register a purchase money security interest for goods other than inventory and intangibles. Previously, the PPSA provided only 10 days from the debtor's possession of the collateral in which to register a financing statement. As all the other PPSA provinces have nonetheless, adopted a 15 day period, the Ontario Act has now followed suit, giving national lenders a bit more certainty and continuity from one province to another. ■