

PROPOSAL FOR A
**NEW BRUNSWICK
PERSONAL PROPERTY SECURITY ACT**
EXECUTIVE SUMMARY

FOREWORD

In 1989, the Department of Justice commissioned a study of New Brunswick's personal property security law. That action was prompted in part by a representation received from the Law Society of New Brunswick to the effect that:

- (a) The existing law and legal structure governing personal property security in New Brunswick are badly in need of fundamental reform.
- (b) **Personal Property Security Act (PPSA)** type legislation offers the most appropriate reform model since the problems with the existing New Brunswick law are not unique to this jurisdiction. They are the same as, or similar to, those which gave impetus to the **PPSA** reform movement elsewhere in the country.
- (c) The necessary steps towards adoption of a **PPSA** regime in New Brunswick should commence forthwith with full advantage being taken of the extensive work that has been done in other jurisdictions.

The adoption of an appropriate **PPSA** system was seen as having the advantage of bringing New Brunswick's law into harmony with that of most of Canada and the United States. That should facilitate considerably the conducting of normal commercial activities in the province and help create an atmosphere that is more conducive to the growth of such activity. It should also facilitate and encourage inter-provincial and international commercial dealings, particularly with jurisdictions such as the United States where **PPSA** type systems are well known.

It was anticipated that modernization of the law would be accompanied by the introduction of a centralized, computerized registry system. Such a measure would render the system considerably more efficient and useful.

Professor Catherine Walsh of the University of New Brunswick Law School was commissioned to undertake the study. Her report has been completed and we are now in a position to move into the consultative phase of the project. Professor Walsh's report is extensive, including analysis, recommendations, draft legislation and section-by-section commentaries. It exists in English only.

The enclosed Executive Summary is being provided to familiarize the reader with the substance of the report. Anyone wishing to acquire a copy of the full report is invited to submit such request to:

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Comments and representations on the report are invited by September 20th. It is hoped that a legislative proposal can be prepared before the end of the year, based on Professor Walsh's recommendations and representations received from interested parties.

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Director of Law Reform Branch

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June 1991

prepared by

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commissioned by

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Province of New Brunswick**

INTRODUCTION

While taking security against land has been around for centuries, wide spread financing on the strength of a debtor's personal property is essentially a post-industrialization phenomenon. Today, personal property represents at least as important a source of debt collateral as land in both the commercial and consumer contexts.

Unhappily, personal property financing in New Brunswick is hampered by a badly fragmented and staggeringly complex legal framework which fails to accommodate many modern commercial practices.

The deficiencies in the existing New Brunswick law are not unique to this province. They are the heritage of all common law legal systems and derive from the *ad hoc* way in which chattel security law expanded and evolved everywhere over the last century.

Promulgated in 1951, Article 9 of the Uniform Commercial Code in the United States attempted a comprehensive statutory integration of the law governing secured transactions in personal property. The result is widely regarded as the most innovative and successful of the Code articles.

Article 9 has also proved to be a highly exportable legal product. *Personal Property Security Acts* derived from Article 9 are now in force in the majority of Canadian provinces, beginning with Ontario in 1976 and spreading west to Manitoba in 1978, Saskatchewan in 1981, the Yukon Territory in 1982, and Alberta and British Columbia in 1990. The Canadian adaptation of Article 9 has in turn spawned proposals for similar legislative reform in England, Australia and New Zealand.

That the winds of PPSA reform would eventually blow east was inevitable. In May 1987, the Law Society of New Brunswick reported to the Hon. James Lockyer, Minister of Justice, that the time had come for a *Personal Property Security Act* in New Brunswick. With more and more PPSA regimes becoming fully operational in the rest of the country, it was felt that there could be little advantage in New Brunswick continuing to await the outcome of experience elsewhere. The Minister agreed wholeheartedly and the Law Reform Division of Justice commissioned Catherine Walsh of the Law Faculty at the University of New Brunswick to prepare a PPSA proposal for the province. Her work is now complete and what follows here is a summary of the highlights of the proposed new regime.

THE LEGISLATIVE MODEL FOR THE PROPOSED NEW BRUNSWICK PPSA

Contemporary Canadian PPSA legislation offers two models: the 1989 version of the Ontario PPSA and the Model PPSA developed by the Western Canada Personal Property Security Committee. With common roots in Article 9, both models naturally share the same basic structure and philosophy. But there are significant differences not just in drafting style but in substantive result and in overall legislative policy.

The proposed New Brunswick PPSA adopts the Western rather than the Ontario model. The Western approach offers considerably more detailed direction on many is-

sues and, where the two models differ in point of substance or policy, the Western version is regarded by most as steering the preferable course.

Most importantly, perhaps, adoption of the Western Model best promotes the important goal of interprovincial harmonization of PPSA law. It has been adopted by both the British Columbia and Alberta legislatures and is expected to be the model for the Northwest Territories PPSA when one is enacted. The Saskatchewan Law Reform Commission has recently recommended its immediate adoption in place of the current Saskatchewan PPSA and it is expected to be only a matter of time before Manitoba and the Yukon follow suit.

The prospects of achieving interjurisdictional legislative harmony through the Western Model have recently received an additional boost. The initial goal of the Western Canada Personal Property Security Committee was to secure harmony in PPSA legislation in the western provinces and northern territories. But in 1989, representatives from both Ontario and New Brunswick began to attend the Committee's annual meetings. Their participation, combined with New Brunswick's active consideration of a PPSA based on the Western Model, led the Committee to decide in 1990 to "nationalize" its harmonization goals. That decision reached fruition at the June 1991 meeting which also saw the attendance for the first time of representatives from the federal government. A new constitution was proclaimed recreating the Western Committee as the Canadian Conference on Personal Property Security Law.

The principal mandate of the new Conference is to "encourage and facilitate harmonization and compatibility of provincial, territorial and federal personal property security law". To provide the structural support for that mandate, the Conference has given birth to a Registry Committee and a Legislative Review Committee. The goal of the Registry Committee is to facilitate the exchange of expertise and information among Personal Property Registrars and to achieve greater harmony in Registry practices and operational infrastructures. The task of the Legislative Review Committee is to review and assess proposals for changes to the Model Act, whether initially received at the individual provincial level or directly by the Committee. The work of the Committee will provide a significant hedge against idiosyncratic, overly hasty or unnecessary local variations while also ensuring that the Model Act remains responsive to changes in commercial practice.

SCOPE OF THE PROPOSED PPSA

The existing law of personal property security is not one law but many laws. Chattel mortgages, conditional sales, assignments of book debts, fixed and floating equitable charges are each, to a large extent, subject to their own particular and often peculiar set of common law, equitable and statutory rules.

The genius of Article 9 and PPSA legislation lies in replacing this 'system' of discrete security devices with the simple concept of a generic "security interest". It is this evolutionary step which, more than anything else, makes it possible to integrate all aspects of personal property financing in one legislative treatment.

The proposed PPSA will apply to all agreements which create a security interest in personal property or fixtures. Security interest is defined in functional terms to mean any

interest taken in collateral to secure a debt or other obligation, regardless of form or title of the transaction. As such, the Act will apply to the full array of conventional security devices as well as to other more novel transactional forms where they employed to perform a security function.

The registration and priority aspects of the proposed PPSA will also extend to certain non-security dealings in personal property: notably, long-term chattel leases, commercial consignments and absolute transfers of accounts or chattel paper. They have been included for one or both of two policy reasons: to publicize the true state of title to third parties and to reduce debate and litigation on the character of the transaction.

THE PERSONAL PROPERTY REGISTRY

Over the years, the New Brunswick legislature has established no less than four separate statutory regimes to regulate the registration of security interests in personal property: the *Bills of Sale Act*, the *Conditional Sales Act*, the *Assignment of Book Debts Act* and the *Corporation Securities Registration Act*. Which regime regulates a particular transaction depends on a complex mix of factors: the nature of the collateral, the type of security device, the form of the security documentation and the corporate or non-corporate status of the debtor. The logistics of registration and searching are rendered even more complicated by the fact that, with the exception of the *Corporation Securities Registration Act* record, these registries are operated on a county basis,

The proposed PPSA will replace the four existing registry systems with a single Personal Property Registry. Although registry clientele will still be able to conduct registrations and searches locally, the new system will have a computerized province-wide registration data base.

Like the current registry systems, the Personal Property Registry is intended to ensure public disclosure of security interests taken in assets that have been left in the debtor's possession or control. However, registration is presently required only if the collateral takes the form of chattels or book debts. In contrast, the proposed system will apply to non-possessory security interests in all categories of personal property.

The PPSA itself will apply only to consensual security interests. However, the Personal Property Registry will be designated as the appropriate registration venue for a wide variety of non-consensual encumbrances against personal property, giving credit searchers the convenience of 'one-stop shopping'.

The proposed new registry will adopt the concept of notice filing. Rather than having to register the complete security documentation, secured parties will file only a simple notice document called a "financing statement". The financing statement will set out only the basic information necessary to alert a searcher that a security interest may have been taken in certain collateral. Those who have a legitimate interest in knowing more details will be entitled to demand particulars from the secured party of record.

With notice-filing, there is no reason why a single registration cannot cover multiple or successive security agreements provided the registered data continues to accurately reflect the current financing arrangement. The proposed PPSA will permit a single registration to relate to more than one security agreement, a feature that will prove especially advantageous to inventory financiers.

Notice-filing also eliminates any practical obstacle to pre-agreement registration and the PPSA will permit a financing statement to be registered before the security agreement is entered into. Advance registration will enable the immediate release of loan funds and eliminate the need to provide "grace periods" for registration. It will also allow a secured party to ensure its priority ranking while still at the negotiation stage since priority under the PPSA generally relates back to the date of registration. Stringent discharge requirements will protect debtors from the risk of "false registrations" should the security agreement fail to materialize.

Under the existing registration statutes, the filing must be renewed every three years. The single exception is the *Corporation Securities Registration Act* under which a registration remains effective in perpetuity or until positively discharged. The PPSA will introduce the flexibility of variable registration life, sharply reducing the risk of lapse. The Regulations to the Act will permit a secured party to select a registration life of from one to twenty-five years or perpetuity. Registration fees will be prescribed according to a sliding tariff of fees scaled to the period of registration life selected.

PRIORITIES

After more than a century of litigation, many critical priority issues remain unresolved in the existing law. In providing a comprehensive priority code, the PPSA will bring much-needed certainty to the resolution of priority disputes among secured parties claiming a security interest in the same collateral.

As a general rule, priority under the PPSA will be determined according to the order of registration of the competing interests, regardless of when they may actually have attached.

However, registration is not required where the secured party takes possession of the collateral since possession functions just as effectively as registration to publicize the security interest. In the event of a contest between a secured party who has "perfected" its security interest by registration and one who has "perfected" by taking possession, priority will be determined according to the order of the perfecting events.

It may happen, albeit rarely, that none of the conflicting security interests will have been perfected either by registration or taking possession. In that event, the order in which the security interests attached will determine priority.

In addition to these general priority rules, the PPSA will also provide more specialized priority rules in circumstances where commercial practice, elementary fairness or the nature of the particular collateral require a more highly tuned resolution. Notable examples include the super-priority rule for purchase money financiers and the detailed guidance provided on priority disputes involving collateral which takes the form of fixtures, growing crops, accessions, or commingled goods.

Priority disputes may arise not only among secured parties but also between a secured party and a subsequent buyer or lessee of the collateral as well as between a secured party and the debtor's execution creditors or trustee in bankruptcy. The PPSA will also provide comprehensive guidance on resolving both classes of disputes.

DEFAULT RIGHTS AND REMEDIES

For the most part, the proposed PPSA rules on default enforcement reflect existing commercial practice. On default, the Act will give the secured party two basic options. It can seize the collateral, dispose of it by sale, apply the proceeds against the debt and expenses and claim any remaining deficiency from the debtor. Alternatively, the secured party can elect to simply take the collateral in full satisfaction for the debt provided those with an interest in the collateral have no legitimate grounds for objection.

The proposed PPSA will also preserve the debtor's time honored rights to redeem the collateral and to claim any surplus proceeds where the collateral is disposed of by sale. But a new debtor remedy will also become available. A defaulting debtor will have a limited right to reinstate the security agreement on payment of enforcement expenses and the sum actually in arrears exclusive of the operation of any acceleration clause.

Finally, the proposed PPSA will give express recognition to the wide-spread use of receivers and receiver-managers in commercial debt realizations. Receivers will be made expressly subject to the general enforcement requirements of the Act where appropriate and some aspects of existing receivership will be consolidated and refined.

CONCLUSION

The fact that PPSA reform came about to remedy the very deficiencies which presently plague the New Brunswick law of personal property security is reason enough to welcome its advent in this province. But there are others. The adoption of a PPSA will finally bring New Brunswick law into line with the legal framework governing secured financing in the rest of North America. This will facilitate the involvement of the New Brunswick business community in national and continental financing transactions and allow the New Brunswick legal community to once again participate in and benefit from the jurisprudence and commentary in the rest of Canada.

But while PPSA reform is welcome reform, its limits must also be stressed. The Act will change almost nothing in the way of fundamental policy. Its principal public benefit lies in rationalizing and consolidating the central features of the existing law and commercial practice, not in changing them. Larger questions such as the need for special consumer protection measures or the continued desirability of a *laissez-faire* approach to secured financing have been left for another day.

It must also be emphasized that personal property security is an inherently complex field. It is true that the PPSA will reduce that complexity by at least placing the rules between two covers. But the sheer number of relevant players whose interests must all be balanced - the debtor, the secured party, other secured parties, general creditors and their representatives, transferees of the collateral and the general public - renders a radically simplified legislative treatment impossible.