

Banking and Finance Law

December 8, 2017

Bill 154 Receives Royal Assent, Bringing Clarity to the *PPSA*'s Conflict of Laws Rules

On November 14, 2017, Bill 154, *Cutting Unnecessary Red Tape Act, 2017* (“**Bill 154**”) received royal assent from the Legislative Assembly of Ontario. Bill 154 represents an effort by the Ontario government to reduce the inefficiencies created by red tape through the amendment or repeal of various legislation, including the *Personal Property Security Act* (Ontario) (the “*PPSA*”).

Among other things, the amendments in Bill 154 provide further clarification on the *PPSA*'s “location of debtor” rules, which came into force on December 31, 2015 (the “**2015 Amendments**”).

Background

The 2015 Amendments

The *PPSA* provides that the laws of the jurisdiction where the debtor is “located” govern the validity, perfection and priority of security interests in certain classes of collateral, including, for example, intangibles, negotiable documents of title, money and chattel paper. As such, secured parties must be able to identify the location of the relevant debtor to register appropriate *PPSA* financing statements and conduct proper searches. Secured parties must also be able to understand when a debtor's location has *changed* pursuant to the *PPSA*: a failure to respond promptly to this kind of change can result in a security interest becoming unperfected and the secured party losing its priority in the collateral.

Before the 2015 Amendments, determining the location of a business debtor was an uncertain process as it hinged on the location of such debtor's “place of business” or, if such debtor had more than one place of business, its “chief executive office”. Since these terms

were undefined, secured parties were forced to conduct searches and register financing statements in multiple jurisdictions to cover all potential interpretations.

On December 31, 2015, the conflict of laws provisions under section 7 of the *PPSA* were amended to provide that a business debtor's location would be determined according to its entity type or organizational form. For example, if the entity was a corporation, limited partnership or other organization organized under provincial or territorial law, the debtor's location would be deemed to be in the province or territory of incorporation, formation or organization, as applicable.

The transition provisions under subsection 7.2(7) of the *PPSA* enacted in concert with the new debtor location rules gave secured parties five years to *re-perfect* security interests perfected by registration before December 31, 2015.

What Prompted the Bill 154 Amendments to the PPSA?

Unfortunately, the language of the transition provisions was too broad and created an unintended outcome whereby, regardless of whether the location of the debtor changed as a result of the 2015 Amendments, re-perfection before December 31, 2020 would be required for *every* registration made before December 31, 2015. In other words, failure to file a new financing statement before December 31, 2020 would result in a loss of perfection, even if the debtor's location remained the same under both the old and new rules. In addition, the language used in subsection 7(2) of the *PPSA* maintained pre-2015 Amendments language regarding location and relocation, rather than referencing organizational form.

Clarity From Bill 154

Bill 154 clarifies that secured parties will not be required to re-perfect security interests perfected before December 31, 2015 in the applicable classes of collateral if the location of the debtor determined

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under prior law (as defined in subsection 7.2(1) of the *PPSA*) did *not* change as a result of the new rules in subsections 7(3), (4) and (5). Simply put, where the location of the debtor remains the same under both the old and new rules (i.e., in the case of an Ontario corporation with a chief executive office in Ontario), re-perfection before December 31, 2020 will *not* be required.

If the debtor's location changed solely as a result of the 2015 Amendments, then the transition provisions in subsections 7.2(7) and (8) will apply and the security interest will remain perfected only until the earlier of (a) December 31, 2020; (b) the beginning of the day perfection ceases under prior law; and (c) if a factor that determines the location of the debtor under the new rules changes after December 31, 2015 (e.g., continuance of a corporation to another jurisdiction), the earlier of 60 days after the change in the debtor's location or 15 days after the secured party learns of the change.

The amendments to the *PPSA* under Bill 154 also replace the aforementioned reference to location under subsection 7(2) with new language which now specifically references the new location of the debtor rules in assessing a change of jurisdiction, stating "...if the jurisdiction where the debtor is located changes as a result of *a change in a factor by which the location of the debtor is determined under subsection (3)*, the security interest continues perfected only until the earliest of..." [Emphasis added.]. Complementary changes were made throughout section 7 to correct similar inconsistencies.

Practical Considerations

Perfection provides public notice that a secured party has taken a security interest in a debtor's assets and allows that secured party to enforce against others with an interest in the same security. It also determines the ranking of a secured party's interest in collateral. It is critical, therefore, for a secured party to have clear direction from the *PPSA* on factors which may cause a security interest to become unperfected, including a change in the debtor's location.

Thankfully, the latest changes to the *PPSA* correct certain drafting issues from the 2015 Amendments and bring greater certainty to secured parties seeking to maintain perfection of their security interests.

Notably, each province has its own personal property security legislation, and depending on which jurisdiction's legislation applies the debtor may have a different "location". Not all provinces have adopted the same conflict of laws rules now in place in Ontario. Until the other provinces follow suit, a prudent party will need to look at the conflict of laws rules in each relevant jurisdiction, and should consider registering financing statements and conducting searches in each of those jurisdictions.

Bill 154 contains other minor technical amendments to the *PPSA* that are not addressed in this Update. If you have any questions, please contact any member of our Banking and Finance Group.