Consumer Protection Modernization: Notices of Security Interests

Submitted to: **The Ministry of Public and Business Service Delivery**

Submitted by: **The Ontario Bar Association**

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Introduction

Thank you for providing the Ontario Bar Association (**"OBA"**) with the opportunity to provide input on issues related to Notices of Security Interests (**"NOSIs"**) as part of your effort to modernize consumer protection.

The OBA is the largest and most diverse volunteer lawyer association in Ontario, with over 16,000 members who practise on the frontlines of the justice system, providing services to individuals and businesses in virtually every area of law in every part of the province. Each year, through the work of our 40 practice sections, the OBA provides advice to assist legislators and other key decision-makers in the interests of both the profession and the public.

This submission was prepared by the Personal Property Security Law Committee (**"PPSL Committee"**) of the OBA Business Law Section. The PPSL Committee's members are practitioners from large Toronto law firms and small boutique law firms, in-house lawyers working with equipment financiers, and academics, many of whom are recognized as leaders on secured transactions involving businesses and consumers and experts on the Ontario *Personal Property Security Act*. By virtue of this varied membership, the PPSL Committee represents a broad spectrum of perspectives, including vulnerable consumers (as part of *pro bono* work). The submission also has the benefit of input from the broader Business Law Section, including lawyers specializing in consumer protection.

Below you will find an Executive Summary of our Recommendations followed by more detailed answers to the specific questions posed in relation to NOSIs.

Executive Summary of Recommendations

The following summarizes our comments and recommendations:

- Any new provisions to address NOSI issues should appear in the Ontario *Personal Property Security Act* (**"PPSA"**), not the Ontario *Consumer Protection Act* ("**CPA**").
- Section 57 of the PPSA should be amended so that it applies not only where a security interest in consumer goods has been performed or forgiven, but also where a security agreement is "rescinded, cancelled or terminated".
- For consistency, PPSA s. 56(1)(a) should be amended along the same lines.
- We support the proposed alternative NOSI discharge procedure, but the responsible official should be the Director of Titles appointed under the Ontario *Land Titles Act*, not the Director of Consumer and Business Services.
- A new term called "prescribed goods" should be added. This new term would be defined by regulation to mean consumer goods of a type or types specified in the regulations for the purposes of the new debtor rights described below (e.g., hot water tanks, HVAC systems,

and other consumer goods that are commonly sold on a door-to-door basis and that are or may be affixed to real property).
- If the collateral is prescribed goods, the fixture secured party should be required to give the debtor written notice that it holds or will hold a security interest in the fixture collateral and that the secured party may register a NOSI. The notice would have to be in a document that was separate from the security agreement, and it would have to be given before the secured party applied to register the NOSI. In order to proceed with the registration, the secured party would have to furnish proof that the notice had been given.
- If the collateral is prescribed goods, the debtor should be given notice if the security agreement is assigned and also of any change in the secured party's name or contact details.
- According to the Director of Titles' October 27, 2022 Bulletin, from and after January 1, 2023, no NOSI may be filed if the financed or leased consumer goods are windows (other than certain energy efficient windows that are ENERGY STAR compliant), doors and roofs. The PPSA should be amended to codify this new limitation and also to expand it to cover not just the items listed in the Bulletin, but all prescribed goods that when affixed to a building would be "building materials" under the PPSA.
- The application of Part V.1 of the PPSA should be extended to cover the vexatious registration of NOSIs (at present it only applies to PPS registrations).
- No changes are necessary to the law governing NOSI assignments because the applicable PPSA provisions are sufficient.
- The secured party's claim on the collateral upon discharge of a NOSI should be limited to the lesser of: (a) the market value of the collateral at the date of the discharge and (b) the outstanding amount of the secured obligation.
- A plain language guide should be published explaining the consumer's rights under the proposed new provisions, how the proposed automatic discharge procedure works, and the grounds on which it may be invoked.

Details of Submission

The recommendations are numbered and organized to correspond with the Ministry's consultation paper (Modernizing the Consumer Protection Act – February 2023).

6.1) Would the clearer requirements to discharge NOSIs support improved compliance by businesses?

Yes, but the proposed changes fit better in the Personal Property Security Act, than the Consumer Protection Act, because the PPSA already deals with the analogous situations described in cases (1) and (2) below, and, in the interests of avoiding legal fragmentation, it makes sense to have all three cases dealt with in the same statute.

Discussion:

There are three main cases where a debtor might want to discharge a NOSI:
(1) where the secured obligation has been performed or forgiven;
(2) where the secured party never acquired a security interest; and
(3) where the security agreement is cancelled, rescinded or terminated.

The first case is already provided for by the combined effect of ss. 56(1)(a) and 56(4) of the PPSA (in the case where the fixtures are not consumer goods) and ss. 57(1) and 57(4) of the PPSA (in the case where the fixtures are consumer goods).

In the non-consumer goods scenario, the debtor may require the secured party to discharge its NOSI after all of the obligations under the security agreement have been performed and, if the secured party fails to comply within 10 days after receiving the debtor's demand to file a discharge, it must pay $500 to the debtor and any damages resulting from its failure.

In the consumer goods scenario, the secured party is required to file a discharge of the NOSI within 30 days after all the obligations under the security agreement have been performed or forgiven, failing which the secured party must pay the debtor $500 and any damages resulting from its failure.

The principal operative difference between s. 56(1)(a) and s. 57(1) is that where the fixtures are consumer goods and the secured obligation has been performed, the debtor does not need to demand that the secured party discharge the NOSI (as would be the case under s. 56(1)(a) where the fixtures are not consumer goods). Instead, the obligation on the secured party to file the discharge of the NOSI arises automatically once the secured obligations have been performed or forgiven.

The second case is provided for by the combined effect of ss. 56(2) and 56(4) of the PPSA. Where a NOSI is registered by a secured party and the secured party never acquires a security interest in the fixture covered by the NOSI, then the debtor may demand that the secured party discharge the NOSI. If the secured party fails to do so within 10 days of receiving the debtor's demand, the secured party must pay the debtor $500 and any damages resulting from the failure.

The focus of the discussion in the Consultation Paper is mainly on the third case and, more particularly, on where the consumer elects to cancel the contract during the CPA's 10-day cooling-off period. PPSA, ss. 56(1) and 57 would probably not apply in this scenario. Section 56(1) would not apply because it is limited to the case where the secured obligation has been "performed" (in other words, it only applies to the first of the cases described above). Section 57 applies if all the obligations under the security agreement have been "performed or forgiven". It could be argued that the rescission or cancellation of a security agreement results in the secured obligations being "forgiven", but this strains the language of the section, and it is doubtful whether a court would accept the argument. It follows that s. 57, like, s. 56(1), is relevant only to the first of the cases described above.

PPSA, s. 56(2) applies if no security interest is acquired (the second of the cases described above). On its face, the provision appears not to be relevant to the third case. However, s. 95(d) of the CPA provides that "the cancellation of a consumer agreement in accordance with … [the CPA] operates to cancel, *as if they never existed*, … all security given by the consumer … in respect of money payable under the consumer agreement …" (emphasis added). The effect of this provision, arguably, is that, upon a consumer's rescission or cancellation of a consumer agreement in accordance with the CPA, the secured party is deemed never to have acquired a security interest and PPSA, s. 56(2) applies on that basis.

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In summary, the third case described above is not captured by PPSA, s. 56(1) or s. 57, though it may be captured by s. 56(2) but only if the agreement is cancelled pursuant to the CPA (and not on some other ground). For the avoidance of doubt, **we recommend amending s. 57 of the PPSA so that it expressly applies not only where the secured obligation has been "performed or forgiven", but also where a security agreement is "rescinded, cancelled or terminated". For completeness, a corresponding change should be made to s. 56(1).**

This is in substance similar to the reform proposed in the Consultation Paper, except that the Consultation Paper appears to envisage that the new provisions would appear in the CPA, not the PPSA. The proposed changes fit better in the PPSA, because the PPSA already deals with the analogous situations described in cases (1) and (2) above and, in the interests of avoiding fragmentation, it makes sense to have all three cases dealt with in the same statute.

6.2) Do you expect the proposed alternative process to be a significant improvement for consumers over the current requirement to seek a court order?

Yes, it would be a significant improvement for consumers, subject to the following considerations.

The references in the Consultation Paper to "the Director" appear to mean the Director appointed under the Ministry of Consumer and Business Services Act (see Consultation Paper, p. 17). However, in the NOSI context, the references should be to the Director of Titles appointed under the Land Titles Act. Section 10 of the Land Titles Act gives the Director of Titles broad powers "to determine any matter relating to titles of land to which this Act applies", with or without a hearing. On this basis, under the proposed new NOSI discharge procedure, the consumer's application should be made to the Director of Titles; the compliance notice should be issued by the Director of Titles; and if the secured party fails to comply within the required time, the Director of Titles should discharge the NOSI pursuant the powers vested in them by s. 10 of the Land Titles Act. No hearing would be required.

The proposed alternative process should be available in cases where the collateral is prescribed goods (as defined below) and any one of the following events or circumstances apply:

- The security interest has been performed or forgiven;
- The secured party never acquired a security interest in the collateral;
- The secured party fails to give the debtor notice of its intention to register a NOSI (see further the response to Question 6.5) below);
- The secured party, having assigned its interest under the security agreement, fails to notify the debtor of the assignment within X days of the date of the assignment (see further the response to Question 6.6) below);
- The debtor has been unable to locate the secured party, having made reasonable attempts to so; or

- The "prescribed goods" constitute "building materials" under the PPSA.

"Prescribed goods" would be defined to mean consumer goods that are prescribed by regulation for the purposes of this provision (e.g., hot water tanks, HVAC systems, any other similar consumer goods commonly sold on a door-to-door basis).

The proposed new provision should appear as s. 54(4A) of the PPSA.

It would be helpful to publish a plain language guide of the new provisions to facilitate consumer awareness of their rights, the steps involved in the process and the grounds on which the process may be invoked.

6.3) Do you support the ministry's proposal to leave NOSI assignment rules unchanged?

There is no need for changes to deal specifically with "NOSI assignments" because, as explained below, the PPSA already addresses the issue sufficiently.

The Consultation Paper, in Question 6.3) and elsewhere, confuses the NOSI itself with the underlying security interest. The NOSI itself does not give the secured party a security interest. It is simply the instrument used to register a security interest in the Land Titles Registry. The acquisition of a security interest depends on the making of a security agreement between the secured-party and the debtor. The security agreement is a contractual document. A NOSI is not.

On the basis of the foregoing, the discharge of a NOSI does not result in loss of the security interest as the Consultation Paper assumes. It simply means that the security interest becomes unprotected as against a person who subsequently acquires an interest in the real property to which the fixture has been affixed (e.g., a mortgage lender or a buyer of the real property). This means that the security interest will be ineffective against such third parties, but it remains valid and enforceable against the debtor.

Question 6.3) refers to assignment of the NOSI. However, the principal subject-matter of any assignment between the secured party and a third party is not the NOSI but, rather, the security interest (along with the underlying secured obligation). The PPSA already deals adequately with this scenario in the context of PPS registrations. In particular, s. 47 provides that either the assignor or the assignee may (not must) register a financing change statement to identify the new assignee as the party of record. Section 21(2) provides that the assignee inherits the assignor's priority position (regardless of whether a financing change statement is registered under s. 47). Section 56(6) supplements s. 56(1)(a) by providing, in effect, that if, following an assignment of the security interest, the assignor receives a s. 56(1)(a) notice, it must within 15 days after receiving the notice, disclose the assignee's details to the notice sender. All these provisions apply to security interests regardless of whether the security interest is perfected by registration of a financing statement in the PPS Register or is protected by registration of a NOSI in the Land Titles Register.

6.4) Apart from what has been proposed to better protect consumers, should the ministry take further action to protect consumers from the potential negative impacts that may result from consumer contracts that create a security interest?

- ***a) How can this be best achieved?***
- ***b) Do you support the ministry's proposed regulation-making authority that governs the use of security interests or liens in respect of consumer contracts?***

Regulations may be necessary to prescribe the types of goods that would be subject to the special NOSI measures discussed in the responses to Questions 6.2) above and 6.5) and 6.6) below.

According to the Director of Titles' October 27, 2022 Bulletin, from and after January 1, 2023, no NOSI may be filed if the financed or leased consumer goods are windows (other than certain energy efficient windows that are ENERGY STAR compliant), doors and roofs. It would be helpful to codify this limitation by PPS regulation. The regulation should apply not just to the items listed in the Bulletin, but should cover any prescribed goods that when affixed to a building would constitute "building materials". A definition of "building materials" should be added to the PPSA, based on the provision that appears in many of the PPSAs outside Ontario. For example, Saskatchewan PPSA, s. 2(1)(e) defines "building materials" as follows:

> **"building materials"** means materials that are incorporated into a building, and includes goods attached to a building so that their removal:
>
> (i) would necessarily involve the dislocation or destruction of some other part of the building and cause substantial damage to the building, apart from the loss of value of the building resulting from the removal; or
>
> (ii) would result in weakening the structure of the building or exposing the building to weather damage or deterioration;
>
> but does not include:
>
> (iii) heating, air conditioning or conveyancing devices; or
>
> (iv) machinery installed in a building or on land for use in carrying on an activity in the building or on the land.

Apart from the foregoing, we do not believe that any further regulation-making authority is necessary. The PPSA already includes a number of consumer protection-related provisions

which apply where the collateral is or includes consumer goods (see, for example, ss. 5(2), 12(2)(b), 45(2), 45(4), 57, 65(1) and 66(2)). Any additional consumer protection measures the Ministry might want to implement in the future should likewise appear in the Act itself rather than being left to regulations. It is much easier for interested parties to locate and understand the applicable law if it is stated in one place rather than two.

6.5) Should the secured party (e.g., the business that supplied the goods) be required to notify the consumer when it registers a NOSI in the Land Registry System?

a) If yes, should there be requirements as to when this occurs?

As a general rule, the policy should be the same as for the registration of a financing statement in the PPS Register. However, there may be a case for special rules where the collateral is prescribed goods.

PPSA, s. 46(6) provides that within 30 days after registration, the secured party must give the debtor a copy of the verification statement containing details of the registration. However, the debtor may waive their right to receive a copy (s.46(6.1)). Typically, security agreements will contain a waiver provision as part of their fine print terms and conditions. **It follows that in many cases, debtors will unwittingly lose their right to a copy of the verification statement when they sign the security agreement. The vexatious registration provisions in Part V.1 of the PPSA were enacted at least partly with this problem in mind. The vexatious registration provisions apply only to PPS registrations.** Thought might be given to extending the provisions to NOSIs. The NOSI provisions would give the Registrar of Land Titles powers to discharge a vexatious NOSI on the same basis as the other Part V.1 provisions empower the PPS registrar to discharge a vexatious PPS registration. To be clear, this is different from the mandatory discharge procedure discussed in the response to Question 6.2) above, which would apply in the circumstances listed in the Question 6.2) response and which would be provided for in the proposed new s.54(4A) of the PPSA.

There may be particular abuses in the context of prescribed goods which would justify the enactment of special rules requiring notice of a NOSI registration. For example, the secured party might be required to give the debtor in a prescribed form, a notice stating that it holds or will hold a security interest in the fixture-collateral and that it plans to register a NOSI. The notice would have to be given x days before the NOSI is registered and it would have to be in a document that was separate from the security agreement. To complete the registration, the secured party would have to furnish proof that the notice had been given,

6.6) In the case of a contract assignment, should the business or assignee be required to notify the consumer when an assignment occurs?

As a general rule no, but there may be a case for special rules where the collateral is prescribed goods.

Section 56(6) of the PPSA already provides for the service of a notice of assignment in cases where the collateral is not consumer goods. The notice must be sent within 15 days after the secured party receives a demand for discharge of the registration under s. 56(1)(a).

The purpose is to allow for redirection of the demand to the new secured party/assignee. Section 56(6) does not apply if the collateral is consumer goods because in that case, if the secured obligation has been "performed or forgiven", the debtor is entitled to an automatic discharge of the registration under s. 57 and so the issue that s. 56(6) addresses does not arise.

The Ministry's proposed alternative approach for discharging a NOSI does not require any notice from the debtor to the secured party and so, as in the case where s. 57 applies, the issue that s. 56(6) addresses does not arise. It might be argued that if the debtor is unaware of the assignment, they run the risk of making their payments to the wrong party (the assignor rather than the assignee). However, s. 40(2) of the PPSA already protects the debtor against that risk.

On the other hand, there may be particular abuses in the context of prescribed goods which would justify requiring that the debtor be given notice of an assignment. In the absence of such readily available information, debtors may encounter problems paying off the secured obligation and having the NOSI discharged. With these concerns in mind, the secured party might be required to notify the debtor of any assignment within X days. On the same basis, it might also be required to notify the debtor of any change in the secured party's name or contact details. Failure to comply would entitle the debtor to apply for discharge of the registration using the proposed new procedure outlined in the response to Question 6.2) above.

6.7) Should the total value of the registered NOSI be limited to the estimated retail value of the equipment only (i.e., the value of the equipment, but not services)?

a) If yes, how should the estimated retail value of the equipment be determined?

This issue only arises if the consumer is in default under the security agreement.

The Consultation Paper's main focus is on the case where the consumer exercises their right of cancellation within the CPA's 10-day cooling-off period. In that case, the consumer's payment obligation is extinguished, and the secured party has no right to demand any payment as a condition of discharging the NOSI.

The Consultation Paper raises a concern that "security interests are often registered for the total value of the leasing or financing contract, which can include a service component, additional fees and/or installation" and Question 6.3) reflects this concern by suggesting that "the total value of the registered NOSI be limited to the estimated retail value of the equipment". **There are several problems with this suggestion.**

First, the focus should be on the value of the security interest itself, not the NOSI. As explained above, the NOSI is simply the instrument used to register the security interest and, standing alone, it has no intrinsic value.

Secondly, there is no reason in principle why collateral should not be used to secure obligations additional to the purchase price of the collateral. This is common practice in other contexts and the PPSA itself clearly envisages such agreements. Furthermore, read literally, the suggestion in the Consultation Paper would preclude the equipment being used to secure interest charges and the like, an outcome that is presumably not intended.

Thirdly, the nature and scope of the secured obligation depends on the terms of the security agreement (not the NOSI) and the suggestion made in Question 6.3) would involve a substantial interference with the parties' freedom of contract.

Fourthly, it is clear by inference from ss. 63 and 64 of the PPSA (disposal of collateral and distribution of surplus) that the secured party's recovery rights are limited not to the retail price of the collateral but, rather, to the lesser of: (1) the value of the collateral at time the secured party sells it; and (2) the outstanding amount of the secured obligation at that time. It would be wrong as a matter of policy to enact a different rule for fixture security interests.

Where the collateral is a fixture, the secured party, instead of exercising its rights of seizure and sale under the PPSA, may prefer instead to wait until the house is put up for sale. The prospective buyer will require discharge of the NOSI as a condition of the purchase and the secured party may insist on payment of the secured obligation before it discharges the NOSI. In principle, and consistently with PPSA, ss. 63 and 64, the secured party should be limited to claiming the lesser of the value of the collateral on the agreed date for discharge of the NOSI and the outstanding amount of the secured obligation on that date.

Outside Ontario, this limitation is expressly acknowledged in the statute: see, for example, s. 36(13) of the Saskatchewan PPSA. Section 36(13) applies where a party holding a security interest in a fixture has priority with respect to the fixture over a mortgagee of the real property to which the fixture is attached. It provides that the mortgagee may retain the fixture "on payment to the secured party of the lesser of: (a) the amount secured by the security interest that has priority over that interest; and (b) the market value of the goods if the goods were removed from the land". The corresponding provision in s.34(7) of the Ontario PPSA is worded differently. It identifies the amount of the payment by reference to "the amount owing in respect of the security interest having priority over … [the mortgagee's] interest". This provision is less precise than the Saskatchewan version, but it probably means the same thing.

The Consultation Paper does not indicate whether abuses in this connection are prevalent. If they are, a possible response would be to amend the PPSA by providing that:

(1) A secured party may not demand, as a condition of discharging a NOSI, an amount that exceeds the lesser of:
    (a) The market value of the goods on the date the NOSI is discharged if the goods were removed from the land; and

(b) The outstanding amount of the secured obligation.

(2) Upon payment by the debtor of the amount referred to in subsection (1), the secured party must discharge the NOSI within 30 days.

(3) If a secured party fails to comply with subsection (2), the secured party shall, on written notice from the debtor, pay the debtor $500 and any damages resulting from the failure, which sum, and damages are recoverable in any court of competent jurisdiction.

(4) The debtor may use section [XX] [the proposed alternative NOSI discharge process in Part V.1] upon proof that the debtor paid the amount referred to in subsection (1).

For consistency with this proposed new provision and, in the interests of harmonization with the PPSAs in the other provinces, s. 34(7) of the PPSA should also be amended so that it reads the same as s. 36(13) of the Saskatchewan PPSA.

The plain language guide referred to in our response to Question 6.2) above should include a prominent and comprehensible explanation of the limits on the secured party's rights to the collateral and its obligation to file a discharge of a NOSI upon payment of the amount specified above.

Conclusion

Thank you for the opportunity to provide our comments and recommendations. As always, we welcome further discussion as you move forward.