

# Secured parties need to consider obtaining estoppel letters

Charles Rich and  
Melanie DeSouza, Student-at-Law,  
Fraser Milner Casgrain LLP

**Secured parties must now consider obtaining confirmation/estoppel letters from all prior registered secured parties, even where such prior creditors used limiting language in the collateral classifications inserted in their PPSA financing statements.**

In an effort to modernize Ontario's business laws, the province recently

amended several Ontario statutes, including the *Personal Property Security Act* (Ontario) (the "PPSA"). The changes to the PPSA are being implemented in stages, with the first amendments having come into effect on August 1, 2007.

## Check-the-box system

One of the amendments that has yet to be made is the removal of the "check-the-box" system for classifying collateral. Under the current PPSA system, a secured party must check-off up to six boxes on a PPSA financing statement to describe the collateral over which it has been granted a security interest.

Each box represents a class of collateral (i.e., consumer goods, inventory, equipment, accounts, other). No further description of the collateral in which an interest is being taken is required; however, a secured party also has the option of inserting a narrative description of the collateral in a separate box on the financing statement.

## All items in class of collateral

By simply "checking-the-box" all items within the class of collateral for which the box is checked are caught by the financing statement and therefore may be subject to the secured party's security interest, even if the

*See Secured and Unsecured Transactions, page 95*

# Secured and Unsecured Transactions *continued from page 94*

secured party has only been granted a security interest over certain collateral.

Thus, if an existing secured party has been granted a security interest over a particular piece of equipment, but simply checked-off the equipment "box" on its financing statement, a subsequent creditor seeking a security interest in collateral that falls into that class must assume that the prior registered secured party has been granted a security interest in such collateral.

## ***Estoppel to eliminate risk***

To eliminate this risk, the creditor would typically obtain a confirmation or *estoppel* from the prior registered secured party. Such a letter would limit the security interest of such prior secured party to the particular collateral over which it was granted a security interest. This process can be time consuming and can increase the cost of lending transactions.

## ***Narrative description***

The 'check-the-box' system is not used in any other jurisdiction in Canada or the U.S. When the contemplated amendments are implemented, Ontario's personal property registry system ("PPR") will mirror the systems of the other Canadian jurisdictions by requiring a secured party to submit a narrative description of the collateral by item or type.

## ***No collateral box***

There will no longer be any collateral "boxes" to check off. The new sys-

tem will significantly reduce (if not eliminate) the need to obtain *estoppels* from previous registered secured parties. Note that as the move to the narrative collateral description system will require significant changes to the Province's infrastructure and computer systems, it will take some time before it can come into effect (approximately one to two years).

## ***Revised s. 46(3)***

It was believed that the Province would hold off on making any changes to the PPSA which would affect the PPR until after the replacement of the 'check-the-box' system. However, one of the amendments made on August 1, 2007 was a substantial revision of s. 46(3) of the PPSA.

The "old" s. 46(3) stated that where a description of collateral was included in a financing statement by a secured party and such description limited the scope of the collateral classification, the secured party could only claim a perfected security interest in the collateral as limited by such description.

## ***No limits***

Due to the amendment of s. 46(3), the perfected security interests of secured parties are no longer limited by a general collateral classification that limits the scope of the collateral.

Consequently, unless a purchase money security interest is obtained, a secured party seeking a first priority security interest in a particular item within a class of collateral can no

longer be certain that a prior registered secured party's interest is limited to the description set out in the general collateral description box.

For example, if a creditor has been granted a security interest over a particular computer and on its financing statement checked the equipment "box" and inserted a general collateral description limiting the collateral to the particular computer, due to the amendment of s. 46(3), the creditor's financing statement could still perfect a security interest over *all* equipment of the debtor.

## ***Significance***

Secured parties must therefore consider whether they will require *estoppels* from prior registered parties with an interest in that class. In addition, there remains some uncertainty about whether the change to s. 46(3) impacts *all* PPSA registrations or only those filed on or after August 1, 2007.

The need to obtain additional *estoppel* letters unfortunately will increase the cost of certain financings as well as lengthen the time it takes to complete some financings.

There is hope that the problems created by the changes to s. 46(3) of the PPSA will be remedied by the Province in the coming months. However, until a solution is implemented, it is essential for secured parties to consider the need to obtain confirmations regarding PPSA registrations which are no longer limited by their general collateral descriptions.