

CITATION: Royal Bank of Canada v. Cutler Forest Products Inc., 2022 ONSC 6629
COURT FILE NO.: CV-22-00684833-00CL
DATE: 20221223

SUPERIOR COURT OF JUSTICE – ONTARIO

COMMERCIAL LIST

IN THE MATTER OF Section 101 of the *Courts of Justice Act*, R.S.O. 1990, c. C43, as amended, and in the matter of Section 243(1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B3, as amended

RE: Royal Bank of Canada, Applicant

AND:

Cutler Forest Products Inc., Respondent

BEFORE: Penny, J.

COUNSEL: *Roger Jaipargas*, counsel for the Applicant

Timothy C. Hogan and Robert Danter, counsel for Fuller Landau Group Inc., Receiver

Craig R. Colraine, counsel for Paccar Leasing Company Ltd.

HEARD: November 25, 2022

ENDORSEMENT

[1] The Fuller Landau Group Inc., in its capacity as Receiver appointed by order of Dietrich J. in August 2022, seeks three substantive heads of relief:

- an order approving the Second Report of the Receiver dated November 14, 2022 and the activities of the Receiver and its legal counsel;
- an order approving the professional fees and disbursements of the Receiver and those of its legal counsel; and
- the court's direction regarding the relative priority of the Royal Bank of Canada and PACCAR Leasing Company in respect of three leased trucks. Should the court find that the RBC's interest is in priority to that of Paccar, the Receiver seeks an order for the immediate return by Paccar to the Receiver of one of the trucks currently in Paccar's possession, the 2021 Kenworth T880.

[2] The first two of these items are not in dispute. The Second Report is approved (subject to the usual qualification that only the Receiver, in its personal capacity and only with respect to its own personal liability, shall be entitled to rely upon or utilize in any way the court's approval of the Receiver's report). The fees of the Receiver and its counsel are reasonable and are also approved.

[3] It is the third issue that is in dispute. As I will explain, the perfected security interest of the RBC must prevail over the unperfected security interest of Paccar. To this end, I order the immediate return to the Receiver, at Paccar's cost, of the 2021 Kenworth T880. I also authorize the sale and distribution of proceeds of all three trucks by the Receiver.

BACKGROUND

[4] The facts are not in dispute.

[5] The RBC is the senior lender of Cutler Forest Products Inc. (referred to as Cutler or the Debtor) with valid security and a priority registration under the Ontario *Personal Property Security Act*, R.S.O. 1990, c. P.10. It has a first in time registration as of April 2, 2007, including a General Security Agreement (GSA) over all of Cutler's present and after acquired personal property and undertaking, including "equipment".

[6] The Receiver of Cutler was appointed under s. 243(1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 and s. 101 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43. The receivership was over "all of the assets, undertakings and properties of the Debtor acquired for, or used in relation to a business carried on the Debtor, including the proceeds thereof". The Receiver was empowered by the order "to sell, convey, transfer, lease or assign" the property of the Debtor.

[7] Paccar leased three trucks to the Debtor:

2018 Peterbilt 337 for a term of 36 months;

2021 Kenworth T880 for a term of 84 months; and,

2021 Kenworth T270 for a term of 84 months.

[8] It is common ground that:

- Paccar's lease is a security interest within the meaning of the PPSA (Paccar being a lessor of goods under a lease for a term of more than one year);
- the PPSA applies to "every transaction without regard to its form and without regard to the person who has title to the collateral that in substance creates a security interest". This includes Paccar's truck leases;
- Paccar failed to perfect a security interest against the Debtor regarding the trucks until after the appointment of the Receiver. Regarding the Peterbilt and T880, it did not register against a named "debtor" and did not do so within the required 15 days

of the Debtor's possession. Regarding the T270, Paccar failed to register against a "Motor Vehicle"; it also failed to register within 15 days of the Debtor's possession;

- as a result of defects in its registrations, Paccar does not have a valid purchase money security interest (PMSI) in the trucks and does not have a perfected security interest in the trucks; and
- Paccar retained title to the trucks. Further, for the purposes of this motion, Paccar's leases on the trucks did not secure payment or the performance of an obligation. They are "true" leases.

[9] On October 12, 2022, the court issued an Approval and Vesting Order regarding the sale of Cutler's assets. The trucks were excluded from the sale and the AVO pending resolution of the priority and entitlement dispute between Paccar and the Receiver and the RBC.

Positions of the Parties

[10] Paccar argues that:

- the Paccar truck leases are "true" leases, in that they do not secure payment or the performance of an obligation. The trucks, therefore, do not form part of the property of the Debtor within the meaning of the Receivership Order. As a result, the trucks cannot be sold or disposed of by the Receiver;
- its unperfected security interests in the trucks are valid against the Receiver under the provisions of s. 20(1)(b) of the PPSA because the Receiver is not a trustee in bankruptcy and does not "represent the creditors" of the Debtor;
- the Receiver's proposed sale of the trucks is a form of enforcement on the RBC's security. Part V of the PPSA, dealing with rights and remedies on default, only applies to a security interest if it secures "payment or performance of an obligation". For the purposes of this motion, it is not disputed that Paccar's leases of the trucks do not secure the payment or performance of an obligation. They are "true" leases and are, Paccar argues, exempt from the enforcement provisions of Part V.

As a result, Paccar argues, neither the RBC nor the Receiver ever had a right to enforce against the trucks because the Debtor never had a proprietary interest in the trucks to begin with. Cutler was never more than a mere lessee. Paccar was, and remains, the owner of the trucks and is entitled to their return.

[11] The Receiver, supported by the RBC, argues that:

- the 2007 amendments to Ontario's PPSA unambiguously brought "true" leases within the PPSA registration system. Paccar's interest as lessee of the trucks became registerable. Its priority could have been, but was not, preserved by the registration of a PMSI in the prescribed manner and within the prescribed time. Having failed to perfect its security interest, Paccar's interest in the trucks became

subordinated to the RBC's prior in time, perfected security interest in the Debtor's property (which included the trucks – the Debtor's right to exclusive possession under the lease being a form of property). Paccar's interest in the trucks, as a result, can only be realized after the RBC interest has been paid in full;

- Paccar's arguments rely on a pre-2007 understanding of the effect of the PPSA registration system. The focus is no longer on matters of title or ownership (i.e., the "true" lease question) but on priority of registration;
- section 20(1)(b) of the PPSA has no application. The Receiver is not asserting its own independent interest in the trucks. It is merely seeking the direction of the court based on its understanding of the law. It is the RBC's registration and interest, not the Receiver's, which is at stake here; and
- Part V of the PPSA is irrelevant to these proceedings. Neither the Receiver nor the RBC seek to rely on statutory remedies under the PPSA.

ANALYSIS

True Lease/The Role of Ownership

[12] While it is true that the PPSA has not entirely done away with the concept of a "true" lease (that is, a lease not for the purpose of securing performance or payment of an obligation), it is important to understand how, since 2007, the PPSA has fundamentally changed the law around the preservation and priority of a lessor's interest. That is what I shall address in the first section of this analysis.

[13] As the Court of Appeal for Saskatchewan wrote in *International Harvester Credit Corp. of Canada v. Bell's Dairy Ltd. (Trustee of)*, (1986), 30 D.L.R. (4th) 387 (Sask. C.A.), the law has long been concerned with security transactions under which title to goods rests with one person (the true owner), while their possession is enjoyed by another (the ostensible owner). The potential for mischief in such arrangements is obvious, a fact which prompted early legislation dealing with the two most frequently encountered instances: chattel mortgages and conditional sales. This early legislation, however, did not apply to a true lease of goods (as distinct from a security transaction in the form of a lease). This form of dealing – the true lease – in which title and possession are separated, was left to the common law. As a general rule, the common law did not allow the lessor's title to leased goods to be defeated through some dealing by the lessee. All this changed, however, when the PPSA (in Ontario, in 2007) brought about far-reaching statutory changes to the common law.

[14] The object of the PPSA is to modernize and consolidate the law of personal property as security for debts, so as to provide an orderly, predictable system for taking and enforcing security interests. The scope of the statute includes all transactions, regardless of their form and irrespective of the intention of the parties, that either create or are deemed to create a security interest in personal property and fixtures. In Ontario, since 2007, the law treats true leases of goods as though the parties had intended the property to serve as security for the amounts owing by lessee. This is a singularly important departure from the law as it existed before this Act came into being.

[15] The legislature has, by enacting the PPSA, set aside traditional concepts of title and ownership to a certain extent. Property rights subject to provincial legislation are what the legislature determines them to be. This is precisely what was done in the PPSA, which implemented a new conceptual approach to the definition and assertion of rights in and to personal property. Priority and realization under the PPSA revolve around the central statutory concept of a “security interest”. The rights of parties to a transaction that creates a security interest are explicitly not dependent on either the form of the transaction or upon traditional questions of title. They are defined by the PPSA itself: see also *Giffen (Re)*, [1998] 1 S.C.R. 91, at para. 26.

[16] A “security interest” under the PPSA embraces the interest of a lender on the security of goods, a seller of goods on time, a consignor and, in the case of a commercial lease exceeding one year in duration, a lessor. These persons share one thing in common under the statute: each has an interest, rooted in title, to some particular goods in another’s possession. Generally speaking, that interest, *once perfected*, will entitle its holder, in the event of default, to look to the goods ahead of anyone else to satisfy their claim.

[17] Relevant to this case, the PPSA:

- defines a “debtor” to include a “lessee of goods under a lease for a term of more than one year” (s. 1(1));
- applies to “every transaction without regard to its form and without regard to the person who has title to the collateral that in substance creates a security interest...” (s. 2(a));
- applies to “a lease of goods under a lease for a term of more than one year even though the lease may not secure payment or performance of an obligation” (s. 2(c));
- defines a purchase money security interest to include “the interest of a lessor of goods under a lease for a term of more than one year” (s. 1(1)); and
- provides that a PMSI has priority over any other security interest in the collateral if the PMSI was perfected within 15 days of the debtor taking possession (s. 33(2)).

[18] Thus, the PPSA provided Paccar with the means of preserving the priority of its interest in the trucks over the interest of the RBC under its GSA. As I will discuss, however, Paccar failed to act on this opportunity.

[19] With this general understanding, I will first turn to the question of the effect of s. 20(1) of the PPSA on the analysis of this dispute.

Section 20(1) of the PPSA

[20] As noted above, a lessor of goods for a term exceeding one year in duration is deemed to have a security interest which, *if perfected*, generally permits lessors to look to the goods ahead of anyone else to satisfy their claim.

[21] A security interest is perfected once it has attached and all steps required for perfection have been completed (s. 19). A security interest attaches when value is given or the debtor has rights in the collateral (s. 11). Registration perfects a security interest in any type of collateral (s. 23).

[22] Section 20 of the PPSA contains two relevant provisions governing priority of security interests. Section 20(1)(a)(i) provides that, until perfected, a security interest is subordinate to the interest of a person who has a perfected security interest in the same collateral.

[23] Section 20(1)(b) provides that, “until perfected, a security interest in collateral is not effective against a person who represents the creditors of the debtor, including an assignee for the benefit of creditors and a trustee in bankruptcy.” The Court of Appeal held in *Royal Bank of Canada v. 1231640 Ontario Inc. (Trustee of)*, 2007 ONCA 810, 289 D.L.R. (4th) 684, that a receiver, because it does not take title to the property of the debtor (unlike a trustee in bankruptcy), does not qualify as a “person who represents the creditors of the debtor” within the meaning of s. 20(1)(b).

[24] To paraphrase the Court of Appeal for Saskatchewan in *International Harvester*, at paras. 33 and 34, when left unperfected, a security interest is decidedly vulnerable. A third party may derive an interest in the same goods by virtue of some dealings with the person in possession of them, and, depending on who the third party is (i.e., if they are one of the persons mentioned in s. 20(1)), they may become entitled to priority over the lessor. That is, they may become entitled, ahead of the person holding the unperfected security interest, to look to the goods to satisfy their claim. In Ontario, this includes, since 2007, goods in the possession of a person pursuant to a lease for a term exceeding one year.

[25] Absent perfection of their security interest, therefore, a commercial lessor of goods on a lease whose term exceeds one year may find itself standing in line behind a person referred to in s. 20(1)(a)(i); namely, a person with a perfected security interest in the same collateral. That is the thrust of s. 20 and the perfection, attachment and registration regime under the PPSA.

[26] Here, although Paccar did attempt to file financing statements with respect to the trucks, there is no question that Paccar failed to register a valid security interest; Paccar’s interest was not perfected. This is admitted. Thus, Paccar holds an *unperfected* security interest in the trucks. On its face, Paccar’s security interest in the trucks is, by virtue of s. 20(1)(a)(i), subordinate to the interest of the RBC which has a perfected security interest in the same collateral.

[27] Paccar relies, however, on the exclusion of the Receiver from the effect of s. 20(1)(b) since the Receiver is not a trustee in bankruptcy and does not “represent the creditors” of the Debtor. It argues that its unperfected security interest *is*, by virtue of s. 20(1)(b) and *Royal Bank*, effective against the Receiver.

[28] The problem with this argument is that it ignores s. 20(1)(a)(i). The RBC in this case has a perfected security interest in the trucks, by virtue of its first in time GSA covering all the Debtor’s property. The Receiver is not purporting to bring a personal claim for the right to sell the trucks. It is asking for the court’s direction on whether Paccar’s unperfected security interest in the trucks

is subordinate to the RBC's perfected security interest, such that the RBC must be paid its loan from the Debtor's property before Paccar's debt can be paid.

[29] Whether Paccar's unperfected security interest is effective against the Receiver, therefore, does not address, and does not resolve, the central question – “is Paccar's unperfected security interest effective against the RBC?”

[30] In my view, due to Paccar's failure to avail itself of the protection, under s. 33(2), of perfecting a valid PMSI, its *unperfected* security interest is subordinate to the prior, *perfected* security interest of the RBC under the GSA. It matters not whether Paccar's unperfected security interest is effective against the Receiver *per se*.

Section 57.1 and the Exemption from Part V

[31] This brings me to the second argument advanced by Paccar; that ownership rights attaching to a “true” lease are preserved by Part V of the PPSA, dealing with statutory rights and remedies on default.

[32] Section 57.1, (which begins Part V) provides that Part V applies to a security interest *only* if it secures payment or performance of an obligation. In other words, Part V of the PPSA does not “apply” to a true lease.

[33] This raises the question of what s. 57.1 means. How do the rights and remedies on default under Part V interact with the priority of security interests laid out in such detail in Parts II, III and IV? And, what does it mean for Part V not to “apply” to a true lease of the trucks?

[34] Paccar says s. 57.1 means that its reservation of title under a true lease trumps all. Neither the Receiver nor the RBC can exercise rights or remedies against the trucks, regardless of Paccar's failure to perfect and the RBC's superordinate perfected security interest in the trucks. The trucks must be turned over to Paccar due to its residual ownership under the leases.

[35] The Receiver says that Part V is irrelevant to these proceedings. Neither the Receiver nor the RBC is seeking to exercise any rights or remedies under Part V of the PPSA. Rather, the RBC has sought and obtained relief under s. 243(1) of the BIA and s. 101 of the CJA.

[36] Section 57.1 has similar replications in most provinces' PPSAs. It appears, however, that the meaning and effect of s. 57.1 have received little judicial consideration; the issue posed in this case appears to be a matter of first impression.

[37] To address this uncertainty over the meaning and effect of s. 57.1, I shall first review the correct approach to the interpretation of statutes. I shall then outline what Part V of the PPSA is and what it does. Then, I will turn to the critical question at hand – does the fact that Part V does not “apply” to a true lease mean, as submitted by Paccar, that Paccar's reservations of title prevail over the perfected security interests of the RBC such that the RBC cannot enforce its superordinate interest in priority to Paccar?

[38] The modern principle of statutory interpretation, commonly called the “text, context and purpose” principle, is now well settled. It was set out in *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1

S.C.R. 27, at para. 21, and followed in *Bell ExpressVu Limited Partnership v. Rex*, 2002 SCC 42, [2002] 2 S.C.R. 559, at para. 26, citing Driedger, Elmer A., *Construction of Statutes*, 2nd ed. Toronto: Butterworths, 1983 at p. 87: “[T]he words of an act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.”

[39] In essence, Part V establishes, for personal property, the remedies of possession, power of sale and foreclosure analogous to mortgage remedies. On default, the secured party has the right to take possession of the collateral (s. 62). The secured party also has the right, on notice, to dispose of the collateral (s. 63). The secured party has the obligation to account and Part V governs the distribution of any surplus upon disposition (s. 64). The remedy of foreclosure is available regarding consumer goods (s. 65). And, the debtor may, at any time prior to disposition, redeem the collateral upon tendering payment of all obligations secured by the collateral (s. 66). Notably, nothing in Part V (a) prevents a secured party from applying to the court for the appointment of a receiver (s. 60), and (b) affects the registration and priority scheme established in Parts II, III and IV.

[40] Part V, therefore, essentially establishes a scheme of “self-help” rights and remedies which operate without the need for court intervention. At the same time, the ability to seek court intervention by means of a receivership application is expressly preserved.

[41] From reading these provisions as a whole, I conclude that s. 57.1, in stipulating that Part V does not apply to a true lease, means that the statutory self-help rights and remedies enumerated in Part V do not apply to a true lease; that is, not to the lease, and not to the lessor or the lessee.

[42] This does not mean, however, as argued by Paccar, that its unperfected reservation of title to the trucks under a true lease defeats any perfected security interest in the same collateral. Paccar’s argument, if successful, would entirely defeat the purpose of bringing commercial leases of personal property for a term of more than one year within the registration and perfection scheme of the Act in 2007. That purpose, to reiterate, arose from the potential for mischief in security transactions under which title to goods rests with one person (the true owner), while their possession is enjoyed by another (the ostensible owner). The object of the PPSA is to modernize and consolidate the law of personal property as security for debts and provide an orderly, predictable system for taking and enforcing security interests. Paccar’s argument requires interpreting s. 57.1 as nullifying the effect of the very registration and perfection requirements that the same 2007 amendments imposed upon the lessor of personal property for a term of more than one year. That is not an intention I am prepared to attribute to the legislature.

[43] Rather, I find that the RBC’s application for the appointment of the Receiver does not fall within the ambit of Part V. There is no suggestion here of the RBC seeking to exercise self-help remedies under Part V to realize on collateral after default. As expressly contemplated by s. 60 of the PPSA, the RBC chose not to exercise self-help remedies of possession and disposition in favour of a court-supervised process of realization under the BIA and the CJA. Part V, therefore, has no application to the facts of this case.

[44] The circumstances of this case are essentially indistinguishable from the decision of Yamauchi J. of the Court of Queen’s Bench of Alberta in *Wells Fargo Foothill Canada ULC v.*

Big Eagle Hydro-Vac Inc., 2015 ABQB 546, 21 Alta. L.R. (6th) 236. In that case, Wells Fargo held a perfected security interest over all of the property of Big Eagle under a GSA. Wells Fargo obtained an order of the court appointing a receiver. The receiver sought to dispose of the property of the debtor. The lessor of certain equipment objected on the basis that it held title to the equipment (although it had not perfected its security interest). In those circumstances, the Alberta court concluded that the unperfected interest of the equipment lessor was subordinate to the perfected security interest of Wells Fargo. The court asked whether this was “fair” to the lessor. The answer was “Yes” because the lessor could have protected its position by taking a PMSI in the collateral. As a result, the receiver was entitled to dispose of the equipment.

[45] To similar effect is the decision of the Court of Queen’s Bench of Alberta in *1777575 Alberta Ltd. v. Sprung Instant Structures Ltd.*, 2014 ABQB 354, 14 C.B.R. (6th) 52. There, the court addressed the issue of priority between the perfected general security of a creditor and an unperfected lessor of a financing lease. In its decision, the court unambiguously stated that its findings would have been equally applicable to a “true” lease. The PPSA created a “priority based approach” which did not rely on common law notions of who actually had title to the collateral. Sprung, the unperfected lessor, “ignored, at its peril, the fundamental changes effected by the statute in relation to ownership interests in personal property”: at para. 15.

[46] Paccar would distinguish *International Harvester* and *Giffen* on the basis that they concerned special priorities between a trustee in bankruptcy and other security interests, whereas in this case there is no trustee. While it is true that those cases involved a trustee and this case does not, the courts’ basic analysis of the intended purpose and operation of the PPSA in those cases does not turn on the unique status of a trustee in bankruptcy. This point is emphasized by the Court of Queen’s Bench of Alberta in *Sprung*. At para. 19, the court pointed out that the only reason there is so much emphasis in *Giffen* on the effects of PPSA legislation in bankruptcy is because that case dealt with a bankruptcy. However, the court also noted that nothing in the Supreme Court of Canada’s decision in *Giffen* restricts its analysis of the “title effects” of the amendments to the PPSA (bringing leases of personal property for a term of more than one year into the registration and perfection regime) to a bankruptcy situation. Indeed, at para. 54 of *Giffen*, the court recognized “that, for the purposes of priority, the PPSA replaces the common law principle that one cannot transfer better title than she possesses. It is a policy choice of the legislature that an unsecured creditor’s position, as represented by the trustee, is more meritorious than the unperfected security interest of a secured creditor.” This extract, said Veit J. in *Sprung*, at para. 19, “demonstrates that it is the PPSA, not the BIA, which has changed the common law relating to title; proceedings under the BIA can, of course, take advantage of that change.”


CONCLUSION

[47] For these reasons, I find that the RBC’s perfected security interest prevails over Paccar’s unperfected security interest as lessor. To this end, Paccar is required, at its own cost, to deliver to the Receiver immediately the 2021 Kenworth T880. The Receiver is authorized to sell all three trucks (subject to the usual accounting after sale and disposition of any surplus proceeds).

[48] The Second Report of the Receiver is approved (subject to the now standard *Target* qualifications). The fees of the Receiver and its counsel are reasonable and are also approved.

COSTS

[49] The Receiver sought no costs. None are ordered.


_____ Penny, J.

Date: December 23, 2022