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The Influence of the ULSIA on the Proposed New Brunswick Land Security Act

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Norman Siebrasse* and Catherine Walsh**

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I. INTRODUCTION

The Uniform Land Secured Interest Act ("ULSIA")¹ may well be the proverbial "prophet [which] hath no honour in [its] own country."² Although apparently not yet adopted by any of the United States, it provided the Canadian authors of this paper with a valuable resource in the development of our just-completed "Proposal for a New Brunswick Land Security Act".³ The actual prototype for the Land Security Act ("LSA") was the

1. U.L.S.I.A., 7A U.L.A. 220 (Supp. 1995).

2. See *John* 4:44 (King James).

3. NORMAN SIEBRASSE & CATHERINE WALSH, NEW BRUNSWICK GEOGRAPHIC INFORMATION CORPORATION, TENTATIVE PROPOSAL FOR A NEW BRUNSWICK SECURITY ACT

province's recently-proclaimed Personal Property Security Act ("PPSA").⁴ However, the New Brunswick PPSA was derived from PPSAs previously enacted elsewhere in common law Canada,⁵ all of which were derived, in turn, from Article 9 of the Uniform Commercial Code.⁶ Because the ULSIA was inspired by Article 9, it was of obvious and direct relevance to our own efforts to simplify and consolidate land security law along modern personal property security lines.⁷

(Feb. 1996) [hereinafter SIEBRASSE & WALSH]. The proposal was commissioned by the New Brunswick Geographic Information Corporation, the Crown corporation responsible for the administration of real and personal property registration in the province. The proposal has not yet been accepted by the government of the province, and consequently nothing in this article can be taken to reflect official policy of the province. We owe a great debt both in terms of conceptual inspiration and detailed advice to Rod MacKenzie, the Vice President, Legal, of NBGIC and to Mary Kimball, Deputy Registrar of Deeds and Registrar of Land Titles for the province. However, they do not necessarily share all of the views expressed in this article.

4. Personal Property Security Act, S.N.B. ch. P-7.1 (1993), *amended by* ch. 22, 1994 S.N.B. 1 & ch. 33, 1995 S.N.B. 1 (Can.). For a section-by-section review of the purpose and operation of the Act, see CATHERINE WALSH, *AN INTRODUCTION TO THE NEW BRUNSWICK PERSONAL PROPERTY SECURITY ACT* (1995).

5. PPSAs derived from Article 9 are in operation currently in seven Canadian jurisdictions: in Ontario, R.S.O. ch. P-10 (1990) (Can.); in Manitoba, R.S.M. ch. P-35 (1987) (Can.); in Saskatchewan, S.S. ch. P-6.2 (1993) (Can.); in the Yukon Territory, R.S.Y. ch. 130 (1986) (Can.); in Alberta, S.A. ch. P-4.05 (1988) (Can.); in British Columbia, S.B.C. ch. 36 (1989) (Can.); and now New Brunswick, S.N.B. ch. P-7.1 (1995). The legislation is not entirely uniform from one jurisdiction to the next. Note that the Northwest Territories and Nova Scotia have both enacted PPSAs, with implementation expected sometime in 1996, once the electronic personal property registries now under construction in each jurisdiction are complete; differences in the computer and legal environment in each jurisdiction coupled with the rapid pace of technological change have made it impossible for new PPSA jurisdictions to simply import the registry software already in use in an existing PPSA jurisdiction. S.N.W.T. ch. 8 (1994) (Can.); S.N.S. ch. 13 (1995-96) (Can.). In addition, Book 6 of Quebec's new Civil Code establishes rules for conventional hypothecs on movables which, while reflecting the property concepts and legal style of that province's civilian legal tradition, also contains many substantive features that will be familiar to lawyers versed in Article 9/PPSA law. See C.C.Q. book 6, tit. 3, ch. 2, § IV, arts. 2702-2709 (1994) (Can.). This leaves only two Canadian jurisdictions, Newfoundland and Prince Edward Island, without a reformed personal property security law either in operation or pending proclamation.

6. U.C.C. art. 9 (1977). For an American perspective on the Canadian counterparts to Article 9, see Bernard J. Roth, *Article 9 North of the 49th: Its Development in Canada's Personal Property Security Acts*, 27 UCC L.J. 251 (1995).

7. Another valuable resource was the ONTARIO LAW REFORM COMMISSION, MINISTRY OF THE ATTORNEY GENERAL, *REPORT ON THE LAW OF MORTGAGES* (1987) [hereinafter OLRC REPORT].

In any law reform project, the initial gathering of political and institutional support for change is often the greatest challenge. Therefore, this article begins its comparative review of the ULSIA and its Canadian relative with a brief explanation of why the drafters think New Brunswick offered a hospitable climate for the reform of land security law at this particular time.

II. THE REFORM CONTEXT

New Brunswick, with a population of only about three quarters of a million people and located in the geographically and politically marginalized Atlantic Region, is traditionally one of Canada's "have-not" provinces. In 1987, the Liberal Party swept to power under the leadership of Premier Frank McKenna, with a strong mandate to "open the province for business," while increasing government efficiency and eliminating deficit financing. But clearly, if the government was to achieve its primary goal to attract business investment, it could not also reduce the cost of governing if this meant a concomitant decline in the quality of the province's already fragile business infrastructure. So while steps were taken to reduce the size of government, they were accompanied by significant institutional changes intended to improve the efficiency with which government services were delivered. To a significant extent, "re-engineering government" in New Brunswick proved to be more than a slogan to mask indiscriminate across-the-board cuts.

The institutional change relevant to the creation of New Brunswick's proposed LSA was the creation of a Crown corporation, New Brunswick Geographic Information Corporation, which is responsible for operating the real and personal property registration systems in the province.⁸ In Canadian legal parlance, a Crown corporation is a corporation wholly owned by the provincial or federal government that legislates it into existence. Legally, it remains an agent of the government but in structure and operation it is given a significant degree of autonomy akin to that enjoyed by a private corporation with the aim of achieving service to its clientele on a cost-recovery basis. It is true that in any monopoly, and particularly a publicly-owned monopoly, service to clients and cost-recovery can be

8. See New Brunswick Geographic Information Corporation Act, S.N.B. ch. N-5.01 (1989) (Can.). The corporation also has responsibility for real property tax assessment information and for the province's geographic information database, a consolidation of responsibilities that is meant to allow land registry information to be incorporated and updated efficiently with the physical and fiscal cadastre. *Id.* § 4.

hollow mottos, but in the authors' perhaps biased experience, they have been taken to heart in the case of New Brunswick Geographic Information Corporation ("NBGIC").

NBGIC's first major initiative in the secured financing area was to contract for the construction of a Personal Property Registry ("PPR") to support the implementation of the province's Article 9-inspired PPSA.⁹ However, reform of the province's cumbersome and antiquated land registration system was also a standing item on the corporation's agenda. Additionally, and in the prevailing atmosphere of budget and resource constraints, it struck the vice president for legal policy that at least some aspects of the work done on the PPSA/PPR project might well perform double duty on the land security side.

From the corporation's perspective, perhaps the most immediately attractive feature of the PPSA approach was its replacement of "document-filing" with "notice-filing." Rather than having to file a copy of the actual mortgage or other security documentation in the PPR, secured parties simply enter a notice of the security agreement¹⁰ that contains only the bare information necessary to alert a searcher of the possible existence of a security interest in the described collateral. If notice-filing was carried over to land security interests, there was no reason to think that it would not produce the same advantages as had been demonstrated by experience in PPSA jurisdictions. These advantages include: a reduced administrative and archival burden on the registry; greater flexibility in the drafting, amendment, and rollover of security agreements; enhanced confidentiality of the debtor's financial affairs; and simplified informational requirements for registration with a correspondingly reduced risk of invalidating error.

9. Personal Property Security Act, S.N.B. ch. P-7.1. In May 1987, the Law Society of New Brunswick, the self-regulating professional organization that represents the province's lawyers, recommended the enactment of a modern PPSA to the province's Attorney General. That recommendation fit well with the new government's expressed desire to create a positive and efficient business environment for outside investment and a PPSA proposal was commissioned. Draft legislation, adapting the western Canadian version of the PPSA to the New Brunswick legal and policy environment, was submitted to the Department of Justice in August 1993 and, following approval by the department's former law reform division, turned over to NBGIC for implementation. One of the authors of this paper, Walsh, was the author of the PPSA proposal and worked closely with NBGIC in its implementation. The other author of this paper, Siebrasse, has been the corporation's principal external research and policy advisor on land law issues.

10. The agreement is called a "financing statement," in compatibility with the Article 9 terminology. See S.N.B. ch. P-7.1, § 1.

A second appealing feature of the PPSA registry model was its relatively sophisticated registration and searching capabilities. Registrations in the PPR are entered directly by clients¹¹ into a computerized data-base that is indexed and searchable according to debtor name as well as collateral serial number in the case of 'large ticket' goods for which a reliable serial number is universally available.¹² In contrast, although a land titles registry indexed by parcel identification number operates in one county in New Brunswick,¹³ the principal land registry is an antiquated deed depository system organized according to a rudimentary grantor/grantee index.¹⁴ While considerable developmental work had been done on the automation of the land records through the use of scanning and optical disk storage, it became increasingly clear to certain of NBGIC's senior administrators that a full electronic conversion of the mechanics of registration and searching coupled with a redesign of the indexing structure was needed. Thus, in the short term, adaptation of the PPR model to the land context presented a welcomed opportunity to implement a geographic parcel indexing system for the whole province, without having to make a wholesale conversion from a deed registry to a land titles system. In the long term, it might even be possible to adapt the PPR software design to at least the security aspects of the land records, thereby effecting a partial conversion

11. While all the Canadian PPSA registries incorporate an electronic database, New Brunswick has gone somewhat further than its sister jurisdictions in making the system completely client-administered. Clients are wholly responsible for entering their own registrations into the registry database and for conducting their own searches with direct access made available either through computer terminals located in each of the 15 registry offices maintained by NBGIC in the province or from the client's own premises in the case of frequent users who have the resources and demand to establish the necessary on-line communication links. Direct electronic access benefits both system administrators and system users: administrators benefit because the legal responsibility for and administrative burden of registration is transferred wholly to the client, and users benefit because the time lag between submission of the relevant information to the registry and its entry in the database is eliminated, enabling registrants to control the effective time of registrations and searchers to obtain search results on "real time."

12. The general regulation under the PPSA, S.N.B. ch. P-7.1, Reg. 95-57 (1995) (Can.), currently defines "serial numbered goods" to mean motor vehicles (including combines, tractors, and road building machinery), trailers, mobile homes, boats, outboard motors for boats, and aircraft (as there is no national aircraft register yet in place at the federal level in Canada). Serial number searching is considered essential to ensure disclosure of a security interest granted by a predecessor in title of the immediate transferor of goods-collateral since a search according to the more usual debtor name criterion will not disclose the registration.

13. Land Titles Act, S.N.B. ch. L-1.1 (1981) (Can.).

14. Registry Act, R.S.N.B. ch. R-6 (1973) (Can.).

to electronic registration and searching without having to incur the heavy costs normally associated with ground-up software development.

A final important impetus to NBGIC's commissioning of the LSA proposal was the ready availability and adaptability of the PPSA substantive law model. The corporation recognized that it would be more efficient to simply codify land security law along PPSA lines, using the experience and resources it had recently developed, than to try to rewrite the existing complex statutory and judicial rules to fit a modern registration environment, or to develop a new substantive code from scratch. Of course, the PPSA model was also thought to offer an appropriate model, even independent of efficiency concerns. The legislation had already proved its substantive worth in the personal property financing context. Moreover, prior to the PPSA, the rules governing the relations of debtor and secured party were practically identical in the two contexts. Thus, harmonization of land security law with the PPSA would respect the historical identity between the two contexts, while greatly simplifying the legal process for secured financing. This is particularly true in the field of commercial transactions, where real and personal property are routinely assigned as common collateral for the same debt.

III. ORGANIZATIONAL STRUCTURE OF THE LSA

Just as the ULSIA¹⁵ adopts the organizational framework of Article 9,¹⁶ the proposed New Brunswick LSA¹⁷ adopts that of the PPSA.¹⁸ The act is therefore divided into seven parts, roughly chronicling the various stages through which a security interest may pass, from its initial attachment and perfection through to its enforcement as against both the debtor and third parties.

Parts I, II, and V correspond generally with parts 1, 2, and 5 of the ULSIA. Part I, "Interpretation and Application," defines terms, establishes interpretation principles, and delineates the scope of application of the act. Part II, "Validity of Security Agreement and Rights of Parties," addresses the pre-default relationship of the secured party and debtor, including the formality and evidentiary rules governing their security agreement, the validity of future advance clauses and the requirements for attachment of an effective security interest. Part V, "Default Rights and Remedies," codifies

15. U.L.S.I.A., 7A U.L.A. at 220.

16. U.C.C. art. 9 (1977).

17. SIEBRASSE & WALSH, *supra* note 3.

18. S.N.B. ch. P-7.1.

the procedural and substantive obligations of both parties, should the debtor's default necessitate enforcement of the security agreement.

Although part III of the LSA and part 3 of the ULSIA both cover "Perfection and Priorities," the LSA coverage is far more comprehensive.¹⁹ As a model uniform act that must be integrated with individual state land law policy and systems, the ULSIA is forced to defer to the registration statutes of the various states on issues of perfection and priorities. In contrast, as the law reform initiative of a single jurisdiction, the New Brunswick LSA incorporates a comprehensive self-contained perfection and priority regime to regulate ranking, both as among consensual security interests and as against other classes of proprietary claims.²⁰

Part IV of the LSA, "Registration," deals with the procedural and substantive aspects of registering and searching land security interests, consistent with New Brunswick's decision to effect reform of the registration framework as part of its general reform of land financing law.²¹ The LSA has no equivalent to part IV of the ULSIA on "Maximum Finance Charges and Usury." Issues under these heads were considered to be adequately regulated by the competitive market, supplemented by existing statutory and equitable sources, such as the provincial Unconscionable Transactions Relief Act.²²

Part VI of the LSA, "General and Miscellaneous," addresses such significant general issues as the applicable supplementary law, the parties' overriding obligations to conduct themselves in good faith and in a commercial reasonable manner, and civil liability for breach of any statutory obligation imposed by the act.²³ Part VII, "Transitional," establishes rules to regulate perfection and priority in transitional situations involving pre-LSA security interests.²⁴

The balance of this paper compares the LSA with the ULSIA in a relatively detailed fashion. In the interest of conserving space, the authors have emphasized the differences rather than the similarities between the two acts. In general, if no mention is made of a particular provision of the ULSIA, it is because the LSA is substantially identical to the ULSIA on that point.

19. See SIEBRASSE & WALSH, *supra* note 3, at 33-65.

20. *Id.*

21. *Id.* at 66-84.

22. R.S.N.B. ch. U-1 (1973) (Can.).

23. SIEBRASSE & WALSH, *supra* note 3, at 137-46.

24. *Id.* at 147-57.

IV. INTERPRETATION AND SCOPE OF APPLICATION

A. *Generic Functional Terminology*

Like the ULSIA, the LSA adopts generic terminology consistent with the Article 9/PPSA functionalist approach to the conceptual structure of secured financing.²⁵ Regardless of whether a particular transaction involves a conventional mortgage or some less self-identifying form of security, the interest created is uniformly referred to as a security interest if its substantive function is to secure payment or performance of an obligation. Generic terminology is carried over to the identification of the parties ("secured party" and "debtor"), their underlying contract ("security agreement"), and the property that is the subject of the security interest ("collateral").

The substitution of a functionalist approach to the characterization of security interests in land does not constitute as radical a departure from the *status quo* as the same change presented in the personal property security area. The significantly more complex nature of personal property made the evolution of personal property security law a correspondingly complex process with different security devices developed over the years for different categories of property. Thus, the PPSA introduced a rationalizing influence into what had become an extraordinarily fragmented and confused area of the law.²⁶ In contrast, secured financing against land, at least in common law Canada, is relatively straightforward and typically involves the use of one of only two relatively well-understood transactional forms, the mortgage or the equitable charge, the legal characteristics of which have become largely assimilated over the years. Although not unknown, the use of other transactional forms, such as agreements of sale and lease, is rare in contemporary practice. This rarity reflects the dominance of the Canadian chartered banks in the secured lending field, a dominance which is owed in part to the privileged position chartered banks were afforded from an early date under federal banking legislation, and in part to the diminished risk they face in low equity financing transactions because of the ready availability of mortgage insurance under the Canada Mortgage and Housing Corporation Program.²⁷

25. *See id.*

26. *See* Personal Property Security Act, S.N.B. ch. P-7.1.

27. *See* JAMES E. HATCH, *THE CANADIAN MORTGAGE MARKET* (1975).

B. *General Scope of Application*

The application of the LSA, like the ULSIA, is restricted to *consensual* transactions that function to create a *security* interest in land. But while non-consensual and non-security transactions are thus excluded from the direct reach of both regimes, the comprehensive sweep of the LSA's part III priority code means that the proposed legislation will nonetheless apply to resolve ranking between a consensual security interest and all forms of competing third party interests in the collateral, whether consensual or secured in character.²⁸ Moreover, complementary amendments to existing legislation will authorize the registration on a notice-filing basis of a variety of non-consensual "security interests" in land (e.g., the claim of a judgment creditor of the debtor), as well as integrate the rules governing their priority and enforcement with the substantive and policy framework of the LSA. In the longer term, it may become feasible to bring tax liens within the scope of the act. At present the greatest impediment to registration of tax liens is the administrative burden which would be involved in registering large numbers of the liens annually. But because the records of the taxation office are computerized, and it is anticipated that the LSA will soon be automated, registration of a tax lien in the LSA system can potentially be as administratively convenient as entering it in the current records of the taxation office. In this indirect way, the LSA is intended, to a far greater extent than the ULSIA, to establish the legislative basis and impetus for a comprehensive consolidation of the law governing the rights of all classes of creditors (outside of bankruptcy, which is federally regulated) against the debtor's land.

C. *Application to Security Interests in Land-Related Rights to Payment*

A significant issue in the United States has been whether an assignee's security interest in a note and mortgage must be perfected according to local real estate law, in addition to perfection under Article 9. This issue has not arisen in Canada because the promise to pay and the security interest are generally evidenced by a single document, and real property law clearly governs its assignment. The LSA and PPSA are complementary in their scope: the LSA applies to any instrument creating a security interest in land or land-related interest (e.g., a right to a stream of rental payments, or payments owing under a mortgage) where the land is specifically identified

28. SIEBRASSE & WALSH, *supra* note 3, at 33-65.

in the instrument. The PPSA applies in all other cases. Thus assignment of mortgage-backed securities is governed by the PPSA, but assignment of a specific mortgage is governed by the LSA.

V. VALIDITY OF SECURITY AGREEMENT AND RIGHTS OF PARTIES THERETO

A. *Freedom of Contract in the Making of a Security Agreement*

The LSA closely tracks the ULSIA in affirming freedom of contract.²⁹ The LSA provides that the agreement is effective according to its terms, unless otherwise provided in the LSA or any other act. In addition, it specifically abolishes doctrines relating to clogs on the equity of redemption and collateral advantage.³⁰ Options to purchase which are not dependent on default are specifically approved.³¹

The LSA provides for an obligation of commercial reasonableness as well as an obligation of good faith in the performance of security agreements,³² as there are some Canadian cases which suggest there may be a difference between the two, with good faith being a less stringent standard. These obligations may not be disclaimed.

B. *Formal and Evidentiary Requirements for Security Agreements*

The formal requirements for attachment are essentially the same as in section 203 of the ULSIA. Namely, value must be given, the debtor must have an interest in the collateral, and the debtor must have signed a security agreement describing the collateral.³³ The LSA has no equivalent to section 204 (Use or Disposition without an Accounting), as Canadian law has never had a rule similar to that in *Benedict v. Ratner*.³⁴

C. *Defense Against Assignee of Obligation*

The LSA departs somewhat from section 206 of the ULSIA in its treatment of defenses against an assignee of the an obligation. Under the ULSIA, modifications are binding only if the assignee specifically empowers

29. *Id.* at 15, 17.

30. *Id.* at 16.

31. Cf. U.L.S.I.A. §§ 201, 211, 7A U.L.A. at 236, 244.

32. SIEBRASSE & WALSH, *supra* note 3, at 137-38.

33. *Id.* at 18-21.

34. 268 U.S. 353 (1925).

the assignor to “act as a servicing agent.”³⁵ In contrast, under the LSA, following our PPSA, modifications generally are effective, subject to stipulations in the contract of assignment and subject to the overriding obligation to act in good faith and in a commercially reasonable manner.³⁶ Further, to protect the tenant or obligor, who may not be sophisticated and is generally an innocent bystander in a dispute between assignee and assignor, the LSA provides detailed provisions governing conflicting demands for payment.³⁷ While the LSA allows the obligor to demand proof of the assignment, the drafters did not wish to burden the obligor with the obligation of correctly assessing the proof in order to be relieved of potential liability for double payment. Therefore, the LSA provides that when faced with conflicting demands, the obligor may pay amounts owing into court, or, in the case of residential tenants, into the Rentalman’s office. In New Brunswick, the Rentalman’s office is already set up to administer damage deposits for residential tenants, and any interested party may apply to the court for direction.³⁸ In order to ensure that an obligor is made aware of its rights, the notice from the secured party demanding payment must inform the obligor of its rights in the case of conflicting demands.³⁹ A notice which does not contain this information is not valid, and the obligor is not obliged to make payment pursuant to it.⁴⁰

D. *Power of Debtor to Lease*

The LSA does not provide a specific power to lease equivalent to that found in section 207 of the ULSIA,⁴¹ but relies on supplementary common law to imply such a power where appropriate. Unlike the ULSIA, the LSA does not make a reasonable residential lease which is subordinate to the security interest binding on a secured party.

E. *Alienability of Debtor’s Interest: Right to Accelerate on Transfer*

The LSA closely reflects section 208(a) of the ULSIA, in that it provides that, while the security agreement may not prevent alienation of the

35. U.L.S.I.A. § 206, 7A U.L.A. at 238.

36. SIEBRASSE & WALSH, *supra* note 3, at 137-38.

37. *Id.* at 60-61, 63-64.

38. *Id.*

39. *Id.*

40. *See id.* at 61, 65 (stating requirements for valid notice).

41. U.L.S.I.A. § 207, 7A U.L.A. at 241.

collateral, it may provide that transfer without the consent of the secured party is grounds for acceleration of the debt.⁴² However, the policy issues addressed by section 208(b) are dealt with somewhat differently in the LSA. In order to preserve the debtor's ability to sell a favourable interest rate on transfer, the LSA provides that a secured party's consent, under a purchaser approval clause, may not be withheld simply because the prevailing interest rate is higher than the rate in the agreement, unless otherwise specified in the agreement.⁴³ That is, if the secured party intends to take advantage of a purchaser approval clause to call in mortgages which are below existing rates, it must make this intention clear in the agreement, so that the debtor will not be taken by surprise.

The LSA also deals much more extensively than the ULSIA with the rights between the secured party, the debtor, and the new owner of the collateral. In the absence of evidence of intention to the contrary, the LSA implies an obligation by the transferee to perform the obligation of the debtor, and to indemnify the transferor for any liability incurred as a result of non-performance of the debtor's obligations. This reflects existing law and practice. The LSA also allows the secured party to pursue any transferee directly rather than being required to obtain an assignment of the indemnification agreement. Perhaps most importantly, when the secured party consents to the assumption by the purchaser of the transferee's obligations, the transferee is released from all liability unless he agrees in writing, prior to the transfer, to remain liable.⁴⁴

Presently, under Canadian law, the original debtor remains liable for the debt even after the property is sold and the new owner enters into an assumption agreement with the secured party, unless a court is willing to find novation, or unless the original debtor becomes a surety and a material variation exists in the agreement. The courts are becoming more willing to so hold, but the law remains very uncertain and the debtor may be unfairly surprised to find herself liable for a mortgage which she believed had been "assumed" years earlier by the purchaser of the mortgaged property. Further, because a finding of novation or suretyship turns on the facts, and because there is no presumption in favour of such a finding, the present law is uncertain, and as such, difficult to take advantage of.⁴⁵

Under the LSA, the debtor may consent to remain liable, but the consent must be in writing and must specifically identify the transfer. This

42. *Id.* § 208(a), 7A U.L.A. at 241.

43. *See* discussion *infra* note 118.

44. *See* discussion *infra* note 118.

45. *See* discussion *infra* note 118.

means that a clause in the security agreement, which provides that the debtor will remain liable notwithstanding any subsequent transfers, will not suffice. This is to ensure that the debtor will choose between remaining liable and paying off the mortgage at the time when the property is sold.⁴⁶

F. *Request for Statement of Account*

While section 209 is reflected in the LSA,⁴⁷ the LSA's provisions dealing with the right to obtain information about the security agreement are much more extensive than those in the ULSIA, because the LSA is based on notice-based financing.⁴⁸ Since the Registry only provides the name and address of the secured party and notice that there is a charge, but no further details, the right to obtain detailed information about the debt from the secured party is essential.

VI. REGISTRATION, PERFECTION, AND PRIORITIES

A. *Relative Scope of LSA and ULSIA*

As observed earlier, the most substantial structural difference between the ULSIA and the LSA is the comprehensive treatment afforded by the latter to the registration, perfection, and priority status of security interests in land.⁴⁹ Because these issues are intimately connected to the more general land registry structure and policies of individual jurisdictions, they fall outside the reform mandate of the drafters of the ULSIA. In contrast, the New Brunswick LSA project was commissioned by NBGIC, which is vested with the overall responsibility for the operation of the general land registry system in the province, at a time when reform of both the structural and substantive incidents of that system is very much in the air.

B. *Perfection by Registration*

Like Article 9 and the PPSA, part III of the LSA uses the term "perfection" to denote the publicity step necessary to make a security interest effective against third parties on attachment.⁵⁰ However, while a

46. See discussion *infra* note 118.

47. A small change is that the debtor is entitled to a free account only every 12 months under the LSA, rather than every six months.

48. STEBRASSE & WALSH, *supra* note 3, at 32.

49. *Id.* at 33-38.

50. *Id.* at 34.

security interest in personal property can be perfected by either registration or taking possession of the collateral—or even temporary perfection exists by operation of law in limited circumstances—registration is the sole method of perfection available under the LSA.⁵¹ This difference reflects the elevated importance of registration in land law in light of the role of the land registry as a record of both title and encumbrances against title.

C. Notice Filing

As mentioned earlier, part IV of the proposed LSA follows the Article 9/PPSA precedent in adopting notice-filing, popular with both system administrators and system users, in place of the instrument-filing approach currently used in both the Land Registry and, for most purposes, in place of the Land Titles registration systems in the province.⁵² Although the registration venue will remain the same, secured parties will no longer be required to register a copy of the security documentation itself even in the abbreviated form now sanctioned by the Standard Form of Conveyances act.⁵³ Rather, a security interest will be considered perfected on registration of a simple “financing statement” setting out the names and addresses of the debtor,⁵⁴ the duration of effectiveness of the registration and a description of the relevant collateral by its parcel identification number (“PID”).⁵⁵ Those with a legitimate interest in learning the full details of the financing arrangement can contact the secured party, either directly (where they have an existing interest in the collateral) or through the intercession of the debtor (in the case of prospective secured creditors and

51. *Id.*

52. The PPSAs do not represent the first use of notice-filing in Canadian law. Rather, a form of notice-filing has been in operation since the early part of this century for registration of the *sui generis* statutory form of security interest available to the chartered banks under what is now § 427 of the federal *Bank Act*. See *Bank Act*, R.S.C. ch. B-1.01, § 427 (1995) (Can.).

53. R.S.N.B. ch. S-12.2 (1973) (Can.).

54. The regulations under the proposed LSA will incorporate the same rules for determining the legal name of both corporate and individual debtors that apply currently under the PPSA. Thus should provide welcome guidance on what is currently a controversial question, as well as ensure, in the longer term, consistency in the electronic records in the two contexts for the purposes of computer-based searching.

55. As is the case with registrations under the PPSA, a registrant will be able to select a registration life expressed either as a term of whole years (with registration fees set according to a sliding tariff that increases with each additional year) or as infinity (subject to a single lump sum registration fee).

other transferees) under the fully elaborated disclosure process established by part II of the act.⁵⁶

D. *Manual or Electronic Filing?*

As noted at the beginning of this paper, NBGIC contemplates the implementation of a client-administered, fully electronic environment for registrations under the LSA similar to that currently available for PPSA registrations.⁵⁷ Indeed, as we have seen, it was the possibility of being able to re-use the technology and expertise developed for the PPSA on the land side that explains, in no small part, the corporation's support for the LSA project. However, to maintain flexibility and to enable incremental reform, the LSA was drafted in technologically neutral language. The drafters anticipate that it will be initially implemented using paper financing statements and manual filing.

E. *Compulsory Amendment or Discharge*

To alleviate the problem of undischarged security interests remaining on the record and clouding title, the LSA incorporates the PPSA's compulsory discharge and amendment policy under which a secured party is obligated to discharge or amend a registration, on demand by the debtor, to accurately reflect the status of the financing relationship between the parties.⁵⁸ If the obligations of the debtor have been performed, and the secured party fails to comply with a demand by the debtor to register a discharge, the debtor may register the discharge. Under the paper-based version of the LSA, a debtor who registers a discharge is required to notify the secured party within thirty days, to allow the secured party to challenge the discharge.⁵⁹ If, in the worst case scenario, the debtor registers a discharge when not entitled to do so, fails to notify the secured party, and enters into a new security agreement with a third party, the original secured party will lose its priority, but the debtor will be liable to the original secured party for any harm caused by an unwarranted discharge, and will also face criminal sanctions for fraud.⁶⁰ This is considered sufficient incentive to prevent debtors from fraudulently taking advantage of the compulsory discharge provisions. The risk of fraud under the LSA is no

56. SIEBRASSE & WALSH, *supra* note 3, at 15-32.

57. *See* discussion *supra* note 13.

58. SIEBRASSE & WALSH, *supra* note 3, at 80-82.

59. *Id.*

60. *Id.*

greater than under the current system, where registration of a fraudulent discharge is also possible.⁶¹ Thus, the compulsory discharge provisions greatly ease the burden of dealing with undischarged security interests, without increasing the exposure to fraud which exists under the current system. It is anticipated that when an automated, paperless system is implemented, the burden of sending notification to the secured party on registration of the discharge will be shifted to the registrar rather than the debtor, thus greatly reducing the risk of fraud.

F. *Priorities Generally*

In contrast to the rather complex set of priority rules found in the PPSA and Article 9, the priority scheme of the LSA is straightforward. Regardless of whether the contest involves competing security interests or a security interest and some other type of claim, registration is paramount in assessing priority.⁶² Thus, ranking generally turns on the order of registration; an unregistered interest is subordinated to a registered interest, and it is only when neither interest is registered that priority reverts to the ordinary common law *nemo dat* rule of order of attachment.⁶³ The relative complexity of the Article 9/PPSA rules compared to the simple first-to-register rule in the LSA⁶⁴ is primarily a function of the less comprehensive scope of personal property registry systems. While a land registry ordinarily records both ownership interests and encumbrances on ownership, a personal property registry is usually limited to encumbrances and even then rarely purports to be comprehensive.⁶⁵ Since a first-to-register priority rule is

61. *Id.*

62. SIEBRASSE & WALSH, *supra* note 3, at 33-55. Two qualifications should be mentioned. The first relates to the priority status of tenants of leased collateral. Although the order of registration normally decides priority between the rights of the tenant in the collateral and the rights of the secured party, leases for a term of less than three years need not be registered to be valid and effective against third parties. Accordingly, in this one case, priority under the LSA instead turns primarily on whether the tenant is in possession when the financing statement is registered. *Id.* at 44-46. The second qualification relates to security interests taken in leased or mortgaged land. The security interest in the land is deemed to include a security interest in the payments made under the lease or mortgage, without the need for a fresh registration, for the purposes of determining priority as against a secured party holding an assignment of the payments as independent collateral. *Id.*

63. *Id.* at 33-34.

64. *Id.* at 34-35.

65. Under complementary legislation enacted at the same time as the PPSA went into effect, the Personal Property Registry in New Brunswick was made the registration venue for a variety of personal property interests other than PPSA security interests, most notably, the

possible only if the competing interests are all registerable in the first instance, the PPSA and Article 9 necessarily incorporate supplementary rules to resolve priority between secured parties and third party claimants outside the registry system, such as purchasers and lessees of the collateral.⁶⁶

G. *General Abolition of Doctrine of Actual Notice*

Although the New Brunswick Registry Act on its face adopts registration as the principal ranking mechanism for priority, actual notice of the existence of a prior unregistered interest can still invert priority.⁶⁷ The doctrine of actual notice injects an unwelcome level of uncertainty into property transactions and undermines the reliability of the public record as a mechanism for ordering priority. The LSA project was therefore seen as creating a welcome opportunity to enact a wholesale abolition of the actual notice qualification. Complementary amendments to the Registry Act will extend the pure first-to-register rule found in the LSA to resolve the priority of competing land claims generally.

H. *Priority of Security Interests in After-Acquired Land*

Under the PPSA, the registration of a financing statement covering the debtor's after-acquired personal property generally gives priority over

interest of an unsecured creditor who has recovered a money judgment against the debtor. But while all jurisdictions have made similar efforts to expand the scope of the PPR, no jurisdiction has yet succeeded in subjecting all non-possessory personal property claims to a registration requirement in the first instance, let alone to a requirement to register in a common venue. The most notable exclusions from any registration requirement, though this is changing gradually, are the statutory liens created by both federal and provincial legislation in favour of government entities to secure their tax and other revenue claims.

66. Nor can we expect greater harmony to develop over time. The establishment of a comprehensive title registry is an impractical and even undesirable proposition in view of the often mutable and temporary character of personal property and varied forms it takes. And even if a title register were feasible, it would still not be possible to adopt a universal first-to-register rule for personal property interests. Exceptions would inevitably have to be created to give effect to other policies, such as free negotiability for instruments, securities, and the like, or to accommodate the choice of law problems created by the mobility of personal property, problems for which no counterparts exist in land financing.

67. A decision by the Supreme Court of Canada, in *United Trust Co. v. Dominion Stores Ltd.*, 71 D.L.R.3d 72 (1977), introduced an element of the doctrine of actual notice into the theoretically pure land titles acts of some jurisdictions. However, the New Brunswick Land Titles Act was drafted subsequently to this decision and incorporates wording designed to ensure that the doctrine of actual notice does not apply. This wording has not yet been tested in the courts.

subsequently registered interests.⁶⁸ However, an exception exists for serial-numbered goods that are held by the debtor as either consumer goods or equipment. Unless the goods are registered and searchable by specific serial number, the security interest is vulnerable to subordination to subsequent third-party interests.⁶⁹

In developing the LSA proposal, the drafters gave some thought to extending the PPR data base of debtor names so as to allow the registration of a security interest covering any land subsequently acquired by the debtor to bind third parties. But after considerable discussion among the drafters, and with NBGIC, it was decided that the LSA should approach land in the same manner as the PPSA approaches serial numbered goods. Accordingly, in order to perfect a security interest in land, the LSA requires the secured party to register a financing statement that discloses the specific parcel index number ("PID") of the collateral.⁷⁰ In other words, the registration of a financing statement that describes the collateral simply as "all present and after acquired lands" will not constitute adequate perfection, and the security interest will be subordinated to subsequent interests that *are* registered according to the relevant PID.⁷¹

Several considerations supported the drafters' final decision on this point. First, the drafters feared that the contrary rule would complicate the process of searching title to a degree that had to be considered unacceptable in a modern reformed registry system. Second, the drafters recognized that to allow the first-registering secured party to take a prior-ranking security interest in a debtor's after-acquired lands creates what amounts to a situational monopoly over the debtor's future financing needs even if an exception is made for purchase money financing.⁷² The same problem exists of course in the personal property context, but it is less troublesome there because the negotiable and transient character of personal property necessitates the creation of significant exceptions to the after-acquired property financier's priority over third parties, thereby diminishing the monopoly problem. Finally, the drafters felt that in view of the role of the Land Registry, in contrast to that of the Personal Property Registry, as a record of both ownership interests and encumbrances on ownership, the law should generally discourage the proliferation on the record of future interests

68. Personal Property Security Act, S.N.B. ch. P-7.1, § 35.

69. *Id.*

70. SIEBRASSE & WALSH, *supra* note 3, at 68-69.

71. *See id.* at 36-37.

72. *See id.* at 37.

with the impediments to the integrity and operation of the system that they inevitably pose.

I. *After-Acquired Land and the Claims of Judgment Creditors*

Under the Registry Act, as it presently reads, the registration of a “memorial” of judgment binds the interest of the judgment debtor identified in the memorial in any lands acquired within five years of registration.⁷³ Allowing judgment creditors to bind after-acquired land in this manner prevents judgment debtors from effectively preferring new creditors by subjecting their after-acquired land to a security interest before the registered judgment was amended to specifically cover the new lands.⁷⁴ This policy also encourages the voluntary liquidation of debt, since the judgment creditor cannot deal with his or her assets without paying off the debt. At a purely mechanical level, however, the existing land registration system unquestionably presents obstacles to the effective registration of judgments against a debtor’s after-acquired lands. In the Registry Act context, searchers must depart from normal practice and search the grantor-grantee index *back* five years to determine whether a memorial has been registered against a grantee named in a later conveyance of land.

The difficulty of searching for judgment liens is exacerbated under a parcel-based indexing, such as is proposed for the LSA, because registration can be effected only against a specific parcel or parcels of registered land, and then only once the judgment debtor becomes the registered owner.⁷⁵ To maintain the integrity of the land registry, the LSA provides that a judgment, as any other interest, must be registered against a specific parcel to bind the land.⁷⁶ To maintain the advantages of self-enforcing judgments, the LSA requires that a registrant who wishes to register a transfer of a parcel of land will be required to present a current search result to the Registrar, disclosing a search of the *Personal Property Registry* according to the name of the prospective transferee.⁷⁷ According to the proposed LSA, “[i]f the name of the prospective transferee matches the name of a debtor against whom a judgment has been registered in the PPR, notice of the judgment must be registered against the relevant parcel of land when the

73. *See id.*

74. After all, as a practical matter, judgment creditors are rarely in a position to continually monitor the debtor’s estate for the acquisition of new assets.

75. *See* SIEBRASSE & WALSH, *supra* note 3, at 67.

76. *Id.* at 50.

77. *Id.*

transfer is registered and before any security interest in the parcel can be registered.”⁷⁸ Therefore, to fully protect its interest, the judgment creditor must first search the land registry for parcels registered in the name of the debtor⁷⁹ and register a notice of judgment against those specific parcels, thus preventing the debtor from dealing with his or her presently owned land without paying off the judgment debt. Next, the judgment creditor must register a notice of judgment in the PPR, which will indirectly bind after-acquired land.⁸⁰

J. *Priority for Future Advances as Against an Intervening Judgment Creditor*

Under the PPSA, a perfected security interest has priority over the subsequently-registered interest of a judgment creditor only to the extent of advances made before the secured party has actual notice of the intervening registration of a notice of judgment.⁸¹ Registration constitutes constructive, not actual notice. The adoption of this priority rule prevents a debtor from remaining judgment proof by increasing the share of debt owed to secured creditors even after judgments in favour of unsecured creditors have begun to accumulate. A similar policy makes evident sense for land law; the pre-PPSA law in relation to chattel mortgages on this point is identical to the pre-LSA law in the land context, and has been incorporated in the LSA.⁸²

VII. DEFAULT

A. *Rights and Remedies*

As with the ULSIA, the rights and remedies on default are confined to those which are described in part V of the act or in the security agreement.⁸³ Rights granted to the debtor or obligations imposed on the secured party cannot be waived or varied unless specifically provided for in the act.⁸⁴ The LSA recognizes and codifies five primary default remedies available to secured parties against the collateral:

78. *Id.*

79. The parcel indexed land registry will also include an auxiliary name index.

80. SIEBRASSE & WALSH, *supra* note 3, at 67.

81. Personal Property Security Act, S.N.B. ch. P-7.1, § 14(2).

82. See SIEBRASSE & WALSH, *supra* note 3, at 50-51.

83. *Id.* at 85-89.

84. *Id.* at 87.

1) right to collect rents from leased collateral and to collect payments owing under a security agreement covering land that is collateral under a subsequent security agreement executed by the secured party in favour of his or her financier; 2) right to take possession of the collateral; 3) right to dispose of the collateral by private sale or lease; 4) right to retain the collateral in full satisfaction of the secured debt; and 5) right to appoint a receiver to manage and realize the value of the collateral.⁸⁵

For their part, debtors are given a non-excludable:

1) right of redemption; 2) right to reinstate the security agreement outside of receiverships; 3) right to any surplus from a disposition by sale or lease; and 4) right to require disposition by sale rather than foreclosure.⁸⁶

B. *Reinstatement of the Security Agreement and Acceleration Clauses*

As explained in the commentary:

[s]ecurity agreements that provide for payment at fixed intervals commonly contain an acceleration clause under which the entire outstanding secured obligation becomes due and payable upon default in the payment of any one instalment. Such a clause is unobjectionable to this extent that it simply allows the secured party to realize in full upon a debt which is non-performing. However, it could also be invoked to allow a secured party to accelerate the entire debt as a single late payment which occurred because of some unforeseen and unavoidable delay. For this reason acceleration clauses are often considered harsh and legislation giving relief from their effect has been implemented in a number of jurisdictions as well as in the New Brunswick PPSA.

But while arbitrary invocation of the acceleration clause is possible, it is rarely in the interest of a secured party to call in an otherwise sound loan as a result of a single default, as this simply increases administrative costs to no benefit. On the contrary, in general the secured party will voluntarily make every effort to give a debtor a chance to reinstate an agreement when the default is inadvertent or the result of temporary cash-flow problems. In addition to calling in loans

85. *Id.* at 87-88.

86. *Id.* at 88.

clause to call in a loan in the face of persistent defaults which are raising the lender's administrative costs in a case where default is ultimately inevitable. In a competitive market, such as the Canadian mortgage market, this use of the acceleration clause will indirectly lower the cost of the loan to the borrower. [On the other hand], if the lender has given the debtor an informal opportunity to reinstate the agreement, and default is in fact ultimately inevitable, then the debtor will be unlikely to take advantage of a formal right of reinstatement. And . . . some unscrupulous lenders may take advantage of the clause to call in a loan after a single default if interest rates have risen sufficiently that incurring the costs of calling in the loan and relending the money at a higher rate is profitable (although reputational constraints make it unlikely that a major lender would resort to this tactic regularly). Further, all lenders do not always act rationally, and in some instances, perhaps because of bad personal relations between the debtor and the creditor, the loan might unjustifiably be called in as the result of an insignificant default.

The arguments for and against a right of reinstatement are therefore fairly closely balanced. Acceleration clauses are not routinely abused, and a right of reinstatement may simply draw out the time and expense involved in realizing on the security in instances where the clause is properly invoked; but a right of reinstatement is unlikely to be taken advantage of by large numbers of borrowers, so that the price of such a right in terms of increased lending costs is probably quite low.⁸⁷

One of the drafters, Siebrasse, is not in favour of such a right, while the other drafter, Walsh, does favour this right. In the end, the drafters decided to include a limited right of reinstatement in the proposal in order to harmonize the LSA with the PPSA, and with real property law in some other major jurisdictions. A default would be curable at any time before disposition of the collateral by tendering only the amounts past due, exclusive of any amounts owing due to the acceleration clause, plus reasonable expenses of the secured party. As explained in the commentary to this section of the act:

[t]his provides protection from arbitrary invocation by the lender when interest rates rise, for example, while retaining the secured party's right to call in a loan which is perpetually in arrears. The contemplated provision would not make such clauses void, but . . . simply provides for a right of reinstatement, so that if an acceleration clause were invoked and the default is not cured, the entire debt would be due and

87. SIEBRASSE & WALSH, *supra* note 3, at 130-31.

owing. A requirement that the debtor pay the lender's reasonable expenses would deter willful abuse of the reinstatement right by the debtor. The debtor would also be required to cure any other default by reason of which the secured party intended to dispose of the collateral. As additional protection against abuse of the right, the debtor would not be entitled to reinstate more than twice annually. Finally, in the unusual event that these protections were insufficient, the secured party would be entitled to apply under 39 to terminate the debtor's right of reinstatement.⁸⁸

The right of reinstatement is not available in the context of a receivership in a commercial debt realization.⁸⁹

In contrast, the ULSIA does not provide a right of reinstatement per se, but provides for a notice period of fifteen days before the acceleration clause may be invoked.⁹⁰ This allows the debtor to cure an inadvertent default, and reinstate the security agreement, while giving the secured party a certain cut off point, beyond which the right of reinstatement will not be exercised. However, it is unlikely that a right of reinstatement would be helpful to a debtor suffering unusual cash-flow problems of longer than two weeks' duration. On the other hand, the ULSIA is more favourable to the debtor in that there is no limit to the number of times the agreement can be reinstated, so long as the debtor acts within fifteen days.⁹¹

C. Receivership

While appointment of a receiver by the court is possible, in Anglo-Canadian practice, a power to appoint a private receiver is invariably found in commercial security agreements. Since the private receiver can be appointed more quickly, more easily, and more cheaply, the appointment is made by the secured party, and the powers of the receiver and its remuneration can be spelled out in the security agreement. A privately appointed receiver is generally preferred over a court appointed receiver throughout the Commonwealth, except perhaps in circumstances where the secured party anticipates a challenge to the receiver's authority, or other such difficulties.⁹² In view of the many advantages of a private receivership it is not

88. *Id.* at 131-32 (citations omitted).

89. See discussion *infra* note 118.

90. U.L.S.I.A. § 502, 7A U.L.A. at 252.

91. See *id.*

92. See JACOB S. ZIEGEL & D.L. DENOMME, THE ONTARIO PERSONAL PROPERTY SECURITY ACT: COMMENTARY AND ANALYSIS (1994).

clear why the practice has not caught on in the United States.⁹³ The LSA does not confer the power to appoint a private receiver, which must still be found in the security agreement, but the LSA specifically sanctions such an appointment, and places certain obligations on a privately appointed receiver, primarily with regard to record keeping.⁹⁴ The LSA also specifically provides for a judicially appointed receiver.⁹⁵

D. Collection of Rents

The treatment of the right to collect rents under the LSA differs from that found in section 505 of the ULSIA in several respects.⁹⁶ First, in the provision dealing with the obligor's rights vis-a-vis an assignee, "assignee" is defined to include a secured party.⁹⁷ The effect is that the LSA implies an assignment of rents whenever a security interest is taken in the underlying property, unless the parties agree to the contrary. The rationale for this is that the legal default rule should replicate the most commonly desired arrangement, and in practice, an assignment of rents is almost invariably taken.⁹⁸ Further, in contrast to the ULSIA, if the debtor is in default under a security agreement, the secured party is entitled to all rents, and not only those accruing after notice is given.⁹⁹ This includes all arrears, even if the rents became payable before default. This simplifies the action, as there is no need for the debtor to apportion the arrears between the secured party and the debtor, and there is no good reason for allowing the debtor to milk the property of rents which happened to accrue before default. The debtor is not, in principle, disadvantaged, as the arrears are of course applied to the debt. Under the LSA, because the secured party is deemed to be an assignee, a demand for payment on default is subject to the notice requirements which apply in the case of an assignment of the right to

93. See Jacob S. Ziegel, *The Privately Appointed Receiver and the Enforcement of Security Interests: Anomaly or Superior Solution*, in CURRENT DEVELOPMENTS IN INTERNATIONAL AND COMPARATIVE CORPORATE INSOLVENCY LAW 451 (Jacob S. Ziegel ed., 1994).

94. SIEBRASSE & WALSH, *supra* note 3, at 135.

95. *Id.* at 136.

96. The LSA follows the ULSIA in providing that a secured party need not be in possession to collect rents. The arguments are reviewed in Julia P. Forrester, *A Uniform and More Rational Approach to Rents as Security for the Mortgage Loan*, 46 RUTGERS L. REV. 349 (1993), which recommends the approach adopted by the ULSIA and the LSA.

97. SIEBRASSE & WALSH, *supra* note 3, at 60.

98. *Id.* at 93.

99. *Id.* at 92.

payment and the concomitant right to pay rents into court in the case of conflicting demands.¹⁰⁰

E. *Duties of the Secured Party in Possession*

The question of the proper scope of the duties of a secured party in possession raises difficult questions. The traditional duties are generally perceived by secured parties as onerous, and as a result, possession by the secured party is a remedy which is resorted to only reluctantly. Section 505(d) of the ULSIA addresses this issue by specifically enumerating a number of duties, including the duty to carry reasonable insurance, to maintain the property, and to make repairs, which amount to a partial codification of existing law.¹⁰¹ However, as the commentary to this section of the proposed act discusses, and as was also noted by the Ontario Law Reform Commission ("OLRC"), a specific enumeration of this sort:

sacrifices the flexibility of the existing standard, cannot be exhaustive, and may "lead to [] mechanical and therefore insufficient compliance." Further, a non-exhaustive enumeration of duties is unlikely to satisfy secured parties, who are more concerned about the standard required in relation to the performance of clearly established duties, rather than the lack of clarity as to the nature of the duties.

Consideration was given to specifically relaxing some of the existing duties, but while the duties may be burdensome, they generally address a real underlying concern. Some duties are not onerous in themselves, but give rise to uncertainty and potential litigation. For example, the duty to take reasonable care in collecting rents and ensuring that the premises are not left vacant, is sufficiently imprecise that it can always provide the basis for an attack by the debtor in deficiency proceedings, and the lost rents from vacancy in a commercial property may be very substantial, especially if considerable time is needed to dispose of a valuable property in a commercially reasonable manner. The obligation to make repairs, while denying the secured party's claims for major improvements, may result in difficult decisions for the secured party. However, the alternative, to deny the debtor the benefit of rents lost by the mismanagement of the secured party, or to permit the secured party to allow the property to fall into disrepair, is a cure worse than the disease.

The LSA therefore neither enumerates the secured party's duties, nor specifically relaxes its duties. [Rather the] LSA parallels the [New

100. See *supra* part V.C.; see also discussion *infra* note 118.

101. U.L.S.I.A. § 505(d), 7A U.L.A. at 257.

Brunswick] PPSA in providing that a secured party in possession must take reasonable care in the management and preservation of the property. This is subject to the overall standard of commercial reasonableness imposed by s. 41, so that the provision should be read as requiring "commercially reasonable" care. This is not intended to effect any specific change in existing law. It is nonetheless possible that some specific duties under existing law will be held to be commercially unreasonable.¹⁰²

F. *Methods of Disposing of the Collateral*

Under the LSA, the debtor's interest in the collateral may be terminated either through an agreement by the secured party to retain the collateral in full or partial satisfaction of the debt,¹⁰³ or by the exercise of the power of sale by the secured party. The former remedy is similar to, but more powerful than the agreement to acquire the debtor's interest contemplated in section 507,¹⁰⁴ and the latter is similar to the power provided in section 509.¹⁰⁵ There is no provision for judicial sale such as that found in section 510 of the ULSIA,¹⁰⁶ nor is there a provision equivalent to the traditional remedy of strict foreclosure, that is, a judicial declaration that the collateral is retained by the secured party in satisfaction of the debt. These remedies have not been available in New Brunswick for a number of years and were not thought to be sufficiently useful to revive.

G. *Retention of the Collateral in Full or Partial Satisfaction of the Debt*

In a remedy modelled after the PPSA, and similar to that found in Article 9, the LSA allows the secured party to propose to retain the collateral in full or partial satisfaction of the debt.¹⁰⁷ The remedy is broader than the agreement to acquire the debtor's interest which is contemplated in section 507 because it extinguishes all interests subordinate to that of the secured party.¹⁰⁸ Accordingly, a proposal to retain the

102. SIEBRASSE & WALSH, *supra* note 3, at 101-02 (citing OLRC REPORT, *supra* note 7, at 230).

103. *Id.* at 109.

104. *See* U.L.S.I.A. § 507, 7A U.L.A. at 258.

105. *See id.* § 509, 7A U.L.A. at 261.

106. *See id.* § 510, 7A U.L.A. at 262.

107. *See* SIEBRASSE & WALSH, *supra* note 3, at 144 (incorporating § 69 of the PPSA); *see also* discussion *infra* note 118.

108. *See* U.L.S.I.A. § 507, 7A U.L.A. at 258.

collateral must be sent to parties who would be entitled to be notified if a power of sale were exercised, namely all parties with a right to redeem, including the spouse of the debtor.¹⁰⁹ Any party with an interest in the collateral has fifteen days after the proposal is made to object.¹¹⁰ If no objection is made within that time, the secured party is deemed to retain the collateral in satisfaction of that part of the debt which was specified in the proposal. The interest of all subordinate parties is extinguished, except for the interest of parties who were entitled to, but did not receive notice. The interest of subordinate parties who did not receive notice will be extinguished by a subsequent sale to a bona fide third party, and their only remedy thereafter will be for damages against the secured party for failure to give notice.¹¹¹

The LSA gives the secured party the option to retain the collateral in partial satisfaction of the debt to provide additional flexibility. This option will be particularly useful if a deficiency is anticipated and the debtor is solvent: by agreeing to a proposal for retention of the collateral in partial satisfaction, expenses of the sale are avoided, thereby increasing the amount which may be credited against the debt, while the secured party retains the right to pursue the deficiency.

This drastically simplified power to retain the collateral in satisfaction of the debt is perhaps reminiscent of the strict foreclosure which was at one time granted by American courts, and which was perceived to operate so harshly that it was eventually eliminated. Abuse of the remedy under the LSA is prevented because any party with an interest which would be extinguished has the right to object; even one objection is sufficient to block a foreclosure proposal. However, the basis for objection must be a legitimate one. The objector must of course have an interest in the collateral, and the secured party is entitled to demand proof of the interest, and can proceed as if no objection was made if proof is not forthcoming. The objector must also be adversely affected by the foreclosure. Of course, the party's interest will be cut off by the disposition, but this alone is not sufficient to give a right to object, as it will not have an adverse effect on that party if the market value of the collateral is less than the debt owed to the foreclosing creditor plus its enforcement expenses. If faced with a frivolous objection, the secured party is entitled to apply to a court for a ruling that an objection is ineffective because the objection was motivated

109. See SIEBRASSE & WALSH, *supra* note 3, at 144.

110. See *id.*

111. *Id.* at 107-08, 119-20.

by a purpose other than protection of the objector's interest in the collateral. Costs in such a motion may be awarded against a party who makes a frivolous objection, thus providing sufficient disincentive for such objections.

H. *Creditor's Power of Sale*

The LSA grants the secured party the right to dispose of the collateral by sale or lease, whether or not such a right was specified in the security agreement. Other than this, the power of sale provisions of the LSA are very similar to those found in section 509 of the ULSIA, with some differences regarding timing and notice periods. The delay period between notification that the secured party intends to exercise its power of sale, and the earliest date at which the sale may be held, was set at five weeks under section 509(a) of the ULSIA.¹¹² This time period was apparently set with the goal of providing sufficient time for the debtor to obtain court relief to control any aspect of the foreclosure.¹¹³ However, the great majority of sales will not justify judicial intervention, and it is unduly burdensome to structure the process around an unusual event. The LSA contemplates that challenges to the validity of the sale can be made after the sale, with damages as a remedy. This remedy will generally be adequate, and will ensure that the secured party realizes on the security only when it has at the least a prima facie right to do so. The delay period in the LSA is intended solely to give the debtor time to cure the default or refinance the property when in a position to do so expeditiously, and the LSA therefore adopts a somewhat shorter notice period of thirty days.

The ULSIA provides that a notice of intention to foreclose may not be given to a protected party until payment is five weeks overdue. This effectively doubles the time between default and the earliest possible sale. As the OLRC points out, to the extent that the delay before the sale is intended to allow the debtor or other parties with a right to do so to redeem the collateral, there is no justification for longer notice periods for protected borrowers, since there is no connection between the type of borrower and the chance of improvement of its financial prospects in the near future.¹¹⁴ Further, secured parties typically make every effort to encourage the debtor to pay before taking steps to realize on the security. To impose an

112. U.L.S.I.A. § 509(a), 7A U.L.A. at 261.

113. James M. Pedowitz, *Mortgage Foreclosure Under the Uniform Land Transactions Act (As Amended)*, 6 REAL ESTATE L.J. 179, 186 (1978).

114. OLRC REPORT, *supra* note 7, at 169.

additional formal notification period will either add to the delay when there is no hope of redemption, or will encourage secured parties to issue a formal notice at the first legal opportunity, so as not to be hampered by the notice requirement when a decision is made to realize on the collateral. This would unduly formalize the process, and in so doing, might impede informal attempts to reinstate the debt.

I. *Effect of Disposition*

As under section 512 of the ULSIA,¹¹⁵ a sale to a bona fide purchaser for value, pursuant to the power of sale in the LSA, conveys title free of all interests subordinate to that of the debtor or the secured party.¹¹⁶ It has been suggested that under the ULSIA, “a failure to observe significant statutory requirements” would “undoubtedly” result in a void sale, particularly when the secured party is not financially responsible, so that no compensation is forthcoming.¹¹⁷ Whatever the merits of this position as an interpretation of the ULSIA, it is certainly contrary to the intended interpretation of the equivalent provision of the LSA. Such an interpretation, by creating uncertainty in the title given under the exercise of a power of sale, would result in a general reduction in the selling price for such properties, thereby penalizing thousands of debtors and secured parties in cases where all reasonable steps were in fact taken. It is preferable to apply the general principle that where one of two innocent parties must suffer, the party should bear the loss who could best have avoided it. Only parties who borrow from lenders who are both unscrupulous and financially irresponsible expose themselves to the risk that they will be financially harmed by an improper sale. Because there is no dearth of responsible lenders, a decision to borrow from an irresponsible lender will typically be made to obtain a lower interest rate. There is no reason why parties who take such a calculated risk should later be compensated to the detriment of the good faith purchaser and borrowers generally. Of course, when the purchaser is a party to the bad faith sale, the same logic does not apply, and he or she should not be protected.

115. See U.L.S.I.A. § 512, 7A U.L.A. at 265.

116. SIEBRASSE & WALSH, *supra* note 3, at 107-08, 119-20.

117. Pedowitz, *supra* note 113, at 194-95.

VIII. CONCLUSION

The proposed Land Security Act will soon be brought to the New Brunswick government for approval in principle.¹¹⁸ If the proposal is approved, the drafters anticipate that it will be implemented in the near future. While, for better or for worse, the drafters have deviated from the ULSIA in a number of respects, there is no question that the guidance provided by the ULSIA helped them in fashioning a better proposed act than would otherwise have been possible. The drafters hope that some of the observations and modifications that they have recommended may likewise be of assistance to future law reformers.

118. This article was written at the same time as the final draft of the report (the tentative act) was being prepared. After this article was completed, but just prior to the submission of the report, NBGIC indicated that they viewed some of the drafters' recommendations, which they intended to make, as changes to the law which are outside the scope of their legislative mandate. Therefore, NBCIG would be unwilling to present those recommendations to the executive branch of the government for adoption as an official policy proposal. These aspects of the report, in particular, the detailed treatment of the rights of the debtor after alienation of the mortgaged property in part V.E. of this paper, the right of reinstatement of the security agreement discussed in part VII.B., and the secured party's right to retain the collateral in full or partial satisfaction of the debt discussed in part VII.G., were therefore removed from the final report to NBGIC. Discussions are currently underway between the authors, NBGIC, and the Law Reform Branch of the New Brunswick Department of Justice regarding the possibility that the Law Reform Branch will assume responsibility for bringing forward these particular recommendations.

