



THE COURT OF APPEAL FOR SASKATCHEWAN

Citation: 2009 SKCA 35

Date: 20090312

Between:

Docket: 1572

Innovation Credit Union

Appellant

- and -

Bank of Montreal

Respondent

Coram:

Sherstobitoff, Jackson & Smith JJ.A.

Counsel:

Donald Layh, Q.C. for Innovation Credit Union

Rick van Beselaere for Bank of Montreal

Appeal:

From: 2007 SKQB 471

Heard: May 12, 2008

Disposition: Appeal Allowed

Written Reasons: March 12, 2009

By: The Honourable Madam Justice Jackson

In Concurrence: The Honourable Mr. Justice Sherstobitoff

The Honourable Madam Justice Smith

Jackson J.A.

I. Introduction

[1] This appeal concerns a priority dispute between a prior unregistered security interest taken under *The Personal Property Security Act, 1993*¹ (the “PPSA”) in agricultural equipment and a subsequent security interest taken and registered under the *Bank Act*² in the same collateral. Both security agreements are valid and the debtor had proprietary rights in the collateral when the *Bank Act* security came into effect. The central issue is which security interest takes priority in these circumstances.

[2] Sections 427(2) and 435(2) of the *Bank Act* apply to resolve this dispute. On a proper interpretation of these sections, they provide that the prior PPSA interest defeats the *Bank Act* security on the basis that the Bank acquired its interest subject to the prior interest regardless of the fact it was unperfected. Applying this priority rule to the facts of this appeal necessarily results in the appeal being allowed, and the proceeds of the sale of the collateral being granted to the Credit Union.

II. The Facts

[3] The facts in this case are succinctly stated in the judgment of the learned Chambers judge.³ It must be noted, however, that this appeal does not concern collateral claimed as after-acquired property. Unlike the companion appeal

¹ S.S. 1993, c. P-6.2.

² S.C. 1991, c. 46.

³ 2007 SKQB 471, [2008] 4 W.W.R. 143.

involving Radius Credit Union,⁴ the debtor had proprietary rights in the collateral in question before the *Bank Act* security came into existence.

[4] A Saskatchewan farmer, James Buist, granted a security interest in all of his present and after-acquired personal property (mostly farm equipment) to the Innovation Credit Union, pursuant to a General Security Agreement dated October 7, 1991. The Credit Union did not register its security interest in Mr. Buist's property in the Personal Property Registry until June 28, 2004.

[5] Meanwhile, beginning in 1998 and continuing until January of 2004, the Bank of Montreal loaned Mr. Buist money secured on the same collateral that had been used to secure the Credit Union's loans. Mr. Buist did not disclose to the Bank that he had already granted a General Security Agreement to the Credit Union. It is common ground that the Bank took the necessary steps to register the requisite notices under s. 427 of the *Bank Act*, and followed its usual practice of searching the Personal Property Registry prior to doing so.

[6] In 2004, Mr. Buist defaulted on repaying his loans to the Credit Union and to the Bank, and the latter seized and sold collateral comprised entirely of agricultural equipment and some hay. It is the proceeds from the sale of that collateral, less costs of sale, which are the subject of the priority dispute in this case. The amount that is in dispute is \$32,891.31.⁵

⁴ *Radius Credit Union v. Royal Bank of Canada*, 2009 SKCA 36 [*Radius*].

⁵ Appeal Book, p. 102a [Affidavit of Mary Stewart, Bank Officer, Bank of Montreal].

[7] Mr. Buist owed \$58,856.36 to the Credit Union, as of December 15, 2004,⁶ which is a date close in time to the date of the Bank's seizure of the collateral. At the time of enforcement of its interest, Mr. Buist was indebted to the Bank for an operating loan that had a balance of \$72,609.97.⁷ The Bank also held equipment loans, but those are not the subject of this appeal.

III. Decision of the Chambers Judge

[8] The learned Chambers judge recognized the legal dilemma before him: the allocation of priority between two security interests, in the same collateral, each taken pursuant to a fundamentally different secured transactions regime. He resolved this dilemma by constructing a bridge between the two systems, so as to permit the Bank to rely on the other secured creditor's failure to perfect its security interest. He wrote:

[52] In the present case the issue of perfection by registration and therefore notice to all of the security interest claimed by the Credit Union is central to the determination of this priority dispute. If the provisions of s. 428 of the *Bank Act* referring to "all rights subsequently acquired in, on or in respect of [that] property ..." includes priority rights then by the second rule in the *Agricultural Credit Corp. of Saskatchewan* [(1994), 115 D.L.R. (4th) 569 (Sask. C.A.)] case the Bank succeeds in its claim of priority in this case. Priority is obtained by the Credit Union in respect of its prior security interest only when that interest is perfected, in this case, by registration. Registration gives notice to all third parties of the nature of the security interest claimed and implicitly its priority. [Emphasis added.]

[53] This conclusion is a reasonable interpretation of the provisions of s. 428 of the *Bank Act*. It is also in accord with and reflects two policy goals. The first is to achieve compatibility between these two security regimes and avoid future conflicts. Each of the two systems (the *Bank Act* and PPSA systems) have provisions for registration of security interests. Each system allows for searches of these registrations as public records by anyone concerned to do so. The respective registries provide notice to all of the nature of the interest claimed and the priority in time to which those interests are entitled. The development of modern technologies now allows these registrations and searches to be done "on line" and

⁶ *Ibid.*, p. 30a [Affidavit of Norma Cave, Risk Management Officer, Innovation Credit Union].

⁷ *Ibid.*, p. 99a [Affidavit of Mary Stewart].

all financial institutions, whether Banks, Credit Unions or others extending credit are or should be aware of the existence of the two systems and the availability of the systems to conduct due diligence to identify other security interests that are claimed in respect to the property of a borrower.

[54] The second policy goal is to achieve commercial and business lending efficacy and predictability. This court's conclusion that registration (and consequently the notices provided by the registration systems of the *Bank Act*, and PPSA) establish priority ensures that lenders have notice of competing security interests and underwrite loan applications accordingly. This avoids the "hidden lien" problem and contributes certainty to commercial lending practises.

[55] In conclusion, the security interest of the Bank, although taken subsequent in time to the security interest of the Credit Union, nevertheless obtains priority to that of the Credit Union because the Credit Union's interest was not perfected by registration under the PPSA prior to the Bank taking its security interest and registering notice of its intention to do so under the *Bank Act*.⁸

The issue, of course, is whether statute law or common law permits a bank, as the holder of *Bank Act* security, to rely on a *PPSA* secured creditor's failure to perfect its security interest.

IV. Questions to be Answered

[9] The central issue in this case gives rise to these subsidiary questions:

1. What is the proper framework of analysis to resolve the priority dispute in this case?
2. Does the priority rule created by s. 428(1) of the *Bank Act* apply?
3. If not, do ss. 427(2) and 435(2) of the *Bank Act* apply to resolve this priority dispute?
4. If so, what right or title did the debtor retain after the Credit Union acquired its security interest in the collateral?

Sections 427(2), 428(1), and 435 of the *Bank Act* are reproduced in the body of the text, when they are first considered, and in Appendix "A".

⁸*Innovation Credit Union v. Bank of Montreal*, supra note 3.

V. What is the Appropriate Framework of Analysis?

[10] Before turning to an examination of the legislation and the jurisprudence, I must acknowledge the difficult exercise faced by counsel and the Chambers judge in this case, and by courts in general, when faced with a conflict between *PPSA* and *Bank Act* security. As Professor Ziegel writes: “when a court is required to determine priorities between a s. 178 [now s. 427] security interest and a security interest governed by PPS legislation it may be engaging in the logically impossible task of comparing apples and oranges or trying to square the proverbial circle.”⁹ The courts are, however, assisted in this task by a large body of academic literature,¹⁰ reference to which will be made both in this case and in the companion decision involving Radius Credit Union.

[11] The Chambers judge’s intentions are clearly laudable. In the best traditions of the common law, he sought a solution to a continuing problem. In my respectful opinion, however, his chosen solution will create other problems, including further litigation, and is contrary to existing jurisprudence and to the existing legislative base, such as it is.

⁹ Jacob S. Ziegel, “Interaction of Personal Property Security Legislation and Security Interests under the Bank Act” (1986-87) 12 Can. Bus. L.J. 73 at pp. 73-74.

¹⁰ For a comprehensive list of this literature as of 2003, see Marc-Alexandre Poirier, “Analysis of the Interaction between Security under Section 427 of the Bank Act and Provincial Law: A Bijural Perspective” (Automne 2003) 63 R. du B. 289 at 295, at footnote 14 [Poirier]. For materials subsequent to 2003, see Richard H. McLaren, *Secured Transactions in Personal Property in Canada*, 2d ed., looseleaf (Toronto, Ont.: Thomson Carswell, 1989); Ronald C.C. Cuming, Catherine Walsh, Roderick J. Wood, *Personal Property Security Law* (Toronto, Ont.: Irwin Law, 2005) at p. 590-97; Ronald C.C. Cuming, “Case Comment: *Innovation Credit Union v. Bank of Montreal*—Interface between the *PPSA* and Section 427 of the *Bank Act*: Desirable Policy vs. Hard Legal Analysis” (2008) 71 Sask. L. Rev. 143.

[12] It is common ground that the *PPSA* cannot derogate from the rights accorded to the Bank under the *Bank Act*. Relying on *Bank of Montreal v. Hall*,¹¹ the trial judge correctly stated that “[t]o the extent that a conflict exists between the Bank's rights to enforce *Bank Act* security and provincial statutes restricting enforcement rights, the federal statute prevails.”¹² The Bank, however, did not pursue any argument based on federal paramountcy. Indeed, there is no “actual conflict in operation”¹³ between the two systems of law, nor does “compliance with the federal statute necessarily entail defiance of its provincial counterpart.”¹⁴ In *Hall*, it was found that the bank was restricted by provincial legislation with respect to the enforcement of rights that had been conferred upon it by the *Bank Act*.

[13] Resolution of the dispute in the instant case, however, does not require compliance by the Bank with provincial law. Enforceability of the Bank’s interest is not restricted. Furthermore, as will be seen later in these reasons, the *Bank Act* itself looks to the general law of the province to determine what “right or title” of the debtor is acquired by a bank when it takes security pursuant to that *Act*.

[14] The priority rule considered by the learned Chambers judge is contained s. 428(1) of the *Bank Act*:

Priority of bank’s claim

428. (1) All the rights and powers of a bank in respect of the property mentioned in or covered by a warehouse receipt or bill of lading acquired and held by the bank,

¹¹ [1990] 1 S.C.R. 121[*Hall*].

¹² *Innovation Credit Union v. Bank of Montreal*, *supra* note 3 at para. 21.

¹³ *Hall*, *supra* note 11 at p.152.

¹⁴ *Ibid.*, p. 153.

and the rights and powers of the bank in respect of the property covered by a security given to the bank under section 427 that are the same as if the bank had acquired a warehouse receipt or bill of lading in which that property was described, have, subject to subsection 427(4) and subsections (3) to (6) of this section, priority over all rights subsequently acquired in, on or in respect of that property, and also over the claim of any unpaid vendor.¹⁵ [Emphasis added.]

The Chambers judge held that priority could be granted to the Credit Union pursuant to this subsection “in respect of its prior security interest only when that interest is perfected...by registration.” Applying this rule to the case before him, he held that the Bank was entitled to priority over the Credit Union. As I will demonstrate, the Chambers judge’s decision, in my respectful view, cannot be supported.

[15] While the issue on this appeal is one of first instance, the result in this case can be said to have been anticipated by a series of decisions from this Court and the Court of Appeal of Ontario: *Rogerson Lumber Co. v. Four Seasons Chalet Ltd.*,¹⁶ *Bank of Montreal v. Pulsar Ventures Inc.*,¹⁷ *Bank of Nova Scotia v. International Harvester Credit Corp.*,¹⁸ *Royal Bank of Canada v. Agricultural Credit Corp. of Saskatchewan*,¹⁹ and *Royal Bank of Canada v. Moosomin Credit Union*.²⁰

[16] In *Rogerson* the priority dispute was between a *Bank Act* security and a subsequent, unperfected conditional sale agreement. A company sold

¹⁵ *Supra* note 2.

¹⁶ (1980), 113 D.L.R. (3d) 671 (Ont. C.A.) [*Rogerson*]. This decision is analyzed in Jacob S. Ziegel, “Interaction of Personal Property Security Legislation and Security Interests under the Bank Act” (1986-87) 12 Can. Bus. L.J. 73 at pp. 74-88.

¹⁷ [1988] 1 W.W.R. 250 (Sask. C.A.); (1987), 58 Sask.R. 224 [*Pulsar*].

¹⁸ (1990), 73 D.L.R. (4th) 385 (Ont. C.A.) [*International Harvester*].

¹⁹ (1994), 115 D.L.R. (4th) 569 (Sask. C.A.); (1994), 120 Sask.R. 205 [*Agricultural Credit*].

²⁰ 2003 SKCA 115; [2004] 5 W.W.R. 494, leave to appeal to S.C.C. refused [2004] 1 S.C.R. xii [*Moosomin Credit Union*].

lumber under an oral conditional sales agreement, whereby the vendor retained title to the sold lumber. The bank seized the lumber as after-acquired property under its s. 88 security (now s. 427) before the purchaser had executed a written conditional sales agreement, and before the vendor had registered its security interest in the Personal Property Registry. At the moment when the bank seized the lumber, the purchaser had not yet paid anything on account of the purchase price.

[17] Arnup J.A. held that the *PPSA* cannot prejudicially affect a bank's interest acquired pursuant to a federal statute. At the same time, however, he confirmed that the *PPSA* conferred no rights or priority on the bank either. He wrote:

Since the agreement in the nature of a conditional sale between the plaintiff and Four Seasons is valid, the purchaser, Four Seasons, could not give the Bank security over the goods so sold, and the plaintiff vendor has priority over the Bank with respect to the goods, unless some provision in either the *Bank Act* or the P.P.S.A. takes away the vendor's priority or precludes the enforcement of its agreement. Reference may conveniently be made to *Bank of Montreal v. Guaranty Silk Dyeing & Finishing Co. Ltd.*, [1935] O.R. 493, [1935] 4 D.L.R. 483, 16 C.B.R. 363, where Masten, J.A., said at p. 506 O.R., p. 489 D.L.R.:

... in my opinion, The Bank Act purports to confer on a bank holding a security under sec. 88 only such right and title to the goods, wares and merchandise therein mentioned as was at the time held by the person who gives such security to the bank. Such I think is the meaning of subsec. 7 of sec. 88 and of subsec. 2(b) of sec. 86 of The Bank Act, R.S.C. 1927, ch. 12.

(Section 88(7) referred to is the substantial equivalent of the present s. 88(2)(c) and s. 86(2)(b) is virtually unchanged as s. 86(2)(b) of the present *Bank Act*.) At that time s. 88 did not enable a bank to acquire security on after-acquired property, but the legal position as to after-acquired property must be the same as that of presently-owned property, albeit as of a later date; as and when the bank's customer acquires an interest in property, subsequent to the giving of s. 88 security, the bank acquires as security the interest of the customer in that property. In the case of a conditional purchaser, the value of the interest of the purchaser increases as further payments to the vendor are made, and the bank's security grows correspondingly more valuable in respect of the goods purchased under the conditional sale.

The P.P.S.A. cannot prejudicially affect the Bank's interest, acquired pursuant to a federal statute. Conversely, the P.P.S.A. confers no rights or priority on the Bank on the facts of this case. The only relevance of the P.P.S.A. is whether it prejudicially affects the plaintiff's interest....²¹ [Emphasis added.]

[18] In concurring reasons, Houlden J.A. also construed the *Bank Act*, found that it did not confer priority on the bank, and held that the *PPSA* did not provide the applicable priority rule. He wrote:

If it is assumed for the purposes of this appeal that Four Seasons was the owner of the lumber within the meaning of s. 88(2), then, by virtue of the above sections, Four Seasons could not give the bank any greater right or title to the lumber than it itself possessed: *Bank of Montreal v. Guaranty Silk Dyeing & Finishing Co. Ltd.*, [1935] O.R. 493, [1935] 4 D.L.R. 483, 16 C.B.R. 363. Four Seasons having paid nothing to the bank and having done nothing to add to the value of the lumber, the bank acquired nothing under its s. 88 security.

Section 87 of the *Bank Act* provides that if a previous holder of a warehouse receipt or bill of lading is a person entrusted with the possession of goods by the owner thereof, upon the acquisition of the warehouse receipt or bill of lading, the bank becomes vested with all the right and title of the owner. This section has, however, no application to s. 88 security since in the case of s. 88 security, the warehouse receipt or bill of lading is made directly to the bank and there is no previous holder: *Barry v. Bank of Ottawa* (1909), 17 O.L.R. 83.²²

In the result, the *Bank Act* “conferred no rights or priority on the bank on the facts of this case.”²³

[19] Wilson J.A. (as she then was) dissented on the basis that, at the time of the delivery of the collateral to the conditional purchaser, it fully became an “owner,” which meant that the bank’s prior interest in the after-acquired

²¹ *Rogerson*, *supra* note 16, pp. 676-77.

²² *Ibid.*, p. 682.

²³ *Ibid.* See also *Kawai Canada Music Ltd. v. Encore Music Ltd.* (c.o.b. *Electronic Keyboard Centre*), (1993), 101 D.L.R. (4th) 1 (Alta C.A.), leave to appeal to S.C.C. refused [1993] 3 S.C.R. ix, which concerned *Bank Act* security and subsequently registered security interests taken under the *Conditional Sales Act*, R.S.A. 1980, c. C-21. The Court followed *Rogerson* and found in favour of the conditional seller.

property attached to the collateral. The interest of the supplier in her view was, in essence, a right “subsequently acquired in, on or in respect of” the debtor’s property, to use the words of s. 428(1) of the *Bank Act*.

[20] The overall significance of the majority’s decision in *Rogerson*, for the purposes of the appeal before this Court, cannot be overstated. The equivalent of s. 428(1) of the *Bank Act* did not apply, notwithstanding the fact that the interest of the seller was subsequent to that of the bank. The *PPSA* did not apply so as to grant priority to the bank, notwithstanding the fact that the *PPSA* interest was unperfected. The unregistered *PPSA* interest was not subordinated to the *Bank Act* interest, as the bank security was not one of the types of interests falling within the protection of the provincial legislation. Priority was accorded to the subsequent unregistered interest based on an application of the principles of property law, the vendor having, in effect, retained full title, and in a jurisdiction that in 1980 had adopted a modern personal property registration system.

[21] Some seven years later, this Court in *Pulsar*²⁴ considered a priority competition between a *Bank Act* security and a subsequently taken and perfected *PPSA* security interest in the same collateral. The principal issue was whether the assignment of a security interest in present and after-acquired property, granted pursuant to s. 178 [now s. 427] of the *Bank Act*, takes priority over a perfected security interest in the same after-acquired property granted subsequently under the *PPSA*. To resolve this question, the Court, like the Court in *Rogerson*, had to address the question of the appropriate

²⁴ *Pulsar*, *supra* note 17.

analytical framework, but this time to resolve a priority dispute between federally and provincially created security interests, in after-acquired property. The issue was complicated by the fact that the bank had also registered its interest under the *PPSA*.

[22] Vancise J.A., for the Court in *Pulsar*, wrote:

In order to resolve the question of priority one must examine the relevant provisions of the *Bank Act*, which is the law that governs any dispute between *Bank Act* security and a provincial security interest: see *Landry Pulpwood v. Banque Can. Nat.*, [1927] S.C.R. 605 at 615. If the *Bank Act* provides directly or by implication a priority rule, then that provision will govern notwithstanding that it is in conflict with a provincial scheme of priorities. This rule is based on the primacy of federal law. The relevant provisions of the *Bank Act* are ss. 178, 179 and 180. Those sections set out provisions governing the priority of a s. 178 interest. A s. 178 security interest does not have to be registered in a personal property security registry and its priority is not governed by the internal rules of *The Personal Property Security Act*.²⁵

...

In this case the security interest granted to the bank was first in time, both as to date of registration under s. 178(4) and entering into a security agreement under s. 178(1). If the security interest granted by the borrower to Pulsar had been perfected prior in time to the bank taking the assignment, then its security would have attached to the after-acquired property in priority to that of the bank. Cuming and Wood argue that priority between a s. 178 security interest and a personal property security interest should be determined by awarding it to the person who first enters into a security agreement. They state [at pp. 276-77]:

When a similar dispute arises between equitable charges or mortgages, equity awards priority to the holder of the agreement which was first executed: *qui est in tempore potior est jure*. The principle underlying this rule is the idea that a present though inchoate security interest arises when an agreement is executed. Professor Goode has described its theoretical basis:

“Here we have a striking example of the intellectual subtlety of the common law. In a number of cases the courts have ruled that whilst, in a sense, an agreement for security over after-acquired property cannot attach to that property prior to acquisition, yet the agreement constitutes a *present* security. In other words, it creates an inchoate security interest which is waiting for the asset to be acquired so that it can fasten on to the asset but which, upon acquisition of the asset, takes effect *as from the date of the*

²⁵ *Ibid.*, p. 253.

security agreement. Acquisition of the asset produces the situation in which the security is deemed to have continuously attached to the asset from the time of execution of the security agreement. This may seem metaphysical but has its counterpart in other branches of law.”

A first in time priority rule has also been applied in a priority dispute between two banks each claiming section 178 security interests in after-acquired property. [*Royal Bank of Canada v. Bank of Montreal*, [1976] 4 W.W.R. 721 (Sask. C.A.)].

In the absence of an effective registration system, I favour this approach.

...

What is of significance in determining priority here is the time at which the respective security interests were entered into. The appellant's security interest was granted prior in time to the respondent's security interest under *The Personal Property Security Act* and it attaches to the inventory in priority to the respondent's security interest.

Section 179 of the *Bank Act* sets out the basic scheme governing the priority to a bank's claim pursuant to s. 178. That section provides that the bank's rights in the secured property have priority "over all rights subsequently acquired in, on or in respect of such property", and also over "the claim of any unpaid vendor" except in circumstances where the unpaid vendor has a lien on the property and the bank has knowledge of the lien at the time it takes its security. Section 179(1) clearly establishes that a bank's s. 178 security takes priority over competing claims that are created or arise at a later time than the assignment to the bank.

The appellant [the Bank] therefore has priority over the respondent [Pulsar] in connection with the inventory secured by the s. 178 assignment.²⁶

[Italics in original; underlining mine.]

Thus, the Court in *Pulsar* set aside the priority rules of the *PPSA*, and looked to the *Bank Act* to resolve the dispute. Since both interests attached simultaneously, s. 179(1) [now s. 428(1)], which refers to “subsequently” acquired interests, however, could not apply. The Court concluded that “[w]hat is of significance in determining priority here is the time at which the respective security interests were entered into.”

²⁶ *Ibid.*, pp. 259-60.

[23] The next decision, in this line of jurisprudence, is *International Harvester*,²⁷ where the Ontario Court of Appeal considered a priority competition between an imperfectly registered conditional sales contract and a subsequent *Bank Act* security. When the debtor defaulted, the bank applied for a declaration that its interest had priority over the prior unperfected security interest. As in *Pulsar*, the case was complicated by the fact that the bank had registered its claim under the *PPSA*, as well as under the *Bank Act*. In consequence, all three judges wrote, with differing approaches and emphasis. Nonetheless, the result is clear: judgment was granted in favour of the prior unperfected provincially created security interest.

[24] Houlden J.A. writes most clearly on the issue raised by this appeal:

... If the security agreement which gives rise to the bank's security interest were not given pursuant to s. 178 of the *Bank Act*, Watt J. would be clearly right. If, for example, instead of s. 178 security, the bank had taken a general security agreement covering all the farm machinery of Howe and had properly perfected its security interest under the *P.P.S.A.*, the bank would have had priority over the unperfected security interest of I.H.C.C. But the bank's security agreement was given pursuant to s. 178 of the *Bank Act*, and it is essential, therefore, to turn to that statute to see what rights are given to the bank by its security agreement: see *Landry Pulpwood Co. v. Banque Canadienne Nationale*, [1928] 1 D.L.R. 493 at p. 500, [1927] S.C.R. 605.

The conditional sales contracts were executed on May 6 and 14, 1981. They were immediately assigned by the vendor to I.H.C.C. The notice of intention to give security pursuant to s. 178 of the *Bank Act* was executed on August 14, 1981, and registered on August 18, 1981. The bank made its loan on June 17, 1983, and took as security an assignment of all the farm machinery of Howe. The only property interest that Howe owned at the time that he gave the s. 178 security interest to the bank was any equity that he possessed in the farm machinery. Section 178 security interest is a creature of statute, and by ss. 178(2) and 186(2), the only property that Howe could encumber when he gave the s. 178 security interest to the bank was the equity that he owned and might thereafter own in the farm machinery.

Section 179(1), in my opinion, confirms this position. It provides that the bank's rights and powers under its s. 178 security have "priority over all rights

²⁷ *International Harvester*, *supra* note 18.

subsequently acquired in, on or in respect of such property". The rights of I.H.C.C. under its conditional sales contracts were acquired prior to, not subsequent to the bank acquiring its rights. Section 179(1) also gives the bank priority "over the claim of any unpaid vendor", but I adhere to what I said in *Rogerson Lumber Co. v. Four Seasons Chalet Ltd.*, *supra*, that "vendor" in s. 179(1) should not be interpreted to include a vendor under a conditional sales contract.

In *Bank of Montreal v. Hall*, (1990), 65 D.L.R. (4th) 361, [1990] 1 S.C.R. 121, [1990] 2 W.W.R. 193, La Forest J. adopted, at p. 370, as accurate the following description of the s. 178 security interest given by Professor Moull in his article in the Canadian Bar Review, *op.cit.*, at p. 251:

The result, then, is that a bank taking security under section 178 effectively acquires legal title to the borrower's interest in the present and after-acquired property assigned to it by the borrower. The bank's interest attaches to the assigned property when the security is given or the property is acquired by the borrower and remains attached until released by the bank, despite changes in the attributes or composition of the assigned property. The borrower retains an equitable right of redemption, of course, *but the bank effectively acquires legal title to whatever rights the borrower holds in the assigned property from time to time.*

The only interest that Howe had in the farm machinery at the time that he gave the s. 178 security to the bank was, as I have said, the equity that he possessed in the machinery at that time or that he might subsequently acquire.²⁸

[Emphasis in original.]

The Court held, in the words of McKinlay J.A., that "neither the provisions of the *Bank Act* which provide for the security nor the provisions of the security document itself give to the bank anything other than the interest which Howe had in the equipment."²⁹ Similarly, Grange J.A. wrote: "I have no doubt that the bank intended and tried to get priority over I.H.C.C. to all the collateral but to succeed in that endeavour it would have had to use a document which purported to give it security on the whole and not just one

²⁸ *Ibid.*, pp. 388-90. Section 9 of Ontario's *Personal Property Security Act*, R.S.O. 1980, c. 375 provided: "[e]xcept as otherwise provided by this or any other Act, a security agreement is effective according to its terms between the parties to it and against third parties."

²⁹ *Ibid.*, p. 400.

which on its face and under the *Bank Act*, S.C. 1980-81-82-83, c. 40 (Part I, s. 2), gave it security only on the borrower's interest in the whole.”³⁰

[25] The significance of *International Harvester* for the instant appeal is that the Court accorded priority to a “prior unregistered provincially created interest.” The bank attempted to rely on the provincial registration of its federally created interest as a means of defeating that interest. Like the case before this Court, if the bank had taken and perfected a provincially created interest, that interest would have prevailed. The Ontario Court of Appeal, however, had no difficulty in rejecting the bank’s approach to resolving the dispute.

[26] *International Harvester* is not squarely on all fours with the instant appeal, however, because the prior unperfected interest in that case was in the form of a traditional title retention security agreement, i.e., a conditional sales contract, whereas in the present case, the prior unperfected interest takes the form of a general security agreement. Nonetheless, the decision is significant because the Court held, as it did in *Rogerson*, that the bank could not acquire, by registration under the *PPSA*, anything more than its security documentation, and the *Bank Act*, had already given it. The Court found that the *Bank Act* gave to the bank only that which remained after the prior unperfected security interest had been given, or in other words, *nemo dat quod non habet*.

³⁰ *Ibid.*, p. 390.

[27] Building on the analysis of these decisions, we reach another decision from this Court: *Agricultural Credit*.³¹ This decision concerned a registered and, therefore, perfected *PPSA* security agreement, and a subsequent *Bank Act* security registered under the *Bank Act*, both claiming an interest in the same collateral. To resolve this dispute, Bayda C.J summarized what he found to be the state of the law regarding the appropriate approach to resolving a priority dispute between provincially and federally created interests. He wrote, for the Court:

In a priority dispute between a s. 178 *Bank Act* security and a security interest that is perfected or is perfectible under the *PPSA*, there are, generally speaking, three basic rules to follow for determining the priority: (1) set aside the *PPSA* from the analysis and determine the priority as if the *PPSA* did not exist; (2) determine the priority pursuant to ss. 178, 179 and 180 of the *Bank Act* (and such other provisions as may be applicable to the circumstances) to the extent it is possible to do so; (3) where appropriate, apply the first-in-time priority rule. (See *Moose Jaw v. Pulsar Ventures Inc.*, (1987), 42 D.L.R. (4th) 385, [1988] 1 W.W.R. 250 (Sask. C.A.); Cuming and Wood, "Compatibility of Federal and Provincial Property Security Law" (1986) Can. Bar Rev. 267 at pp. 274 and 276-7; Ronald C.C. Cuming, "The Position Paper on Revised Bank Act Security: Rehabilitation of Canadian Personal Property Security Law or Curing the Illness by Killing the Patient" (1992), 20 C.B.L.J. 336; *Royal Bank of Canada v. Bank of Montreal* (1976), 67 D.L.R. (3d) 755, [1976] 4 W.W.R. 721 (Sask. C.A.)). An application of these rules to the present case produces this result: because the security interest created by the ACS 1985 Security Agreement came into existence on September 24, 1985, and thus predated the Bank's s. 178 security interests created by the October 3, 1985 and October 3, 1986 general assignments, the former supersedes and takes priority over the latter. (In following this approach I make no comment on the use by the Bank of the provincial filing system to register *Bank Act* security.)³² [Emphasis added.]

Bayda C.J. noted that the foregoing conclusion was "in complete consonance with this court's decision in *Pulsar*" where "the first-in-time priority rule applied and the bank succeeded."³³ He noted, however, that in the case before

³¹ *Agricultural Credit*, *supra* note 19.

³² *Ibid.*, p. 586-87.

³³ *Ibid.*, p. 587.

him the same rule resulted in a different outcome, because “all of the advances by the bank to the debtor and the governing assignments creating the securities in respect of those advances were made *after* the security interest created by the security agreement entered into by the opposing claimant (ACS)”³⁴ [emphasis in original]. The Court concluded that the *PPSA* security, taken and registered prior in time, had priority over the subsequently taken and registered *Bank Act* interest.

[28] Finally, in *Moosomin Credit Union*,³⁵ Lane J.A. summarized this Court’s approach to the resolution of disputes between provincially and federally created security interests:

[38] This Court, in *Royal Bank v. Agricultural Credit Corp. of Saskatchewan* puts it clearly that the common law must be resorted to in order to resolve the priority in such disputes [between *Bank Act* and *PPSA* security].³⁶ [Footnote omitted.]

In the same decision, Sherstobitoff J.A., concurring with Lane J.A. on this point, held that when a prior executed *Bank Act* security interest has attached pursuant to an after-acquired property clause and the *PPSA* interest has later attached, both the common law principle of *nemo dat quod non habet* and the principle of “first-in-time” provide priority to the first taken security interest. Sherstobitoff J.A. wrote:

[5] The loan application and security agreement referred to in the affidavit were dated August 25, 1998, and the Credit Union advanced the money on September 11, 1998. However, since the Bank’s security had attached on August 12, 1998, the McNary’s had no interest to give as security – *nemo dat quod non habet*. Furthermore, the first-in-time principle gave the Bank priority to any claim over the Credit Union: *Moose Jaw (City) v. Pulsar Ventures Inc.* (1987), [1988] 1 W.W.R.

³⁴ *Ibid.*, p. 587-88.

³⁵ *Moosomin Credit Union*, *supra* note 20.

³⁶ *Ibid.*

250 (Sask. C.A.), *Royal Bank v. Agricultural Credit Corp. of Saskatchewan*, [1994]
7 W.W.R. 305 (Sask. C.A.).³⁷

Vancise J.A. concurred with both decisions.

[29] The Chambers judge, in the instant case, attempted to distinguish each of the Saskatchewan decisions. In my respectful opinion, however, if one looks at the analytical framework adopted by these decisions, it is not possible to do so. While there are differences in the factual circumstances, each of these decisions follows the general framework articulated in *Agricultural Credit*: (i) set aside the priority rules of the *PPSA*; and (ii) construe the *Bank Act* to determine if there is any priority rule that may apply. This may involve an examination of the ordinary law of the province to determine what proprietary rights the debtor retains after a prior security interest has been granted. It may also be necessary to apply the first-in-time principle to resolve a given dispute.

[30] It is within this jurisprudential framework that the instant appeal must be decided. The issue is whether the result changes by virtue of the fact that the Credit Union's prior interest was unperfected at the time the Bank took delivery of its security documentation.

VI. Does the priority rule created by s. 428(1) of the *Bank Act* apply?

[31] The Chambers judge interpreted s. 428(1) as creating a priority rule in favour of prior rights, and then decided that those prior rights had to be registered in order to defeat a subsequent *Bank Act* interest. In addition to

³⁷*Ibid.*

implying a priority rule into the section, this interpretation rests on an understanding that the purpose of registration is one of “notice to all.”³⁸ Registration, in the context of the *PPSA*, does not serve this purpose. While its incidental purpose is to permit prospective creditors to search debtor names, and certain types of personal property by virtue of serial numbers, the fundamental effect of registration is to establish priorities by virtue of the time of registration, and for the purposes of the *PPSA* only. Registration no longer constitutes actual or constructive notice in the context of the *PPSA*. Section 47 of the *PPSA* abolishes that concept.

[32] The Chambers judge’s decision permits the Bank to rely on the Credit Union’s failure to register, when the *PPSA* appears to direct the Court away from that conclusion. The Saskatchewan legislature, in its 1993 legislation,³⁹ after this Court’s decision in *Pulsar*, amended the *PPSA* so as to prevent it from being used to resolve priority disputes between *Bank Act* and *PPSA* security. To accomplish this purpose, the legislature declared that *Bank Act* security is not security for the purposes of the *PPSA*:

4 Except as otherwise provided in this Act or the regulations, this Act does not apply to:

...

(k) a security agreement governed by an Act of the Parliament of Canada that deals with the rights of parties to the agreement or the rights of third parties affected by a security interest created by the agreement, including an agreement governed by sections 425 to 436 of the *Bank Act* (Canada).

This amendment has the effect of reinforcing the conclusion in *Rogerson* that a bank has only the rights accorded to it by the *Bank Act*. Therefore, a bank holding security taken pursuant to the *Bank Act* cannot gain access to the

³⁸*Innovation Credit Union v. Bank of Montreal*, *supra* note 3 at para. 53.

³⁹S.S. 1993, c. P-6.2, which came into force on the proclamation date of April 1, 1995.

PPSA priority regime, which provides that a perfected security interest takes priority over an unperfected one (see s. 35(1)).

[33] Then in 2000, the legislature added a further provision:

9(2) A security interest in collateral ceases to be valid with respect to that collateral to the extent that and for so long as the security interest secures payment or performance of an obligation that is also secured by a security in favour of that secured party on that collateral created pursuant to sections 425 to 436 of the *Bank Act* (Canada).⁴⁰

[34] In adding these provisions, the legislature was informed by two reports of the Law Reform Commission of Saskatchewan. In *Tentative Proposals for a New Personal Property Security Act, 1990*, the Law Reform Commission recommended the inclusion of s. 4(k):

It is understandable that the banks should want to convince the courts that section 178 security interests are also Personal Property Security Act security interests. What they want is the reversal of the Rogerson Lumber decision [(1980), 113 D.L.R. (3d) 671 (Ont. C.A.)] so that when they take section 178 security interests in collateral they can determine by a check of the Personal Property Registry whether or not the collateral is subject to a prior provincial security interest to which they will be subject.

The consequence of treating section 178 security interests as Personal Property Security Act security interests is that the banks can have the benefits of The Personal Property Security Act priority system without being bound by it. They hold federally created section 178 security interests and provincial law cannot adversely affect the rights given to the banks by federal law. In the result, the elaborate and highly integrated priority structure of The Personal Property Security Act would be fragmented and applied only piecemeal where section 178 security interests are involved.

As a matter of general public policy, every reasonable effort should be made to reduce the risk to the banks by giving to them the benefits of the provincial registry systems. However, it is the opinion of the Commission that these benefits should not be surrendered by the Saskatchewan Legislature without gaining in return a change in federal law that would introduce a greater measure of

⁴⁰ This formulation was added by *The Personal Property Security Amendment Act, 2000*, S.S. 2000, c. 21.

federal-provincial rationalization in this area of the law and thereby put both provincial lenders and federal banks on a roughly equal legal (and therefore competitive) basis.

Changes in both federal and provincial personal property security law and in business practices which have occurred in recent years have made it necessary to take a very different approach to matters arising from the interface between section 178 of the Bank Act and provincial Personal Property Security Acts. No longer is it sufficient to take the position that section 178 of the Bank Act is a matter solely for the banks and the Federal Department of Finance. What is required is a concerted federal-provincial effort to harmonize Canadian personal property security law so as to facilitate secured lending and to remove distortions in this market produced by differences in federal and provincial law.⁴¹

[35] By 1992 the Commission was of the view that there was little hope for change to the *Bank Act* in the short term. Thus, in its final Report to the Minister of Justice, it recommended that the Saskatchewan legislature go further to provide certainty as to the relationship between the two systems. The Commission wrote:

The Commission has reluctantly come to the conclusion that further measures must be taken to attempt to reduce the difficulties associated with overlap of federal and provincial personal property security legislation. Accordingly, it has recommended in this report the addition of a new subsection to section 4 which is designed to prevent banks from having a provincial security interest and a federal security interest in the same collateral to secure the same obligation. The approach adopted is to declare void a security interest in collateral that secures an obligation also secured by the security interest in the same collateral taken under the *Bank Act*. A detailed explanation of the provision is set out in commentary accompanying section 9(2) of the proposed legislation.⁴²

[36] The Commission went on to describe the purpose of s. 9(2):

Section 9(2) is a companion provision to section 4(k). While section 4(k) is designed to preclude the argument that a Bank Act security is a security interest under this Act, this provision is designed to nullify security interests arising under

⁴¹ *Tentative Proposals for a New Personal Property Security Act* (Saskatoon: Law Reform Commission of Saskatchewan, 1990) at pp. 57-58.

⁴² *Proposals for a New Personal Property Security Act, Report to the Minister of Justice* (Saskatoon: Law Reform Commission of Saskatchewan, 1992) at p. 2.

security agreements in situations where a bank takes both a provincial security interest and a Bank Act security in the same collateral to secure the same obligation. The approach taken in section 9(2) is quite different from that taken in section 4(k). In order to preclude banks from claiming that their Bank Act interests are security interests under the Act, it is sufficient to exclude federal security agreements from the scope of the Act. However, in order to force banks to choose between rights under federal or provincial personal property security law, it is necessary to nullify any attempt to invoke provincial law through a security agreement paralleling an agreement providing for a Bank Act security.⁴³

[37] Counsel for the Credit Union submitted that the reason why the legislature adopted the Law Reform Commission's recommendation on this point was to place pressure on federal lending institutions to use the *PPSA* only, and thereby make the provincial exemption and enforcement mechanisms apply for all debtors. From a juridical standpoint, however, the only salient point with which this Court is entitled to concern itself is that, in this jurisdiction, the legislature has denied the banks the benefit of the priority rules contained in the *PPSA* unless a security interest is taken under that *Act*. The legislature has made its intention clear.

[38] With much respect, the Chambers judge has interpreted s. 428(1) so as to grant priority to *Bank Act* security over a prior, unperfected *PPSA* security interest and thereby created a new priority rule. This is a reading of s. 428(1) that cannot be given to it and is contrary to all past authority. Further, such a priority rule would permit the Bank to rely on the Credit Union's failure to register, which is contrary to the intent of s. 4(k) of the *PPSA*. As will be seen, s. 428(1) may be used to support an interpretation that the *Bank Act* relies on provincial law to determine what a bank acquires when it takes s. 427 security,

⁴³ *Ibid.*, p. 30.

but it does no more than that *vis à vis* a security interest taken prior to the *Bank Act* interest. In summary, s. 428(1) of the *Bank Act* does not apply to resolve the instant dispute.

VII. Do ss. 427(2) and 435(2) of the *Bank Act* apply to resolve this priority dispute?

[39] The issue at this point is whether some other rule in the *Bank Act* applies, or whether we have reached the point in the analysis, referred to in *Agricultural Credit*, where the first-in-time or other common law or equitable priority rule is applied.

[40] The section of the *Bank Act* to be considered first is s. 427(2). It reads:

Rights and powers vested by delivery of document

427. (2) Delivery of a document giving security on property to a bank under the authority of this section vests in the bank in respect of the property therein described

(a) of which the person giving security is the owner at the time of the delivery of the document, or

(b) of which that person becomes the owner at any time thereafter before the release of the security by the bank, whether or not the property is in existence at the time of the delivery,

the following rights and powers, namely,

(c) if the property is property on which security is given under paragraph (1) ... (n) consisting of agricultural implements ..., the same rights and powers as if the bank had acquired a warehouse receipt or bill of lading in which that property was described, or

(d) if the property

...

(v) is property on which security is given under paragraph (1)(n) consisting of agricultural equipment, or

...

a first and preferential lien and claim thereon for the sum secured and interest thereon, and as regards a crop as well before as after the severance from the

soil, harvesting or threshing thereof, and, in addition thereto, the same rights and powers in respect of the property as if the bank had acquired a warehouse receipt or bill of lading in which the property was described, and all rights and powers of the bank subsist notwithstanding that the property is affixed to real property and notwithstanding that the person giving the security is not the owner of that real property,

and all such property in respect of which such rights and powers are vested in the bank under this section is for the purposes of this Act property covered by the security.

[Emphasis added.]

This section makes two important statements relevant to the within appeal.

[41] First, it states that the bank receives a “first and preferential lien and claim thereon for the sum secured and interest thereon.” Second, it states that the bank acquires “the same rights and powers in respect of the property as if the bank had acquired a warehouse receipt or bill of lading in which the property was described.”

[42] The reference to the creation of a “first and preferential lien” does not increase the priority position of a bank *vis à vis* another secured creditor of personal property for this reason: it is contrary to the other, explicit priority rules contained in the *Bank Act*. Thus, this aspect of s. 427(2) has been interpreted, not as a priority rule *per se*, but as a statement of the nature of the interest acquired, and for the purposes of addressing conflicts between a bank and the holder of an underlying interest in real property upon which agricultural equipment or crops are affixed, for example. See William D. Moull, “Security under Sections 177 and 178 of the Bank Act.”⁴⁴

⁴⁴ William D. Moull, “Security under Sections 177 and 178 of the Bank Act” (1986) 65 Can. Bar Rev. 242 at 252-53. See also Poirier, *supra* note 10 at p. 314 and his footnoted references.

[43] The second aspect of s. 427(2) states that the bank acquires “the same rights and powers in respect of the property as if the bank had acquired a warehouse receipt or bill of lading in which the property was described.” This has been labeled the “document of title fiction.”⁴⁵

[44] The document of title fiction arises in this manner. The *Bank Act* describes what a bank acquires when taking a warehouse receipt or bill of lading:

Warehouse receipts and bills of lading

435. (1) A bank may acquire and hold any warehouse receipt or bill of lading as security for the payment of any debt incurred in its favour, or as security for any liability incurred by it for any person, in the course of its banking business.

Effect of taking

(2) Any warehouse receipt or bill of lading acquired by a bank under subsection (1) vests in the bank, from the date of the acquisition thereof,

(a) all the right and title to the warehouse receipt or bill of lading and to the goods, wares and merchandise covered thereby of the previous holder or owner thereof; and

(b) all the right and title to the goods, wares and merchandise mentioned therein of the person from whom the goods, wares and merchandise were received or acquired by the bank, if the warehouse receipt or bill of lading is made directly in favour of the bank, instead of to the previous holder or owner of the goods, wares and merchandise.⁴⁶

[Emphasis added.]

It then must be determined what interest a bank acquires in personal property secured by a s. 427 interest, by reference to what a bank acquires by taking a warehouse receipt or bill of lading, both of which are themselves documents of title.

⁴⁵ Roderick J. Wood, “The Nature and Definition of Federal Security Interests,” (2001) 34 Can. Bus. L.J. 65 at 75.

⁴⁶ *Bank Act*, *supra* note 2.

[45] With few exceptions, judicial authority and the commentators are agreed that s. 435(2) is to be given its plain meaning: a bank acquires only the “right and title” of the person from whom the interest is taken, and leaves to the law of the province to determine what that means. The earliest authority on point is *William A. Marsh Co. v. Buzzell*,⁴⁷ wherein Gibsone J. wrote:

1 (a) It is neither the purpose nor the effect of *The Bank Act*, section 88 ***, to make the security receipt effective to transfer to the bank more rights in the merchandise, etc., than the customer himself has; in other words, it is only the rights in the merchandise which the customer himself has which are transferred to the bank by the security, the rights which third persons may have in the merchandise are not affected or diminished by the act of the customer in giving the security receipt to the bank;

(b) The fact that the customer might have, either erroneously or falsely, represented to the bank that he was owner, when he was not, would not deprive the real owner of his rights;

(c) As against another claimant to the merchandise, in general, the bank is entitled only to the rights which its customer had and which its customer transferred to it.⁴⁸

Buzzell was subsequently followed in *Bank of Montreal v. Guaranty Silk Dyeing & Finishing Co.*,⁴⁹ a decision which formed the foundation of the reasoning in *International Harvester*.⁵⁰

[46] There are no judicial decisions that take a contrary view to this interpretation, but there are a few commentators who have done so. In *Crawford and Falconbridge*,⁵¹ two conflicting statements as to the interpretation of s. 435(2) appear:

⁴⁷ (1928-30), 11 C.B.R. 463 (Que. Sup. Ct.).

⁴⁸ *Ibid.*, p. 466.

⁴⁹ [1935] 4 D.L.R. 483 (Ont. C.A.).

⁵⁰ *International Harvester*, *supra* note 18.

⁵¹ Bradley Crawford, *Crawford and Falconbridge Banking and Bills of Exchange*, 8th ed. (Aurora, Ont.: Canada Law Book, 1986).

Subsection 178(2) [s. 427(2)] equates the position of the bank with that of the holder of a warehouse receipt or bill of lading. The effect of that under the *Bank Act* is set out in sub-ss. 186(2) [s. 435(2)] and 187(1), which provide that where a bank does in fact acquire a warehouse receipt or bill of lading from a customer as security for any debt or liability, it is vested with all the right, title and interest that the previous holder had and intended to pass by endorsing and delivering the receipt. Where the holder was the owner, that interest may be plenary: the bank may acquire the title to the goods. Where the holder was not the owner then, subject to one exception, the bank may take only whatever interest the holder had.... [Footnotes omitted.]⁵²

That quotation states that s. 435(2) gives to a bank only that which the debtor holds. This next passage, taken from further on in the same text, appears to take the contrary position however:

If the bank actually *had* received a bill of lading for the described collateral from the owner, all the existing P.P.S.A.s would give its interest under such a document priority over even perfected security interests in either the goods or the document of title. In order for a security interest in a document of title or in goods represented by a document of title to become perfected, it is necessary for the secured creditor to obtain possession of the document. We can see no reason why the result should be any different merely because there is not any bill of lading in fact, so long as the federal law is competent to require that the rights of the bank be determined *as if* there were.

However, even on this footing the matter is not free of doubt....⁵³

[Emphasis in original; footnotes omitted.]

[47] In a later article on this point, Mr. Bradley Crawford, Q.C. stresses the latter passage quoted above:

... As I noted in 1984, if the bank really had received a clean bill of lading or negotiable warehouse receipt describing the goods (instead of merely being deemed to have received one), it would have taken priority over even a perfected PMSI in the collateral by reason of the rules protecting *bona fide* purchasers in good faith etc. I remain uncontrite on that point.

...

But, if the bank's rights are to be determined solely with reference to the *Bank Act* on this point, why stop at section 186? Section 187 opens another route

⁵² *Ibid.*, p. 424 (vol 1).

⁵³ *Ibid.*, pp. 444-45.

for the bank by giving it the rights of the owner of the goods when the warehouse receipt is transferred to the bank by a person who was entrusted with it by the owner. That is rather like what occurs when a person who has goods under a PMSI agreement purports to transfer them to the bank to defeat the PMSI holder's interest. On that reading, section 187 would give the bank the right and title of the "owner" – i.e., the PMSI holder. The reasoning is admittedly highly technical, but no more so than the reasoning the Court actually used. It has the advantage of preventing an unperfected interest from prevailing, but it does not recommend itself as a convincing means of rationalizing the two statutes' priority schemes over the long term.⁵⁴

[Emphasis in original; footnotes omitted.]

The difficulty with this interpretation of s. 435(2) is that it is contrary to the words of the section, which refer to acquiring "all the right and title to the goods...mentioned therein of the person from whom the goods...were received or acquired by the bank." It also leads to the anomalous situation, recognized by Mr. Crawford, of a bank defeating all prior rights including those acquired pursuant to title retention documents, and leases and consignments, as well as general security agreements, even though such interests may have been duly registered.

[48] That may explain why the majority of the commentators take a different view. Professor Moull writes:

Quite apart from the Bank Act, acquisition of a warehouse receipt or bill of lading typically passes title to the goods covered thereby. However, section 186 of the Act amplifies upon the rights and powers that a bank acquires when it takes a warehouse receipt or bill of lading as security. By subsection (2), any warehouse receipt or bill of lading acquired by a bank under that section vests in the bank, from the date of its acquisition, "all the right and title to the warehouse receipt or bill of lading and to the goods, wares and merchandise covered thereby of the previous holder or owner thereof". As well, by section 179(7) the bank's interest under a warehouse receipt, bill of lading or section 178 security is not affected as the subject goods, wares and merchandise are converted or incorporated into other goods, wares and merchandise in the process of manufacture or production.

⁵⁴ Bradley Crawford, Q.C., "Interaction Between the PPSA and Section 178 of the *Bank Act*" (1992-93) 8 B.F.L.R. 1 at pp. 11-12.

The result, then, is that a bank taking security under section 178 effectively acquires legal title to the borrower's interest in the present and after-acquired property assigned to it by the borrower. The bank's interest attaches to the assigned property when the security is given or the property is acquired by the borrower and remains attached until released by the bank, despite changes in the attributes or composition of the assigned property. The borrower retains an equitable right of redemption, of course, but the bank effectively acquires legal title to whatever rights the borrower holds in the assigned property from time to time.⁵⁵ [Emphasis added.]

[49] Professors Cuming and Wood take the same approach:

... Under section 186(2), the acquisition of a warehouse receipt or bill of lading vests in the bank "all the right and title to the warehouse receipt or bill of lading and to the goods, wares and merchandise covered thereby of the previous holder or owner thereof". Paragraphs (a) and (b) of section 178(2) identify the property to which the bank's interest attaches. Attachment occurs when the debtor becomes the owner of the goods. Thus if the debtor is merely a bailee or lessee of the goods, the bank's interest will not attach. However, the interest of a buyer under a conditional sales agreement is sufficient to constitute the buyer an owner for the purposes of this provision.

The effect of a section 178 security interest is not determined by paragraphs (a) and (b), but rather by paragraphs (c) or (d). Upon attachment of the interest, the bank is in the same position as if a bill of lading covering the goods had been immediately transferred to it. If the bank's customer has legal title, the bank acquires it; if the debtor does not have legal title, then the bank will obtain whatever right is possessed by the debtor. The position of the bank is, in many respects, not unlike that of a mortgagee.⁵⁶

[Emphasis added; footnotes omitted.]

[50] In "Atomic Slipper Co. v. Banque Nat. du Can.: Commercial Practice Meets Constitutional Law,"⁵⁷ Professor MacDonald agrees:

What does this reference to warehouse receipts and bills of lading mean? It

⁵⁵ Moull, *supra* note 44 at 251.

⁵⁶ Ronald C.C. Cuming and Roderick J. Wood, "Compatibility of Federal and Provincial Property Security Law" (1986) 65 Can. Bar Rev. 267 at 272.

⁵⁷ Roderick A. MacDonald, "Atomic Slipper Co. v. Banque Nat. du Can.: Commercial Practice Meets Constitutional Law" (1989) 73 C.B.R. (N.S.) 1. See also Roderick A. MacDonald, "Provincial Law and Federal Commercial Law: Is "Atomic Slipper" a New Beginning?" (1992) 7 B.F.L.R. 437 at 442 and 449.

means that as against third parties the bank stands in the shoes of the debtor and is vested with all the debtor's rights against them. Whatever the nature of the debtor's ownership title – be this as equitable owner, owner under suspensive condition, bare-owner, substitute, institute, owner under resolutive condition, or simple owner – the bank acquires the debtor's title, with all its powers and limitations.⁵⁸
[Footnote omitted.]

Professor MacDonald cites as authority for this proposition the first passage quoted from *Crawford and Falconbridge* above. See also Marc-Alexandre Poirier's commentary, and the authorities upon which he relies.⁵⁹

[51] Mr. Poirier, however, has criticized the analysis contained in some of the prior authorities, including *Agricultural Credit* and *Pulsar*, on the basis that they import into the *Bank Act* itself a subordination of a bank's security to prior existing rights. Rather, in his view, the correct view is that the *Bank Act* relies on provincial law to determine what a bank acquires when it takes *Bank Act* security. He states that the *Bank Act*'s general priority scheme is composed of two basic rules:

Rule 1 – Priority disputes between the bank and competing rights acquired *subsequently* to the attachment of the bank's security are to be determined solely by reference to subsection 428(1) of the *Bank Act*. In such cases, the bank's rights must be considered as having priority....

Rule 2 - Priority disputes between the bank and conflicting rights acquired *prior* to the attachment of the bank's security are to be determined by ascertaining the effect of the document of title fiction under provincial law. As previously stated, the *Bank Act*, through the interplay of subsections 427(2) and 435(2), provides that the bank acquires title to the rights of the debtor in the collateral. Nowhere, however, does the *Bank Act* expressly subordinate the bank's security to prior existing rights. Moreover, contrary to certain views expressed in common law jurisdictions, the subordination of a bank's security to prior existing rights cannot be *implied* in the *Bank Act*. To do so would constitute a failure to recognize the complementary relationship between the *Bank Act* and provincial law. The correct view is that the *Bank Act*, having vested the bank with the rights of the debtor in the collateral

⁵⁸ *Ibid.*, p. 5.

⁵⁹ Poirier, *supra* note 10 at pp. 320-22.

through the document of title fiction, relies on provincial law to determine the consequences of holding such rights.⁶⁰

[Emphasis in original; footnotes omitted.]

The point he makes regarding the interaction of s. 428(1), on the one hand, and ss. 427(2) and 435(2), on the other, is an important one.

[52] At bottom, this is an exercise in statutory interpretation, which requires recourse to the general principles of statutory interpretation, including the need to read the words to be interpreted in their entire context.⁶¹ It is clear that the *Bank Act* provides no express priority rule *vis à vis* prior security interests. To read a priority rule into the *Bank Act* in favour of prior interests, and thereby defeat *Bank Act* security in all cases would have far-reaching ramifications. It would raise, for example, the question as to what types of prior interests would have such effect, which was the conundrum faced by the Chambers judge in the approach that he took.

[53] A conclusion that the *Bank Act* relies on provincial law to determine the consequences of holding a warehouse receipt or bill of lading avoids this problem. Such a conclusion is in keeping with the history of the *Bank Act*, and the wording of the sections under consideration. It enhances credit, but not at the expense of prior interests duly taken and valid under the provincial system of secured transactions. It is consistent with s. 428(1), which accords priority to *Bank Act* security over “rights subsequently acquired,” but to make this statement does not import into the section a priority rule in favour of prior rights. If Parliament did not intend to defer to provincial property law

⁶⁰ *Ibid.*

⁶¹ *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27 at para. 21.

principles, there would be no mechanism to resolve this dispute in the *Bank Act*, and in consequence, the courts would be thrust back upon a consideration of the principles of the general law of the province including the common law and equity in any event.

[54] In summary, a bank, by virtue of the document of title fiction, acquires whatever interest the debtor has in the property at the time the bank acquired its interest. This, of course, brings us to the question of what the debtor owned in this case when the Bank acquired its interest under the *Bank Act*, and this, in turn, necessarily takes us to provincial law governing proprietary interests.

VIII. What right or title did the debtor retain after the Credit Union acquired its security interest in the collateral?

[55] The corollary of the question, what did the Bank acquire by virtue of the document of title fiction, depends on an analysis of what interest the Credit Union had already acquired in the debtor's property before the delivery of the security documentation to the Bank.

[56] The General Security Agreement between the Credit Union and Mr. Buist states that he "GRANTS, CHARGES AND RESERVES to the [Credit Union] A SECURITY INTEREST...IN ALL OF THE DEBTOR'S PRESENT AND AFTER-ACQUIRED PROPERTY, including but not limited to: Goods, Inventory, Equipment (all kinds and types), Accounts, Money, Chattel Paper, Intangibles, Documents of Title, Instruments, Securities, Fixtures, and the property described on the Schedules(s) hereto (all of which property, together with the proceeds as hereinafter described, is herein referred to as the

“Collateral”)”.⁶² The Agreement goes on to provide that “[t]he Security Interest granted by the Debtor to the Credit Union secures the performance or payment and satisfaction of any and all obligations, indebtedness and liability of the Debtor to the Credit Union...”.⁶³

[57] According to the *PPSA*, an agreement in these terms creates a security interest in the property with respect to which it is granted. Clause 2(1)(qq)(i) of the *PPSA* defines a security interest as “an interest in personal property that secures payment or performance of an obligation.”⁶⁴ There can be no doubt, based on the terms of the General Security Agreement mentioned above, that Mr. Buist granted to the Credit Union *a security interest* in all his personal property.

[58] The *PPSA* refers to both “attachment” and “perfection.” Since the security interest, in this case, was not registered and therefore not perfected, that leaves for consideration whether it was attached. Section 12(1) of the *PPSA* provides:

12 (1) A security interest attaches when:

- (a) value is given;
- (b) the debtor has rights in the collateral or power to transfer rights in the collateral to a secured party; and
- (c) except for the purpose of enforcing rights between the parties to the security agreement, the security interest becomes enforceable within the meaning of section 10;

unless the parties have specifically agreed to postpone the time of attachment, in which case it attaches at the time specified in the agreement.⁶⁵

⁶² Appeal Book, p. 33a.

⁶³ *Ibid.*

⁶⁴ *PPSA*, *supra* note 1.

⁶⁵ *Ibid.*

Section 10, which is referred to in s. 12, provides that a security interest becomes enforceable when the debtor has signed a security agreement that contains a description of the collateral, including a claim to all present and after-acquired property. In this case, it is common ground that the Credit Union gave value, Mr. Buist had rights in the collateral before the *Bank Act* interest arose, and the requirements of s. 10 were met. Thus, the Credit Union held an attached security interest in the collateral.

[59] The *PPSA* gives full effect to the concept of attachment and to an attached security interest. Contrary to prior law, a failure to register does not affect the validity, or the enforceability, of the interest. For example, priority among competing unperfected security interests is determined by the order of attachment (see s. 35(1)(c)).

[60] As to what is meant by “attachment”, the *PPSA* does not speak in terms of “title”, “property” or “owner”.⁶⁶ Indeed, s. 2 of the *PPSA* purports to set aside such concepts. The following is one of the earliest statements on the *PPSA* in Canada as to the meaning of attachment:

... It is a term of art used in this Act to indicate when the security interest can be said to attach to the collateral and become enforceable against it. While the term is new, the principle enunciated is not. A security interest attaches when there is an agreement, value has been given and the debtor has right in the collateral to which a security interest can attach. It is basically synonymous with the creation of the security interest because it establishes the time when the rights of the debtor in the collateral are restricted and affected by the rights of the secured party.⁶⁷ [Emphasis added.]

⁶⁶ Jacob S. Ziegel and David L. Denomme, *The Ontario Personal Property Security Act Commentary and Analysis*, 2nd ed. (Markham, Ont.: Butterworths, 2000) at pp. 48-49.

⁶⁷ Fred M. Catzman Q.C., et al., *Personal Property Security Law in Ontario* (Toronto, Ont.: Carswell, 1976) at p. 60.

Similarly, Professors Cuming and Wood, referring to the commentary to Article 9 of the Uniform Commercial Code, write:

... A Personal Property Security Act creates a system of law under which the secured party may by agreement obtain real rights in the debtor's property. These real rights come into existence when the security interest attaches, and because they are sanctioned by provincial statute, they should be considered to be of a legal nature.⁶⁸ [Emphasis added.]

In similar terms, the authors of *Personal Property Security Law* write:

The PPSA uses the term "attachment" to describe the creation of the security interest as distinct from the entry into of the security agreement. Until attachment occurs, no security interest exists and the secured party's rights against the debtor are purely personal and contractual. Conversely, once a security interest attaches, the secured party acquires proprietary rights in the collateral.⁶⁹ [Emphasis added.]

Those proprietary rights include the right to take possession or otherwise enforce obligations under the security agreement,⁷⁰ including the right to sell on default.⁷¹ In sum, the Credit Union's interest was an "attached" interest and, therefore, the Credit Union acquired an enforceable proprietary right.

[61] Applying s. 427(2), read in conjunction with s. 435(2), means that the Bank acquired its interest in the collateral subject to the proprietary rights of the Credit Union. By the time the Bank acquired its interest in the property, the Credit Union already had real rights in the collateral through the attachment of its security interest. Thus, on an application of the *Agricultural Credit* framework, priority must be accorded to the Credit Union.

⁶⁸ Cuming and Wood, *supra* note 56 at p. 275.

⁶⁹ Cuming, Walsh and Wood, *supra* note 10 at p. 17.

⁷⁰ Buist General Security Agreement, Appeal Book, p. 35a.

⁷¹ *Ibid.*

[62] Both counsel for the Bank on this appeal, and on behalf of the Royal Bank on the companion appeal, argued valiantly in support of the decision of the learned Chambers judge, by reference to the need for predictability of outcomes, certainty in individual transactions, and efficiency. They also asserted that the Credit Union should not be entitled to benefit from its concealed lien.

[63] While the Banks' counsel are justifiably concerned about a result that will lead to uncertainty in commercial law, this decision does not render the law uncertain. As I have indicated, the academic community has written prolifically on the topic of federal and provincial security interests.⁷² The result in this case is thus one that can be taken to have been anticipated by the lending community. Except for Mr. Crawford's commentary, quoted above, the academic literature demonstrates a remarkable consistency in support of an interpretation of the law that accords priority to the Credit Union's unperfected security interest. For example, while agreeing with the reasonableness of Mr. Crawford's opinions, Professor McLaren, points out how they are nonetheless not appropriate:

Crawford's opinions are, for the most part, reasonable and are based on the fact that s. 427 security purports to give a bank the equivalent of title to the collateral. However, it is submitted that Crawford's position of subordinating unperfected Act interests that are prior in time is inappropriate. To do so would be to ignore the fact that the Act explicitly provides that a failure to register does not invalidate the security interest. Rather, a simpler rule, and one which would do less harm to both statutes, should be invoked. It is submitted that the rule should simply be a first in time rule. If the Act interest is first in time, then the *Bank Act* interest should be subordinated because it can only attach to the residual interest of the debtor in the collateral. If the *Bank Act* interest is first in time, it should take priority for the same reasons. To use any other rule would involve an analysis of the formalities of the security documents, which is what the policy of the Act

⁷² See footnote 10.

attempts to avoid by making form irrelevant.⁷³ [Footnotes omitted; emphasis added.]

In addition to this being the predicted outcome in this case, it is a certain rule.

[64] By contrast, the result arrived at by the Chambers judge, and supported by the Banks in these two appeals, brings its own problems. As counsel for the Credit Union has correctly pointed out, if the system were such that the banks were entitled to insist on the perfection of the prior *PPSA* interest, the following non-exhaustive list of issues will arise:

1. If the provincial security interest is perfected at the same time the bank reserves its s. 427 security interest, must the provincial interest continue to be perfected thereafter?
2. If the bank searches a debtor's name and receives actual notice of a security interest registered by a provincial lender, but the registration is deficient in a manner prescribed by the regulations to the *PPSA*, can the bank still rely on the "objective test" of a "seriously misleading error" provided by the *PPSA* to challenge the registration, even when the bank was not misled?
3. If, in the case at hand, the credit union had registered a security interest in "all farm machinery" but had failed to describe the serial number of a tractor (as required by the regulations to the *PPSA*) would the bank have enjoyed priority to the tractor, but not the remaining machinery?
4. Are all rules of perfection applicable including perfection by possession?
5. Do the *PPSA*'s rules of temporary perfection apply when, for example, goods are moved from one jurisdiction to another?⁷⁴

[65] With respect to the Bank's argument about predictability and certainty of outcomes, admittedly this result can lead to lending uncertainty in individual cases (as opposed to uncertainty as to the result). In part, the problem in this case, and the companion case, may stem from the fact that it was not until 1980 that banks could take *Bank Act* security in agricultural

⁷³ McLaren, *Secured Transactions in Personal Property in Canada*, *supra* note 10 at pp. 5-325/26.

⁷⁴ Appellant's factum, p. 21.

equipment.⁷⁵ This change in the law has widened the possibility of conflict between the banks and the credit unions and provincial government lending agencies.

[66] There are clear incentives for lending institutions to register under the *PPSA*, not the least of which are the consequences of holding an unperfected security interest. By failing to register a security interest, a provincial lending institution stands to be defeated by many more provincial interests than federally created ones. The problem is the age old one of a debtor failing to disclose—either negligently or fraudulently—that it has borrowed money elsewhere. The *PPSA* provides a solution for the banks as well, but only if they take a security interest under that *Act* and not under the *Bank Act* in this jurisdiction, which is a solution that has been adopted elsewhere.⁷⁶

[67] In short, in the within appeal, the Bank cannot insist on registration under a system of which it is not a part and that it has not adopted. The Credit Union is entitled to priority over the Bank of Montreal by virtue of the Credit Union's prior security interest. The priority rule, resting as it does on ss. 427(2) and 435 of the *Bank Act* and provincial law, does not depend on whether the prior security interest is perfected.

⁷⁵ *Banks and Banking Law Revision Act, 1980*, S.C. 1980-81-82-83, c. 40., s. 178(1)(c).

⁷⁶ Jacob S. Ziegel, "PPSA Problems—The Three C's" (1992) 13 C.B.R. (3d) 1 at pp. 4-5 wherein Professor Ziegel indicates that in Ontario the Royal Bank has opted to bypass s. 427 in favour of having all its security interests governed by Ontario law.

IX. CONCLUSION

[68] The appeal is allowed with costs in this Court and in the Court of Queen’s Bench.

DATED at the City of Regina, in the Province of Saskatchewan, this 12th day of March A.D. 2009.

“Jackson J.A.”
Jackson J.A.

I concur _____
“Sherstobitoff J.A.”
Sherstobitoff J.A.

I concur _____
“Smith J.A.”
Smith J.A.

Appendix “A”

Rights and powers vested by delivery of document

427. (2) Delivery of a document giving security on property to a bank under the authority of this section vests in the bank in respect of the property therein described

(a) of which the person giving security is the owner at the time of the delivery of the document, or

(b) of which that person becomes the owner at any time thereafter before the release of the security by the bank, whether or not the property is in existence at the time of the delivery,

the following rights and powers, namely,

(c) if the property is property on which security is given under paragraph (1) ... (n) consisting of agricultural implements ..., the same rights and powers as if the bank had acquired a warehouse receipt or bill of lading in which that property was described, or

(d) if the property

...

(v) is property on which security is given under paragraph (1)(n) consisting of agricultural equipment, or

...

a first and preferential lien and claim thereon for the sum secured and interest thereon, and as regards a crop as well before as after the severance from the soil, harvesting or threshing thereof, and, in addition thereto, the same rights and powers in respect of the property as if the bank had acquired a warehouse receipt or bill of lading in which the property was described, and all rights and powers of the bank subsist notwithstanding that the property is affixed to real property and notwithstanding that the person giving the security is not the owner of that real property,

and all such property in respect of which such rights and powers are vested in the bank under this section is for the purposes of this Act property covered by the security.

...

Priority of bank's claim

428. (1) All the rights and powers of a bank in respect of the property mentioned in or covered by a warehouse receipt or bill of lading acquired and held by the bank, and the rights and powers of the bank in respect of the property covered by a security given to the bank under section 427 that are the same as if the bank had acquired a warehouse receipt or bill of lading in which that property was described, have, subject to subsection 427(4) and subsections (3) to (6) of this section, priority over all rights subsequently acquired in, on or in respect of that property, and also over the claim of any unpaid vendor.

...

Warehouse receipts and bills of lading

435. (1) A bank may acquire and hold any warehouse receipt or bill of lading as security for the payment of any debt incurred in its favour, or as security for any liability incurred by it for any person, in the course of its banking business.

Effect of taking

(2) Any warehouse receipt or bill of lading acquired by a bank under subsection (1) vests in the bank, from the date of the acquisition thereof,

(a) all the right and title to the warehouse receipt or bill of lading and to the goods, wares and merchandise covered thereby of the previous holder or owner thereof; and

(b) all the right and title to the goods, wares and merchandise mentioned therein of the person from whom the goods, wares and merchandise were received or acquired by the bank, if the warehouse receipt or bill of lading is made directly in favour of the bank, instead of to the previous holder or owner of the goods, wares and merchandise.