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Security Interests in Secured Obligations

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4. Conclusion.

If there is a lesson to be learned from MacKay, it is that the Supreme Court of Canada remains unable to come to grips with questions of rights. Assuming that, as a matter of principle, an apparent abrogation of rights can be justified if it is necessary, it is incumbent upon the court to explain what that necessity is. The court’s failure to do so undermines the persuasiveness of the decision. Moreover, it suggests that apparently sophisticated doctrine, such as was offered by McIntyre J., is worth little in the absence of an adequate analysis of the facts.

The weakness in the court’s approach is not primarily a function of the non-entrenched status of the Bill of Rights. It is a function of our legal culture, which traditionally has defined a role for the judiciary subordinate to that of the legislature.58 This role inhibits the court from asking the questions which must be asked when issues of rights are considered. Old habits die hard, and there is little reason to expect that the court will change its orientation dramatically if a Charter of Rights is entrenched.

MARC GOLD*

* * *

SECURITY INTERESTS IN SECURED OBLIGATIONS.—Complex priority questions arise in connection with secured transactions with secured obligations. Additional complications come to the surface where the statute which governs the secured transaction with the obligation does not apply to the interest securing it. This is typical where the collateral under the secured transaction is an obligation secured by a real estate mortgage. All this came up recently in Re Urman,1 a decision given by Steele J. of the Ontario Supreme Court.

The facts of the case were as follows: before his bankruptcy, Urman carried on business as a real estate mortgage broker. The Canadian Imperial Bank of Commerce (“the bank”) which acted as his banker acquired from him a general assignment of accounts with respect to which a financing statement was properly registered under

58 Gold, op. cit., footnote 24, at pp. 348-358.

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1 (1982), 128 D.L.R. 33, (1981), 38 C.B.R. (N.S.) 261 (Ont. S.C. in Bkcy). All internal cites in this comment are from the C.B.R., being the only report of the case, at the time the comment was submitted for publication.
the Ontario Personal Property Security Act.² Apparently, the general assignment related to all existing and future accounts held by Urman. The financing statement was outstanding at the time of Urman’s bankruptcy.

At all material times, the bank was aware that Urman, in the ordinary course of his business, was acquiring real estate mortgages primarily for resale to his clientele. The bank provided a revolving line of credit for this purpose. Repayment to the bank was anticipated to be from Urman’s sale of mortgages, payment on the mortgages themselves, and from profits on the sale of mortgages. The general assignment provided that all monies collected or received by Urman were to be received by him as trustee for the bank and ought to be paid over to the bank.

Urman’s trustee in bankruptcy ("the trustee") applied to the court for advice and direction³ to determine the respective interests and priorities with respect to certain mortgages held or formerly held by Urman. Four test cases were the subject of the decision. The first, third and fourth cases were contests with respect to mortgages that had been assigned by Urman to specific lenders to secure his indebtedness to each of them.⁴ The subject-matter of the second case was a mortgage held by Urman for the benefit of certain "trust claimants", that is, various persons from whom he received money after he had advanced his own money to the mortgagor-borrower.⁵

Some of the competing assignees, but not the bank, registered their respective interests in the appropriate registry or land titles office. None of the competing assignees or "trust claimants" registered a financing statement under the PPSA.

Steele J. held that the PPSA applied to all of Urman’s assignments. Since the bank registered a financing statement in connection with the general assignment, it held a perfected security interest in all

² Presently R.S.O., 1980, c. 375, as am., hereinafter cited as PPSA.
³ Pursuant to s.16 of the Bankruptcy Act, R.S.C., 1970, c. B-3, as am.
⁴ In the third case the contest was between the bank and a sub-assignee of the mortgage. Originally, the bank approved to the assignee a line of credit for the purpose of purchasing mortgages from Urman. The assignee never availed himself of the approval but acquired mortgages from Urman with funds borrowed from another bank (the sub-assignee) to which the mortgages had been then assigned. In the fourth case, subsequent to the assignment of the specific mortgage, Urman specifically assigned to the bank monies owing under that mortgage.
⁵ Each trust claimant’s rights were spelled out in a detailed trust agreement which constitutes Schedule A of the original judgment. In fact Urman syndicated the mortgage among the various "trust claimants". The court found that "[h]e did not receive the money in trust to be advanced on behalf of the trust claimants but received the money after he had advanced his own money...": Urman, supra, footnote 1, at p. 273.
debts owing under the real estate mortgages.\textsuperscript{6} However, "the bank impliedly waived its charge in each case where Urman sold or transferred a mortgage or the debt created thereunder to others".\textsuperscript{7} On their part, having declined to register financing statements, "these other persons failed to perfect their [respective] security interest[s] and therefore became subordinate to the trustee".\textsuperscript{8} The ultimate winners were therefore Urman's unsecured creditors.\textsuperscript{9}

The remainder of this comment will examine the issues presented by \textit{Urman} in the following manner: Part I will discuss the relationship between a debt and collateral and the implications of this relationship with respect to priorities among competing security interests in the debt and the collateral. Part II will examine whether the analysis of Part I fits into the scheme of the PPSA in cases where the obligation which constitutes the collateral is secured by personal property so that both the security interest in the obligation and the interest securing it are governed by that statute. Part III deals with the direct issues dealt with in \textit{Urman}. It will first examine the applicability of the framework so far established to situations where the obligation which constitutes the collateral is secured by a real estate mortgage. Next, it will deal with the treatment of the bank's waiver in \textit{Urman} and the ultimate victory of the unsecured creditors. Part IV will set forth my conclusions which support the substance of Mr. Justice Steel's decision and examine possible legislative solutions to some of the issues raised by \textit{Urman}. It will also examine critically \textit{Bill 163}, recently enacted in Ontario partly in response to \textit{Urman}.\textsuperscript{9a}

\textbf{I}

In \textit{Thornborough v. Baker},\textsuperscript{10} Lord Nottingham stated that "in natural justice and equity the principal right of the mortgagee is to the money, and his right to the land is only as a security for the money".\textsuperscript{11} Therefore, on the mortgagee's death in this case, the debt was considered to constitute part of his personal estate and became payable to his executor. It did not pass together with the mortgagee's lands to his

\textsuperscript{6} Registration of a financing statement perfects a security interest in intangibles under PPSA, s. 25(1)(c). For the nature of the mortgaged debts as "intangible", see text and footnotes 60-61 \textit{infra}.

\textsuperscript{7} \textit{Urman}, supra, footnote 1, at p. 269.

\textsuperscript{8} \textit{Ibid.}, at p. 279.

\textsuperscript{9} Under PPSA, s.22(1)(a)(iii), "...an unperfected security interest is subordinate to ... the interest of a person ... who represents the creditors of the debtor as ... trustee in bankruptcy. ..."

\textsuperscript{9a} \textit{Bill 163}, 1st Sess. 32nd Legisl., 30 Eliz. II, 1981, received Royal Assent on December 11th, 1981.

\textsuperscript{10} (1675), 3 Swan 628, 36 E.R. 1000.

\textsuperscript{11} \textit{Ibid.}, at p. 630.
heir. The heir held the estate in the mortgaged land on trust for the executor until the discharge of the debt.\textsuperscript{12}

The result is that in equity the mortgage follows the debt. He who holds the debt is entitled to the benefit of the mortgage. This emerges from Morley v. Morley.\textsuperscript{13} In this case, the mortgagees assigned the debt secured by the mortgage but reserved the security to themselves. It was held that the assignment transferred the right to sue on the mortgagor's covenant for payment, but that the mortgagees remained "the persons . . . to foreclose".\textsuperscript{14} Nonetheless, money to be obtained by the mortgagees' foreclosure was to be held by them in trust for the assignees. As "the only persons who could enforce the deed", the mortgagees "would be trustees of the money recovered for the [assignees] . . . and liable to account to them".\textsuperscript{15} This means that the benefit of the mortgage passes to the assignee as an incident of the assignment of the debt secured by the mortgage.

According to Falconbridge, "a complete transfer of the mortgage includes an assignment of the debt and a conveyance of the land, but either may be assigned or conveyed separately".\textsuperscript{16} This however should be read subject to the preceding analysis. A separate assignment and conveyance could create a split between the entitlement to sue on the debt and the entitlement to enforce the mortgage. Nonetheless, as explained, enforcement of the mortgage is to be carried for the benefit of the one holding the debt. No split can be created between the right to the debt and the benefit of the mortgage. He who owns the debt ultimately enjoys the benefit of the security.\textsuperscript{17}

This relationship between the debt and security is reflected in Canadian Bank of Commerce v. Yorkshire & Canadian Trust Ltd, a 1938 decision of the Supreme Court of Canada. The case was concerned with the assignment of money due under a contract for the sale of land. The question dealt with was whether an assignment of a debt for the unpaid price necessarily carries with it the interest in the land reserved by the vendor "as a means of compelling payment of the

\textsuperscript{13} (1858), 25 Beav. 253, 53 E.R. 633.
\textsuperscript{14} Ibid., at p. 259.
\textsuperscript{15} Ibid., at p. 258.
\textsuperscript{17} In the language of an American text book, "the security is inseparable from the obligation, and . . . whoever can establish his claim to the obligation gets with it the security interest . . .". G.E. Osborne, G.S. Nelson and D.A. Whitman, Real Estate Finance Law (1979), p. 315 and n. 43, relying on the classic statement of the U.S. Supreme Court in Carpenter v. Longan (1872), 83 U.S. (16 Wall.) 271, 21 L. Ed. 313, according to which "the debt is the principal and the mortgage an accessory".
\textsuperscript{18} [1939] 1 D.L.R. 401 (S.C.C.).
The court gave an affirmative answer: the security and the right to payment "could not in point of law be separated". The former passed to the assignee as an incident of the assignment of the latter.\(^\text{19}\)

*Jones v. Gibbons*\(^\text{20}\) may appear to be inconsistent with this analysis. The case was a contest with respect to a debt between a transferee of the mortgage securing it and a subsequent assignee of the debt. The court held in favour of the former: "he, who has the estate, has in effect the debt . . . [B]y the assignment of the mortgage the debt necessarily passes, as incident to it."\(^\text{21}\) Nonetheless, this proposition should not be taken to reverse the relationship between a debt and the mortgage securing it. The case was concerned with the construction of the document conveying the mortgage. It held in effect that a transfer of the mortgage without an assignment of the debt secured by it is a futile act and that therefore the document had to be read as conveying not only the mortgage but also the debt. The transferee of the mortgage won not because he was a transferee of the mortgage, but because the document he relied on was construed to convey not only the mortgage but also the debt. The transferee of the mortgage won because his right to the debt was prior in time to that of the subsequent assignee. On final account the decision supports the view that the mortgage follows the debt: without his priority with respect to the debt, the transferee of the mortgage could not retain the benefit of the security.

II

Secured transactions with obligations are governed in Ontario by the PPSA.\(^\text{22}\) Under this statute, a writing or group of writings which evidences both a monetary obligation and a security interest in specific goods is "chattel paper".\(^\text{23}\) Other obligations constitute "intangible".\(^\text{24}\) Monetary obligations incurred in favour of a trader and in the ordinary course of his business, are "book debts".\(^\text{25}\) Where

\(^\text{19}\) Ibid., at pp. 405-406, per Davis J. See also at pp. 406-407 per Kerwin J; and at pp. 408-409 per Hudson J. The result was that "in accepting the assignment of the moneys due . . . the bank . . . lent money . . . upon the security of lands", in violation of the then in force s.75(2)(c) of the Bank Act, 1934 (Can.). Ibid., at pp. 406-407 per Kerwin J.

\(^\text{20}\) (1804), 9 Ves. 407, 32 E.R. 659.


\(^\text{22}\) The PPSA applies to all secured transactions with personal property: ss 2(a), 1(y), and 1(m).

\(^\text{23}\) Ibid., s.1(c).

\(^\text{24}\) Ibid., s.1(m)

\(^\text{25}\) Provided "in the ordinary course of [the trader's] business [they] would be entered in his books". The term is not defined in the PPSA. Its definition comes from
they are evidenced by a writing or group of writings which evidences also a security interest in specific goods, book debts are part of "chattel paper". Otherwise they are "intangible[s]". The PPSA applies not only to the assignment of book debts intended as security, but also to their outright sale.26

The characterization of "chattel paper" as a category of "collateral",27 covering a monetary obligation as well as the security interest in the goods securing it, requires some explanation. In fact, it is only the obligation which constitutes the collateral. The security interest in the goods is incidental to the right to enforce the obligation, and as such, benefits the party with a security interest in the "chattel paper".28 This can be demonstrated by considering the position of an assignee with a perfected security interest in goods as compared to that of a party with a perfected security interest in the obligation secured by these goods.

An assignee of an unperfected security interest may register "a financing statement . . . in which [he] is shown as the secured party".29 An assignee of a perfected security interest may file a financing change statement.30 Registration under section 48(2) is for the purpose of perfecting a security interest in the goods.31 Registration under section 48(1) has nothing to do with perfection: an assignee of a security interest succeeds to the assignor's position "so far as . . . perfection is concerned".32 The effect of registration under section 48(1) is to make the assignee "the secured party of record".33

Inquiries concerning the transaction, authorized under section 20, 26 PPSA, s.2(b).
27 "Collateral" is "property that is subject to a security interest": PPSA, s.1(d).
28 Indeed, even without a direct provision, the PPSA must be read to provide that the security interest in the goods passes to the assignee by an outright assignment of book debts secured by these goods. The doubts of the B.C. Law Reform Commission on this point are not justified. See its report on Debtor-Creditor Relationships (Project No. 2) Part V—Personal Property Security (1975), p. 26.
29 S. 48(2). An assignee may also take advantage of s. 47(2) and where the collateral is goods to be held for sale or lease he may register a financing statement before a security agreement is signed: West Bay Sales Ltd v. Hitachi Sales Corp. of Canada Ltd (1979), 28 C.B.R. (N.S.) 244 (Ont. S.C. in Bkcy), and Ziegel, (1979), 3 Can. Bus. L.J. 222, at p. 233. Stated otherwise, a financing statement may be registered by the assignee before the attachment of the assignor's security interest.
30 PPSA, s. 48(1).
31 PPSA, s. 47(1).
32 PPSA, s. 23(2).
33 PPSA, s. 48(3).
would be addressed to him. He will be entitled to file subsequent financing change statements in connection with the security interest.34

The assignee’s security interest in the goods is, however, not a security interest in the secured obligation. Perfection of the former does not secure perfection of the latter. Perfection of the security interest in the secured obligation is obtained by perfecting a security interest in the chattel paper containing the obligation. All this is demonstrated by the example given in comment 7 to article 9-302 of the Uniform Commercial Code:

Buyer buys goods from Seller who retains a security interest in them which he perfects. Seller assigns the perfected security interest to X. The Security interest, in X’s hands and without further steps on his part, continues perfected against Buyer’s transferees and creditors. If, however, the assignment from Seller to X was itself intended for security [or was an assignment of book debts not intended as security], X must take whatever steps may be required for perfection in order to be protected against Seller’s transferees and creditors.

This example presupposes that the assignment of Seller’s security interest in the goods carries with it the right to enforce Buyer’s obligation,35 so as to give X a security interest in the chattel paper.36 If X does not take additional steps to perfect his security interest in the chattel paper, he ends up with a perfected security interest in the goods and an unperfected security interest in the chattel paper. On Buyer’s default, he will be protected against Buyer’s judgment creditors levying on the goods. At the same time, on Seller’s default, his unperfected security interest in the chattel paper will be subordinate to the interest of Seller’s judgment creditors levying on the chattel paper without knowledge of X’s unperfected security interest.37

Indeed, a perfected security interest in the goods does not protect its assignee against Seller’s transferees and creditors. Protection against them depends on priority with respect to the chattel paper. This is illustrated by adding the following facts to the previous example.

Suppose Seller, after his assignment to X, assigns the chattel paper to Y who perfects a security interest in it.38 On Seller’s default, X’s interest in the chattel paper is subordinate to Y’s security

34 Cf. Comment to ss 9-405 of the American Uniform Commercial Code, herein-after cited UCC.
35 In the manner considered in the last paragraph of Part I, supra.
36 Which is the collateral in the UCC example. See PPSA, s. 1(c).
37 PPSA, s. 22(1)(a)(ii).
interest. On Buyer's default and as between X and Y, who has priority with respect to the goods? X claims to hold a perfected security interest in the goods on the basis of registration either by the assignor or by himself. Y has not registered any financing statement with respect to his interest in the goods. On Buyer's default, will X come ahead of Y on the basis of the perfected security interest in the goods?

Neither the UCC nor the PPSA contains provisions directly dealing with this issue. General principles suggest a negative answer. On Buyer's default the perfected security interest in the goods will not put X ahead of Y. Regardless of registration, a security interest in the goods can benefit only the one entitled to enforce the secured obligation. Where both Seller's assignments, to X and Y, were intended as security, Y who on Seller's default comes ahead of X with respect to the chattel paper, may enforce his security interest in the chattel paper and proceed to collect payments from Buyer. Then, on Buyer's default, having already enforced his security interest in the chattel paper, Y may enforce the security interest in the goods.

Where both Seller's assignments to X and Y were outright assignments of books debts, Seller's default is not a condition precedent to an assignee's rights to proceed against Buyer. Nonetheless, as between X and Y, the right to obtain payment from Buyer is vested in Y, who under the PPSA comes ahead of X with respect to the chattel paper. The result is that on Buyer's default, as between X and him, Y is the one entitled to enforce the security interest in the goods, as well as to benefit from its perfected status as against Buyer's creditors and transferees.

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39 Perfection by Y could be accomplished either by taking possession (s. 24(a)) or by registration (s. 25(a)). X neither took possession nor registered a financing statement with respect to his interest in the chattel paper.

40 PPSA, s. 23(2).

41 PPSA, s. 48(2).

42 See: Part I. supra.

43 The alternative is that as between two outright assignees the priority with respect to the assigned debt is to be determined by non-PPSA rules, namely by the rule of Dearle v. Hall (1828), 3 Russ. 1, 38 E.R. 475 (priority according to the order of notices to the account debtor). This does not sound plausible. While normally, the benefit of the PPSA priority scheme is given to a secured party only where his debtor is in default, the application of the PPSA to the outright assignment of book debts (s. 2(b)) must mean that the outright assignee may benefit from the PPSA priority scheme in the absence of the assignor's default.

44 But see V. Countryman, A.L. Kaufman and Z.B. Wiseman, Commercial Law (2nd ed., 1982), pp. 148-9. I understand their argument to suggest that X and Y compete over the goods as two creditors of Buyer. X's perfected security interest in the goods thus puts him ahead of Y with respect to them. I disagree. Neither X nor Y is Buyer's creditor in his own right. Both are transferees from Seller. He who prevails with respect
All this is consistent with the theme of Part I, namely that the security follows the debt. Entitlement to the benefit of the security interest in the goods is determined according to the priority with respect to the right to enforce the secured obligation. Indeed, "the debt is the principal and the [security] an accessory". 45

III

I will now examine the direct issues dealt with in Urman. 45a I will first examine the applicability of the framework so far established to situations where the obligation which constitutes the collateral is secured by a real estate mortgage. In this context I will consider the experience under the UCC as well as the interaction between real estate law and the PPSA priority scheme. Finally I will deal with the treatment of the bank's waiver in Urman and the ultimate victory of Urman's unsecured creditors.

UCC 9-102(3) provides that "[t]he application of... Article[9] to a security interest in a secured obligation is not affected by the fact that the obligation is itself secured by a transaction or interest to which this Article does not apply". The subsection is illustrated in comment 4 as follows:

The owner of Blackacre borrows $10,000 from his neighbor, and secures his note by a mortgage on Blackacre. This Article is not applicable to the creation of the real estate mortgage. Nor is it applicable to a sale of the note by the mortgagor, even though the mortgage continues to secure the note. However, when the mortgagor pledges the note to secure his own obligation to X, this Article applies to the security interest thus created, which is a security interest in an instrument even though the instrument is secured by a real estate mortgage. This Article leaves to other law the question of the effect on rights under the mortgage [,,] of delivery or non-delivery of the mortgage [,,] or of recording or non-recording of an assignment of the mortgagor's interest. . . .

Originally, comment 4 stated that article 9 applied "to the security interest . . . in the note and the mortgage". 46 This language was modified, and the comment presently states that article 9 applies to the security interest in the instrument, "even though the instrument is secured by a real estate mortgage" (see the second sentence from the
end of the quotation). The modification was a response to a fear raised among real estate mortgage financers that the original language meant that the mortgage or the mortgage-note package was a "general intangible".\(^47\) A security interest in general intangibles is perfected by registration. A security interest in instruments is perfected by possession.\(^48\) The practice among United States real estate mortgagors is to take mortgagors' promissory notes in connection with mortgage indebtedness. The revision of the comment was thus designed to reaffirm the efficacy of perfecting security interests in such promissory notes by taking possession rather than by registration.

Nonetheless, two American cases seized on the modification in the language of comment 4 and held that article 9 does not apply to security interests in real estate mortgages. Where a promissory note and mortgage together become the subject of a security interest, only that portion of the package unrelated to the real property "is now covered by Section 9-102".\(^49\) One case, *In re Bristol Associates, Inc.*\(^50\) was concerned with the applicability of article 9 to a security interest in a real estate lease. The other, *Rucker v. State Exchange Bank*\(^51\) dealt with the position of the mortgage assignee vis-à-vis the mortgagor and his transferees and creditors. None of them was faced with competing priorities with respect to a real estate mortgage, or with the assignee's position vis-à-vis the mortgagee's transferees and creditors. Nor did these courts have anything to say on the split priorities with respect to the note and the mortgage resulting from their decisions. Their authority is strongly undermined by their failure to consider the relationship between the right to enforce the note and the right to enforce the mortgage, namely the relationship between the debt and the mortgage securing it.\(^52\)

Indeed, faced with competing priorities with respect to mortgages and notes, or with the assignee's position vis-à-vis the mortgagee's creditors, one American court went the other way. Thus, in *In

\(^{47}\) See in general, Coogan, Kripke and Weiss, The Outer Fringes of Article 9: Subordination Agreements, Security Interests in Money and Deposits, Negative Pledge Clauses, and Participation Agreements (1966), 79 Harv. L. Rev. 229, at pp. 270-271.

\(^{48}\) UCC §§9-302 and 9-305, corresponding to PPSA ss 25 and 24. All UCC cites are from the 1972 official text.


\(^{50}\) *Ibid.*

\(^{51}\) *Ibid.*

\(^{52}\) The cases are criticized by Shaw, *op. cit.*, footnote 46, at p. 1422. See also Bowman, 'Real Estate Interests as Security Under the UCC: The Scope of Article Nine' (1980), 12 U.C.C.L.J. 99, at p. 132 (in conjunction with pp. 120-121).
The court was concerned with priorities with respect to real estate mortgages and notes secured by them. The contest was between an assignee of the mortgagee claiming a security interest in the mortgages and the notes and the mortgagee’s trustee in bankruptcy. The court concluded that the collateral was an “instrument”, and held for the trustee in bankruptcy since the secured party, not being in possession of the notes, had failed to perfect his security interest. Registration of the assignments of the mortgages in local real property records was of no avail to the secured party.

The Ontario PPSA does not have a provision modelled on UCC 9-102(3). Nonetheless, it is submitted that the provision as construed in Staff Mortgage is good law in the province. This construction is consistent with general principles governing the relationship between debt and mortgage. As will be demonstrated below, it produces a coherent approach to the determination of priorities.

I will now examine the reasoning given in Urman to the application of the PPSA to the competing rights with respect to Urman’s mortgages. Relying on Falconbridge,

It has long been settled that a real estate mortgage security is personal property as well as usually being a conveyance of the title to the land. The mortgage transaction normally includes both an acknowledgement of debt and a conveyance of the land as security and either may be assigned or conveyed separately.

He then considered legislative history, and concluded that “the P.P.S.A. should be read to embrace all personal property in its widest sense”. “Intangible” under section 1(m) is “all personal property, including those in action” which does not fall within a specific class of collateral (namely goods, chattel paper, documents of title, instru-

53 (1977), 550 F. (2d) 1228 (U.S. C.A. 9th Cir.).
54 Under UCC 9-301(1)(b), as well as under PPSA, s. 22(1)(a)(iii), an unperfected security interest is subordinate to the interest of the debtor’s trustee in bankruptcy.
55 Other American cases which are in line with the principal holding of In re Staff Mortgage are cited by Shaw, op. cit., footnote 46, at p. 1421.
56 At the same time there is no parallel in the PPSA to UCC 9-104(j): “This Article does not apply . . . to the creation or transfer of an interest in . . . real estate . . .”. The provision was held to be subject to s. 9-102(3) (quoted at the beginning of Part III, supra): Groves v. United States (1978), 202 Ct. Cl. 660, at p. 675. See Shaw, op. cit., footnote 46, at p. 1421.
57 See supra, footnote 53.
59 Urman, supra, footnote 1, at p. 265.
60 Ibid, at 267. In this direction see also C.T.L. Uniforms Ltd v. ACIM Industries Ltd (1981), 33 O.R. (2d) 139 (H.C.) where Krever J. held (at pp. 146-147) that a leasehold in land is “intangible” under the PPSA. Real estate leases are explicitly excluded from the coverage of Article 9: UCC 9-104(j). They were later excluded from the scope of the PPSA by Bill 163.
ments or securities). Accordingly, Urman's mortgages fell within the ambit of "intangible".

Insofar as Mr. Justice Steele appears to suggest the possibility of splitting between the debt and the benefit of the mortgage, his analysis should be rejected. Nonetheless, his ultimate conclusion was that the mortgage followed the debt, and that priority with respect to the debt conferred on the prevailing party also the benefit or the mortgage. This indeed is in line with Staff Mortgage. It is further consistent with the theme of this comment.

I will now discuss the question of competing priorities with respect to mortgages and the debts secured by them. I will deal with the interaction between real estate law and the PPSA priority scheme first in general, and second as applied to Urman.

It is submitted that the principles determining priorities among competing interests in connection with obligations secured by personal property, discussed in Part II of this comment, suggest a framework governing the determination of priorities with respect to obligations secured by real property. Such a framework was in fact applied in Staff Mortgage as well as in Urman. Thereunder, the position of the mortgagee's assignee as against the mortgagor's creditors and transferees is determined according to the mortgagee's priority with respect to the land. The mortgagee's priority, as well as the mortgagee's remedies are governed by real estate law. But whether a particular assignee succeeds to the mortgagee's position is another matter, not governed by real estate law. To the extent that a particular assignment is governed by the PPSA, namely where it is an assignment intended as security or an outright sale of book debts, whether the assignee claiming under it succeeds to the mortgagee's position, or in other words, the question of the assignee's position as against the mortgagee's creditors and transferees, depends on a timely perfection of the security interest in the secured debt. It is therefore determined under the PPSA.

61 Normally, promissory notes are not used in Canada in connection with mortgage indebtedness. Consistently with this practice, such instruments were not used in connection with Urman's mortgages. For the contrary U.S. practice, see text which follows footnote 48, supra. The difference between the U.S. and the Canadian practice was noted by Britton, Assignment of Mortgages Securing Negotiable Notes (1916), 10 Ill. L. Rev. 337, at p. 338 and n. 8.

62 See footnote 59 and text, supra.

63 See Part I, supra.

64 See text and footnotes 53-55, supra.

65 Ibid.

66 See in general, first paragraph of Part II, supra.
I will now consider the application of this analysis to land governed by the Land Titles Act.67 Under section 93(3) of this act, the registration of a real estate mortgage "confers upon the chargee a charge upon the interest of the chargor . . . free from any unregistered interests in the land". A registered charge is "a security upon the land . . . to the extent of the money . . . actually advanced . . ." and certain future advances.68 Its priority ranks ahead of all interests subsequently registered.69 This priority is, however, only as against the mortgagor's transferees and creditors. Where the mortgagee borrows money and as for his indebtedness assigns the mortgage, the assignee's position as against the mortgagee's transferees and creditors is governed by the PPSA. This stems from the applicability of the PPSA to the security interest in the secured debt and the relationship between that debt and the mortgage securing it. It is further supported by section 69 of the PPSA which provides that in a case of a conflict between the PPSA "and a provision of any general or special Act, other than the Consumer Protection Act" the PPSA prevails. As was in fact suggested by Steele J. in Urman,70 section 100(3) of the Land Titles Act which provides for the effect of registration of a transfer of a charge in the land titles office71 is thus superseded by the PPSA.

Registration of an assignment under the Land Titles Act is nonetheless not meaningless. For example, certain powers, including the power to enforce a charge, are in the hands of one whose interest is registered under the Land Titles Act.72 Unless superseded by the PPSA, this could cause a split between the entitlement to foreclose, determined under the Land Titles Act, and the entitlement to the benefit of the foreclosure, determined under the PPSA according to the entitlement to the debt. Such a split has always existed where a mortgage purported to convey the land separately from the assignment of the debt.73

68 Ibid., s. 93(4).
69 Ibid., s. 81(5).
70 Urman, supra, footnote 1, at pp. 267-268. Steele J. did not mention specifically s. 100(3) of the Land Titles Act, ibid.
71 Under s. 100(3), ibid.: "The transfer [of a charge], when registered confers upon the transferee the ownership of the charge free from any unregistered interests therein, and the transfer of part of the sum secured by a charge confers upon the transferee the ownership of such part free from any unregistered interests therein."
72 See e.g., ss 96 (entry by owner of charge), 97 (foreclosure by owner of charge), 98 (remedy of owner of charge with power of sale) and 99 (dealings with registered charge), ibid.
73 See footnotes 13-17 and text, supra.
This analysis is explained by the following example. Owner of Whiteacre, to which the Land Titles Act applies, borrowed money from Lender. As security for his obligation, Owner mortgaged Whiteacre. The charge was properly registered under the Land Titles Act. Lender borrowed money from Assignee and assigned to him the mortgage as security for his indebtedness. Assignee registered a financing statement under the PPSA. Subsequently, Owner mortgaged Whiteacre to Financer as security for another loan and Lender assigned the first mortgage and Owner’s debt secured by it, to Broker. Financer and Broker respectively registered only under the Land Titles Act. Both Owner and Lender defaulted. Lender comes ahead of Financer with respect to Whiteacre. Assignee prevails over Broker not only as to Owner’s debt secured by Whiteacre, but also as to Whiteacre itself. While Broker, the registered transferee of the charge on Whiteacre might hold the power to enforce the mortgage, this power ought to be exercised solely for Assignee’s benefit. Obviously, foreclosure or the enforcement of the mortgage in Whiteacre is governed by real estate law.

The report of Urman does not state explicitly whether the general assignment from Urman to the bank was intended as security or whether it was an outright sale of Urman’s accounts. Nonetheless, Steele J. spoke of “the bank loan”. Likewise he stated that the general assignment in Urman was “similar” to the one dealt with in In Re Wiarton Lumber Company Ltd. In that case the general assignment was intended as security so we can safely assume that this was the case in Urman. But even if this is an erroneous assumption, Urman’s general assignment to the bank was an outright sale of book debts. Either way, the assignment, governed by the PPSA, conferred upon the assignee-bank priority as against competing unperfected or subsequently registered security interests governed by

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Footnotes:

74 S. 81(5) of the Land Titles Act, supra, footnote 67.
75 For a contrary view see Shaw, op. cit., footnote 46, at p. 1429 and n. 85-87: “[where] both the mortgagee and mortgagor default, the failure of the mortgagee’s [assignee] to record...[the] assignment...could well impair his ability to foreclose on the real property or to withstand a challenge by the mortgagor’s trustee in bankruptcy”. I disagree. See text and notes 62-75.
76 See text and note 61, supra.
77 Urman, supra, at p. 269. See also at p. 268.
78 Ibid., at p. 270.
80 Ibid., at 478.
81 See footnote 84, infra. Nonetheless, Steele J. erred in holding (Urman, supra, footnote 1, at p. 268) that In Re Wiarton Lumber Company Ltd, supra, footnote 79, is an authority to the application of the old book debts legislation to a similar situation. That case dealt with the assignment of debts and choses in action under the federal Bank Act.
the PPSA, as well as against subsequent buyers.\textsuperscript{82} Apparently, all of Urman’s competing assignments, as well as the interest given by him to the “trust claimants” were intended as security.\textsuperscript{83} Since the debts assigned to the competing claimants arose in Urman’s course of business as a mortgage broker, they seem to constitute “book debts”,\textsuperscript{84} and thus even if any assignment was an outright sale, it gave rise to a “security interest”\textsuperscript{85} and was governed by the PPSA.\textsuperscript{86} In the priority contest between the bank and the competing claimants, the former, having a perfected security interest in the secured debts, appeared to win as against the latter who held unperfected security interests in the same collateral. Registration of their respective interests in a registry or land titles office by some competing claimants was of no avail. None of the contests was concerned with rights to the land as against the mortgagor. Rather they were all priority contests among transferees and creditors of the mortgagee, with respect to the secured debts for which the mortgages were accessories.

Nonetheless, at the end of the day the bank was unable to take advantage of its priority and for a good reason. As Steele J. concluded, “the entire purpose of the bank loan . . . was to permit Urman to carry on his business in the normal course”.\textsuperscript{87} The mortgages in Urman’s hands were his “stock-in-trade”\textsuperscript{88} and “the bank never intended, nor did Urman intend, that the general assignment would hamper Urman from dealing with the mortgages and debts thereunder in the normal course of his business”.\textsuperscript{89} The bank rather gave Urman “the implied authority” to sell and deal with the mortgages.\textsuperscript{90} Accordingly, “once [a] mortgage was dealt with or assigned by [Urman], it was freed from the [bank’s] specific charge”.\textsuperscript{91} There-

\textsuperscript{82} See in general ss 9, 22(1)(b) and 35(1). Cf. Bowman, op. cit., footnote 42, at pp. 134-135. For the limits of this priority, see text and footnotes 81-94, infra.

\textsuperscript{83} See in general footnotes 4-5 and text, supra. Note however that Steele J. regarded the “trust agreements” as “trust receipts” falling under s. 2(a)(i) of the PPSA: \textit{Urman}, supra, footnote 1, at p. 274. However, “trust receipts” denotes a mechanism for inventory financing, used in the U.S. more than in Canada, which has nothing to do with the fact situation in \textit{Urman}. In general for the U.S. trust receipt, see \textit{e.g.}: G. Gilmore, Security Interests in Personal Property (1965), Vol. 1, ch. 4.

\textsuperscript{84} For the definition of “book debts” see footnote 25 and text, supra. For the comprehensiveness of the term and its applicability to debts created by the sale of intangibles in the ordinary course of trade of a seller of such intangibles, see \textit{e.g.}, \textit{Shipley v. Marshall}, supra, footnote 25, at p. 569 (E.R.).

\textsuperscript{85} PPSA, s. 1(y).

\textsuperscript{86} PPSA, s. 2(b).

\textsuperscript{87} \textit{Urman}, supra, footnote 1, at p. 269.

\textsuperscript{88} \textit{Ibid.}, at p. 270.

\textsuperscript{89} \textit{Ibid.}, at p. 269.

\textsuperscript{90} \textit{Ibid.}, at p. 271, see also at p. 275.

\textsuperscript{91} \textit{Ibid.}, at p. 271.
fore, notwithstanding the perfection of its security interest, the bank did not come ahead of the competing claimants.

In fact Steele J. found in favour of the competing claimants by treating them as purchasers in the ordinary course of their vendor's business. In Ontario, rights of an ordinary course buyer are protected under section 2(1) of the Factors Act,92 as well as under section 30(1) of the PPSA. Both provisions are limited to buyers of goods; they do not protect a purchaser of debts secured by real estate mortgages. Nonetheless, this aspect of the analysis of Steele J., dealing with the protection of the competing claimants as against the bank, is entirely correct and sound. The PPSA explicitly provides that dealing with the collateral by the debtor in a manner "expressly or impliedly authorized" by the secured party puts an end to the latter's security interest.93 The extinction of the perfected security interest in favour of any ordinary course buyer is in fact a specific situation falling also within the general rule of section 27(1)(a). A purchaser of a secured debt in an authorized dealing94 is definitely protected under the latter.

The competing claimants' victory over the bank turned out to be a phryric victory. To the extent that Urman's assignments and "trust" obligations created security interests in his secured debts,95 perfection by registration was required to protect these interests from Urman's trustee in bankruptcy.96 Having failed to register financing statements, the competing claimants lost the benefit of their security interests. Their failure was of no avail to the bank: "Once the bank waived its rights they cannot be revived . . . merely because other persons have not taken proper action to protect themselves."97 The ultimate winners were Urman's unsecured creditors.98

On its facts Urman was correctly decided. None of the secured parties acted properly to protect their respective positions. The bank had the advantage of having a PPSA financing statement in connection with Urman's mortgages. Nonetheless, it failed to anticipate the

92 R.S.O., 1980, c. 150.
93 S. 27(1)(a). Regrettably, "apparent" authority is not mentioned. Cf. UCC 9-306(2): "A security interest continues in collateral notwithstanding . . . disposition . . . unless the disposition was authorized by the secured party in the security agreement or otherwise." (emphasis added).
94 In any event note that an authorized dealing under s. 27(1) differs from the transfer "with consent" under s. 49(1). The former contemplates the waiver of the security interest by the secured party, typically in inventory or stock in trade. The latter contemplates the retention of the security interest by the secured party.
95 See in general text and footnotes 77-82, supra.
96 PPSA, ss 25(1)(c) and 22(1)(a)(iii).
97 Urman, supra, footnote 1, at p. 279.
98 See footnotes 8-9 and text, supra.
issue raised by the authority given to Urman to deal with the mortgages. The bank was supposed to look only to the proceeds arising from the assignments of Urman’s mortgages.\textsuperscript{99} Probably it failed to perfect a security interest with respect to them as required by section 27(2).\textsuperscript{100} The competing claimants appeared to be entirely unaware of the applicability of the PPSA to their dealings. They thus failed to take steps designed to perfect their respective security interests under the PPSA. Accordingly, the mortgages and the debts secured thereby fell into the hands of Urman’s trustee in bankruptcy.

IV

Urman held that the PPSA applies to the assignment of real estate mortgages, and that priorities with respect to such mortgages are determined according to the PPSA. The decision did not please the real estate bar. Nonetheless, as explained in this comment, the case was correctly decided as a matter of general principles of law as well as of statutory interpretation.

Whether the decision reflects a desirable state of law is obviously an entirely different question. From this viewpoint, the real issue is not the applicability of the PPSA as a matter of general principles and statutory provisions, but rather the desirability of applying the “floating lien” concept into real estate mortgage financing. The question is whether we are interested, on policy grounds, in the creation of a security interest in a mortgage portfolio, in the same way that an effective security interest in changing inventory of goods can presently be created. Stated otherwise, the question is whether we want a mechanism which will enable a mortgage dealer to be financed like a car dealer, as well as enabling a small mortgage lender to obtain funds from a larger lending institution on the security of his mortgage portfolio.\textsuperscript{101}

If such a financing tool is desired, then the PPSA serves as a useful vehicle to accomplish it. In this respect, to enhance its effectiveness, it requires only relatively minor or cosmetic changes. Thus for example, the Act should be amended so as to avoid the split between the right to foreclose and the entitlement to the benefit of a

\textsuperscript{99} PPSA, s. 27(1)(b).

\textsuperscript{100} Urman, supra, footnote 1, at p. 271.

\textsuperscript{101} Cf. the practice of “mortgage warehousing”, widely spread in the U.S. Under this practice: “[T]hrift institutions, including savings and loan associations, saving banks, and credit unions, pledge mortgages and notes of their homeowner borrowers to a commercial bank or mortgage banker as security for their own borrowings. The bank takes delivery of the paper and “warehouses” it until the institution has accumulated a block of mortgages large enough to sell.” Shaw, op. cit., footnote 46, at p. 1415.
mortgage. This may be achieved by explicitly providing in the PPSA that where the collateral is a secured debt, the entitlement to the benefit of a charge securing it is followed by an entitlement to exercise all remedies and privileges in connection with this charge. Another amendment could require that where a general assignment purports to cover debts secured by real estate mortgages, this fact must be noted in the financing statement. The PPSA should also be amended to apply explicitly the section 30(1) ordinary course buyer exception to a buyer of intangibles from one who deals with them in the ordinary course of his business.

Such amendments would undoubtedly improve the operation of the PPSA in relation to security interests in mortgage portfolios. It is nonetheless obvious, that even without them, the PPSA accommodates the "floating lien" concept much better than the Registry Act or the Land Titles Act, where the concept does not fit in at all.

The position of an assignee of a specific real estate mortgage will now be considered. Should he be required to register a PPSA financing statement? Such registration does not enhance the effectiveness of a security interest in a mortgage portfolio. One thing is to say that unless an assignee of a specific real estate mortgage qualifies as an ordinary course purchaser or that the disposition to him is authorized, his interest is subordinate to a security interest in the assignor’s mortgage portfolio, with respect to which a PPSA financing statement was previously registered. Another thing is to say that unless an assignee of a specific real estate mortgage registers a PPSA financing statement his interest will be defeated by the assignor’s trustee in bankruptcy notwithstanding the assignee’s compliance with registration requirements under real estate law. Policy grounds which may justify the former, do not extend to the latter. No useful purpose appears to be served by double registration by an assignee of a specific real estate mortgage. Yet such double registration was required from the competing claimants in Urman. A PPSA financing statement was required for protection from Urman’s trustee in bankruptcy. Real estate registration was still useful for the purpose of rights under real

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102 For the split between the benefit of the mortgage and certain powers and privileges with respect to them, see footnote 72 and text, supra.
103 Cf. PPSA, s. 10(b) requiring land identification in fixture financing and Regulation 3 under the PPSA, O. Reg. 879/75 as amended by O. Reg. 547/79 requiring to set out in a financing statement the classification of the collateral and its description in a case of a motor vehicle classified as consumer goods.
104 Cf. text and footnotes 92-94, supra.
106 Supra, footnote 67.
estate law.\textsuperscript{107} Saying that \textit{Urman} was correctly decided on this point does not mean that it reflects desirable policies.

Needless to say, merely excluding the interest of an assignee of a specific real estate mortgage from the coverage of the PPSA will not serve as a comprehensive solution. An amending statute must provide for the priorities between a security interest in a mortgage portfolio and the interest of an assignee of a specific real estate mortgage. A sound legislative solution should be consistent with the PPSA priority scheme as well as with the policy of avoiding superfluous registrations. Such a solution should provide that for the purpose of the PPSA priority scheme the effect of registering a specific mortgage assignment in a proper land registry office is the same as the registration of a PPSA financing statement with respect to the debt secured by it. Such a provision will not undermine the effectiveness of a security interest in a mortgage portfolio. Registration of a PPSA financing statement in connection with this portfolio will put the secured party ahead of the interest acquired by a subsequently recorded unauthorized real estate mortgage assignment. At the same time, registration of the assignment under the proper real estate statute will put the assignee ahead of a subsequently registered PPSA security interest\textsuperscript{108} as well as the assignor's trustee in bankruptcy.

All this presupposes the desirability of a "floating lien" in connection with real estate mortgages. But if such a mechanism is considered to be undesirable, the best legislative solution is to exclude explicitly all assignments of debts secured by real estate mortgages from the coverage of the PPSA. An assignment of a mortgage will be construed to include an assignment of the debt secured by it.\textsuperscript{109} Priority as to the debt will be determined according to the priority as to the mortgage.

Unfortunately, Bill 163, "An Act to amend the Personal Property Security Act", recently enacted\textsuperscript{10} inter alia in response to \textit{Urman}, neither improves the "floating lien" mechanism, nor excludes altogether real estate mortgage financing from the coverage of the PPSA. It rather introduces confusion and uncertainty into what appears to me a clear, though not always defensible, state of law.

\textsuperscript{107} See text and footnotes 72-73, supra.

\textsuperscript{108} Obviously, where a promissory note is given for a mortgage obligation, no registration of the mortgage assignment whether under the PPSA or in a land registry office, can secure priority to the assignee. See PPSA, s. 31(1)(a), preserving rights of a holder in due course. Assignee's priority against a holder in due course of the note can be provided only by an amending statute. For the use of promissory notes in real estate mortgages financing see footnote 61, supra.

\textsuperscript{109} Cf. last paragraph of introduction, supra.

\textsuperscript{110} See footnote 9a, supra.
Bill 163 contains three provisions applying to security interests in debts secured by real estate mortgages:

1. An amended section 3(1) of the PPSA provides *inter alia* that the assignment of a real estate mortgage is excluded from the coverage of the PPSA. Nonetheless, the PPSA applies to "an assignment of a right to payment under a mortgage ... where the assignment does not convey or transfer the assignor's interest in the real property" (new section 3(1)(e)(ii)).

2. As new section 54(1)(b) provides for the registration of a notice in the proper registry office where "the security interest is ... in right to payment under a mortgage ... of real property to which [the PPSA] applies".

3. Under a new section 36a(2):

A security interest in a right to payment under a mortgage ... of real property, to which (the PPSA) applies, is subordinate to the interest of a person who acquires the mortgagee's ... interest in the mortgage ... if the interest of the person is registered in the proper land registry office before a notice of the security interest is registered in the proper land registry office.

The form of the notice under section 54(1)(b) will be prescribed by regulations. To the extent that such notice will have to identify the land concerned, Bill 163 rejects the "floating lien" concept in connection with real estate mortgages. At the same time, as explained below, the PPSA is not rendered altogether irrelevant in determining priorities in connection with real estate mortgage financing.

Read alone, new section 3(1)(e)(ii) seems to raise the possibility of a split priority between a debt and the right to a real estate mortgage securing it.\(^{111}\) Yet, read in conjunction with new section 36a(2), new section 3(1)(e)(ii) makes more sense. The combined effect of the two provisions is that the registration of a specific assignment in the proper land registry office will put the assignee ahead of a secured party who subsequently registered his PPSA security interest in the land registry office under new section 54(1)(b). The assignee's priority will be with respect to the land as well as to the debt.

What is the position of a security interest in a right to payment under a real estate mortgage to which the PPSA will apply under Bill 163, vis-à-vis the interest of an assignee of a specific real estate mortgage, where the latter registered the mortgage assignment *after* a notice of the security interest had been registered in the proper land registry office? The negative implication from new section 36a(2) is that priority is given to the security interest in the right to payment

\(^{111}\) Cf. text and footnotes 49-52, *supra*. 
governed by the PPSA. But does this priority extend to the real estate mortgage securing the right to payment? A positive answer is suggested if one recalls that the mortgage follows the debt. Nonetheless, is not this rule explicitly rejected by proposed section 3(1)(e)(ii)? Does this mean a split priority? Does this mean that real estate law determines priority? I do not know.

Had Bill 163 been law in Urman, priority would have been given to the competing claimants. Registration of their interests in the proper land registry office, would have protected them against the trustee in bankruptcy. As I indicated, I find this result quite desirable. Nonetheless, Bill 163 does not represent the best way to achieve it.

Benjamin Geva*

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Family Law—Support for Illegitimate Children—Statutory Construction—Retroactive Operation of Law Abolishing Illegitimacy—Retroactive Operation of New Child Support Law.—A wise judge has been quoted early in this century as saying, "There are no illegitimate children; only illegitimate parents", and Ontario's laws have finally caught up with this perceptive reflection with the passage of The Children's Law Reform Act, 1977.¹ Under this enactment, all children, whether born in or out of wedlock are to be treated equally for all purposes in the eyes of the law of the province.² Regrettably, the recent decision of the Ontario High Court in Re Bagaric and Juric³ has suggested that all children are not yet equal, and that the repealed legal regime that distinguished between legitimate and illegitimate children may still survive to haunt those who were unfortunate enough to be born out of wedlock. The case has disturbing implications.

In 1973, nine months after the birth of Elizabeth Bagaric, her unmarried mother brought an application under Ontario's now repealed affiliation legislation⁴ for an order declaring the putative father to be in fact the father of the child and requiring him to pay support. That application was dismissed, no order for maintenance was made,

¹ S.O., 1977, c. 40; now consolidated as R.S.O., 1980, c. 68.
² Ibid., 1 and 2.

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