Municipal Law *continued from page 5*

A private individual does not have these same opportunities available. Moreover, a municipality's repeated use of its funds to support actions against critics is a deterrent in and of itself.

Significance

This brings us full circle, back to examining the fallout from the *Morris v. Johnson* decision. There is no doubt that the Town of Aurora's funding of the action should give anyone pause.

One wonders whether a municipality, before extending funds for litigation against the public, should require the councillor to demonstrate a *prima facia* case of malice on the part of the proposed defendant before providing access to public funds.

At a minimum, any funding should be advanced on the condition that the action is not determined to be SLAPP litigation.

Many more options are likely available. The key is to recognize that, by trying to right one wrong, the damage done to freedom of expression is at least as severe.

If there is any doubt, the manner in which Morris walked away from the action without explanation should continue to serve as an example of why this discussion is important.

Abuse of funds and process

Municipalities are stewards of public funds and must, first and foremost, defend against the abuse of public funds and the court system, especially through SLAPP litigation.

The finding of the Court that the *Morris v. Johnson* action was SLAPP litigation, used to silence opposition, means that public funds were put to an improper use.

The public sees these types of decisions, at least partially, as council defending its own. While Morris will continue to hold the ignominious distinction of ending up on the wrong side of a costs award for "SLAPP'ing" her critics, municipalities must have a discussion on the use of one of the most powerful tools — funding.

Without additional checks and balances, such actions will appear founded on improper motives. Any time a municipality turns its mind to funding litigation, it should be cognizant not to "SLAPP" its critics.

REFERENCES: *Morris v. Johnson,* 2012 ONSC 5824 (Ont. S.C.J.); *Holyday v. Toronto (City)* (2010) 74 MPLR (4th) 194.

SECURED AND UNSECURED TRANSACTIONS

Courts consider true versus security lease

Jenelle Ambrose and Cynthia Hickey,
Fraser Milner Casgrain LLP

The categorization of a lease as either true lease or a security lease impacts the recovery of a lessor.

The issue of whether a lease is a true lease or a security lease continues to generate a lot of controversy and is one of the most litigated personal property security issues.

In Ontario and many other jurisdictions in Canada, a true lease (generally, a lease with a term of more than one year) is deemed to be a security interest under the *Personal Property Security Act* (Ontario) (the "PPSA").

In determining whether an agreement is a true lease or a security lease, the courts have considered, *inter alia*, the following indicia:

a) Nature of the Business;
b) Intention of the Parties;
c) Benefits and Disadvantages of Ownership;
d) Option to Purchase;
e) Transfer of Ownership;
f) Security Interest; and
g) Effect of the Transaction.

Definition

The PPSA's definition of "leases for a term of more than one year" applies to any true lease with an actual term of more than one year. It also extends to any true lease with the potential of having a term exceeding one year. This includes either a lease for an indefinite term or a lease for a term of less than one year but which is automatically renewable for one or more terms, the total of which may exceed one year.

In addition, the definition covers an overholding lessee permitted by the lessor. If the initial and any renewal term(s) of a true lease is less than one year and, with the consent of the lessor, the lessee retains uninterrupted or substantially uninterrupted possession of the leased goods for a continuous period of more than one year, such a lease will become subject to the PPSA, but only after the lessee's possession exceeds one year.

Facts

Most recently, in *Re Scott*, the Ontario Superior Court of Justice considered whether a lease was a true lease and therefore *exempt* from the PPSA's enforcement provisions, or a security lease and subject to the PPSA's enforcement provisions.

Barbara Joan Scott (the "Bankrupt") made an Assignment in Bankruptcy. Around the time of her assignment, the Bankrupt entered into a lease agreement with Ringuette Auto Sales ("Ringuette").

See Secured and Unsecured Transactions, page 7

 continued from page 6

Ringuette did not register a security interest pursuant to the PPSA, but the Bankrupt disclosed to the trustee-in-bankruptcy (the "Scott Trustee") that her vehicle was a lease.

The Scott Trustee sent a request to Ringuette for particulars of the security interest but received no response. Following her assignment, the Bankrupt continued to pay Ringuette the required monthly lease payment for several months. When she defaulted in payment, Ringuette seized the vehicle.

Security lease

The Ontario Superior Court of Justice held that if an automobile is meant to become the property of the debtor after the end of a lease, then the agreement is a security lease and not a true lease.

Moreover, the court found that if a lease is entered into before the debtor's assignment into bankruptcy, then the automobile forms a part of the debtor's property.

The court ordered Ringuette to return all payments made to it after it received notice of the Bankrupt's assignment into bankruptcy. The court found that Ringuette was unaware of the bankruptcy prior to the notice and allowed Ringuette to retain all payments made prior to that notice.

Priority under PPSA

The court also found that Ringuette ought to have registered its security interest in the vehicle, as it was not a true lease. The court held that the Scott Trustee had priority over the automobile by virtue of subs. 20(1)(b) and 20(2) of the PPSA.

Those sections provide that, until perfected, a security interest in collateral is not effective against a person who represents the creditors of a debtor, i.e., a trustee in bankruptcy, and the rights of a statutory lien holder arise at the effective date of bankruptcy or when the lien holder has taken possession.

Financing agreement

New Brunswick's Court of Queen's Bench also considered the composition of a true lease in *Equirex Vehicle Leasing 2007 Inc. v. Powell Associates Ltd*. In that case, the court explained that to determine a true lease, a transaction must be considered in its entirety.

The issue in this case was the nature of the financing contract signed by Ricky Vaughn Douthwright (the "Douthwright Bankrupt"). The Douthwright Bankrupt filed for assignment in bankruptcy and a trustee in bankruptcy (the "Douthwright Trustee") was appointed.

The courts will likely give greater consideration to the intention of the parties in creating a document than to the ultimate form of the document.

One of the assets listed on the Douthwright Bankrupt's statement of affairs was a truck. The Douthwright Bankrupt had financed the truck under the terms of a vehicle lease agreement with Equirex Vehicle Leasing 2007 Inc. (the "Creditor"). The Creditor filed a property claim with the Douthwright Trustee with respect to the truck.

Application dismissed

The Douthwright Trustee conducted a name search in the personal property security registry using the Douthwright Bankrupt's full legal name. As the search showed no record of any security registration, the Douthwright Trustee issued a notice of dispute of property claim. The Creditor applied to set aside the notice of dispute.

The Application was dismissed and the notice of dispute of property claim was held to be valid. The court found that the vehicle financing agreement was a lease for a term exceeding 12 months and as such required any security interest to be perfected pursuant to New Brunswick's *Personal Property Security Act*.

The vehicle financing agreement was, in pith and substance, a lease and not a trust. The court held that the primary intention of the Creditor in using the document was to create a financing agreement, not to establish a trust.

Significance

The determination of whether an agreement constitutes a true lease or a security lease remains relevant both within and outside of the context of the PPSA. The distinction will be especially relevant in instances of insolvency.

Under the *Bankruptcy and Insolvency Act* (Canada) and the *Companies' Creditors Arrangement Act* (Canada), a stay does not apply to a true lease; therefore, lessors under true leases are entitled to certain remedies that are unavailable to lessors under security leases.

The categorization of a lease impacts the recovery of a lessor in many different contexts. It is important to be aware of these categorizations and the factors used in determining a lease's categorization when drafting documents.

It is also important to note that the courts will likely give greater consideration to the intention of the parties in creating a document than to the ultimate form of the document.

REFERENCES: *Re Scott*, 2012 ONSC 4656, 2012 CarswellOnt 10171 (Ont. S.C.J.) (Ont. S.C.J.); *Equirex Vehicle Leasing 2007 Inc. v. Powell Associates Ltd*, 2012 NBQB 42, 2012 CarswellNB 57 (N.B. Q.B.); New Brunswick's *Personal Property Security Act*, S.N.B. 1993, c. P-7.1; *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ; *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36.

See Secured and Unsecured Transactions, page 7