FACTSHEET

BUSINESS MANAGEMENT

ORDER NO. 03-069

SEPTEMBER 2003

AGDEX 817

Ontario Ministry of Agriculture and Food

A GUIDE TO AGRICULTURAL SECURITY AGREEMENTS

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The topic of security and the laws affecting debtors and creditors is complex. This is perhaps why it is easy for business owners, when the business is running smoothly, to fall into a pattern of simply signing documents requested by creditors without taking the time to study the actual meaning of the documents. This Factsheet provides a general overview of security and security agreements, and should give farmers and their advisors a better understanding what they are signing and enable them to reduce the security they give where it is possible and appropriate. Terms "debtor" and "borrower" are used interchangeably as are "creditor" and "lender".

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SECTION 1 — BASICS OF SECURITY AGREEMENTS

WHAT IS SECURITY?

Security is an interest a debtor gives a secured creditor in the debtor's property. Its purpose is to protect the secured creditor if the debtor does not pay what they owe or if they commit some other default under their agreement.

A debtor who has given one creditor security in certain property can give more security in the same property to others, although it might be a default under the debtor's agreement with the first secured creditor to do that. Secured creditors with security in the same property generally do not share it equally if the debtor defaults. Instead, each creditor's rights over the property depend on the rank ("priority") of their particular security. Priority among secured creditors depends on such circumstances as when their security was obtained, when and how it was registered, and the type of security.

WHEN AND WHY TO USE SECURITY

At the time debtors are borrowing money or acquiring goods or services on credit, most fully intend to pay what is owed when due. Unfortunately, good intentions may not be accomplished. The market for products may shrink, weather may destroy crops, disease may strike livestock, interest rates, inflation, or the cost of supplies may rise dramatically.

Prudent creditors try to protect themselves against such uncertainties by taking security. When a debtor defaults, the ability to take property may be faster, cheaper and more successful than starting a lawsuit against the debtor.

In certain cases, it may be beneficial for the debtor to agree to give security. Sometimes a debtor cannot obtain credit at all without giving security. Or, providing security may mean a more favourable interest rate since the creditor's exposure is lessened.
When it makes good business sense, any creditor — whether a farmer, a banker or a supplier — should take security from a debtor. Here are some factors for debtors and creditors to consider.

- Can the creditor afford to lose the amount of the loan if the debtor does not or cannot pay?
- Is this the sort of credit for which other creditors would normally seek security?

- Which property should the security cover? The creditor should conduct a search against the debtor and relevant property to determine if anyone else is registered as owner or secured creditor.

- How much property should security cover? There should be a sensible balance between the amount of the credit and the amount and type of property the security covers.

It is important to ensure that the security documents are properly prepared, signed and registered. Having security that does not work against the debtor and other creditors is worse than not taking security at all as the creditor is lulled into the false belief that they are protected.

SIGNING SECURITY AGREEMENTS

It is important to understand any agreement you sign. Agreements you think provide the lender with limited security may in fact contain clauses giving the lender security over all your assets, similar to a general security agreement. Recognising this before signing any agreement permits you to negotiate with your lender about reducing the amount of security required.

Before signing any agreements a borrower should know the answer to the following questions.

- What must I do under this agreement?

- What can happen to my property and me if I can't live up to my promises in the agreement?

- Are there any practical, cost-effective changes that are likely to be acceptable to my creditor that will make the deal or the documents better for me?

Many creditors, especially large institutions, will be unlikely to change their standard security agreements at the request of one customer. However, they may be willing to reduce the amount of property the security will affect, or to restrict the part of the indebtedness for which security is required.

If you do decide to give your creditor security, make sure you get an exact copy of every security agreement and other documents you sign. Keep these copies in your farm records. These will act as reminder for you to contact your creditor about discharging security when you've paid everything you owe.

WHAT SECURITY AGREEMENTS DO YOU HAVE?

Keeping track of the agreements you sign in the course of business and their implications can be challenging for business owners. The following is a list of common security agreements a business owner might sign based on the creditor involved. This is not an exhaustive list nor does it imply that all of these agreements are used in each case. Any of these agreements might be used where the creditor is a private individual or in a parent–child arrangement. (See *Section 3* for definitions.)

Banks, Farm Credit Corporation and Credit Unions — can use the full range of agreements including mortgages, general security agreements, and letters of direction and loan guarantees.

Agriculture Commodity Corporation — priority agreements and letters of direction

Feeder Finance Co-ops — Purchase Money Security Interest (PMSI)

Agricultural Suppliers — Purchase Money Security Interest (PMSI)

Machinery and Equipment Dealers — Purchase Money Security Interest (PMSI)

DEFAULTING ON A LOAN — TERM DEBT VERSES DEMAND DEBT

Borrowers are sometimes unpleasantly surprised to learn a lender has decided to "call" a loan. "Can the lender do that?" is a usually the first question. The answer depends on whether the debt is *term* or *demand*. Examples of *demand debt* are an operating line or an open promissory note. Demand debt must be repaid when the lender "demands" the repayment. *Term debt*, on the other hand, must be repaid according to the terms of the agreement. Examples of term debt are mortgages or an equipment loan, which could be secured using a chattel mortgage or a PMSI. The only time a lender can demand repayment of term debt is when the borrower "defaults" on the loan. Default usually means a payment is missed, but there may be other circumstances included in the security agreement that constitute a default. The lender then can proceed with action against the borrower to collect on the debt. The actions a lender can take are outlined in the security agreement.

The *Farm Debt Mediation Act* states that a lender must give farmers 15 business days notice before taking any action against them on secured loans.

SECTION 2 — LAND MORTGAGES

Agreements that give a creditor security over land in the registry system are called mortgages. The mortgagor is the person who mortgages the land; the mortgagee is the creditor to whom the mortgage is given. In the land titles system, the name for a mortgage is charge, the mortgagor is the chargor and the mortgagee is the chargee. In this section, the terms "mortgage", "mortgagor" and "mortgagee" are used for both land registry and land titles systems because those words are more commonly used.

Mortgages affecting land follow a simple concept with regard to priorities. The indebtedness secured by a first mortgage has a first priority over the land that is subject only to property taxes. Therefore, if a creditor sells a farm, the creditor holding the first mortgage is entitled to be paid in full from the sale proceeds before any second mortgagee receives any money.

The two types of farm mortgages are:

- *Conventional Mortgages*, which are typically used to finance the purchase of land, and
- *Collateral Mortgages* in which the land is utilized as security for other types of indebtedness.

CONVENTIONAL MORTGAGE

The traditional mortgage registered against property consists of a document executed by a farmer outlining the legal description of the land and repayment terms of the mortgage and a document known as the *Standard Charge Terms*. This document is registered at the Land Registry office where the lender's security interest is noted in the appropriate records.

Traditional standard charge terms often consist of several pages of very fine print. Fortunately, some financial institutions have started to use plain language mortgages that are easier to understand.

Standard charge terms outline the basic contract contained within a mortgage. It usually notes that a farmer charges his entire interest in the property to the lender in exchange for a loan. Provided the business continues to meet the payments, few of the other standard charge terms will be relevant. However, standard charge terms are designed to protect the lender if the farmer experiences financial distress, and accordingly, an array of contractual rights are provided to the lender within its standard charge terms.

The standard charge terms usually outline the rights of lender if a default occurs. Those remedies include selling the farm by power of sale, foreclosure, suing the farmer for possession of the property or for the loan amount and appointing a receiver to manage the farm property. There is also a "personal covenant" that permits the lender to sue a farmer for any shortfall that results if the farm is sold and the proceeds do not pay the loan in full.

COLLATERAL MORTGAGE

A collateral mortgage offers security over real estate when loans are provided for purposes other than the purchase of land.

For example: A collateral mortgage could be used to secure indebtedness undertaken by a farmer through an operating loan, or for the purchase of quota.

Typically, a collateral mortgage remains in place to secure fluctuating advances and new term loan borrowing arranged when previous loans have been repaid.

The first page of the collateral mortgage usually outlines the interest rates, names of the parties and legal description of the land, and in this respect is similar to a conventional mortgage. The difference is found in the schedule registered with the front page of the mortgage. The schedule outlines those areas of the mortgage **c**ontract not contained within the traditional mortgage or standard charge terms. The differences are usually:

- the maximum amount of credit is inserted as the mortgage amount. Because in most cases the actual indebtedness will float up or down during the course of the year, the mortgage must relate to the maximum credit granted to the farmer;
- the interest rate is noted either as a fixed interest rate or as a floating rate;
- the mortgage notes that new loans obtained after the date of the mortgage will be deemed to be secured by the collateral mortgage.

If using a collateral mortgage means a farmer can obtain a more favourable interest rate than the lender will provide without a mortgage, then using a collateral

mortgage makes sound financial sense. However, there is a tendency among some lenders to use collateral mortgages to obtain security over land where the lender would be well protected if its security was limited to the farmer's other assets. In these situations, a collateral mortgage simply serves to provide a financial institution with security over all property and it limits the ability of a farmer to secure credit from other institutions.

SECTION 3 — PERSONAL PROPERTY SECURITY

THE *ONTARIO PERSONAL PROPERTY SECURITY ACT* (PPSA)

Personal property is the term used to describe property that is not land. A variety of security instruments are available to a creditor.

The *Personal Property Security Act* is the provincial law governing security over personal property. The Personal Property Registration Branch of the Ministry of Consumer and Business Services administers it. The *Act* has created a central registry system for the province that permits creditors to file a financing statement outlining the security. Once registered, the creditor filing the document has a secured interest in the property, which takes priority over all subsequent registrations pertaining to the same property.

There are two steps to creating a valid security interest in personal property. First, the borrower must execute a document that creates a contract. The terms of the contract outlines the type of security provided to the creditor and the assets over which the security has been granted by the borrower. The relationship between the borrower and the creditor is governed by the terms of the written contract.

Once the borrower signs the written contract, it is creditor's responsibility to register the financing statement pursuant to the *Personal Property Security Act*. Notice of the Financing Statement is entered in the system and anyone who later searches the farmer's name will be advised of the registered security.

TYPES OF SECURITY AGREEMENTS TO WHICH THE PPSA APPLIES

The PPSA applies to every transaction that in substance creates a security interest, no matter what name the creditor gives to the agreement, with specific exceptions such as liens and pawnbroking. A borrower should be aware that some documents they are asked to sign might not be clearly titled as a security agreement. Once again it is important to understand what the document says. Here are the most common varieties.

General Security Agreement (GSA)

Unless amended to delete some types of property, a GSA creates a security interest in:

- all personal property and fixtures the debtor has when they sign the GSA
- all other property and fixtures the debtor gets later (automatically as soon as the debtor gets them) and
- all proceeds of disposition of any of it.

The general security agreement defines property to include inventory, equipment, accounts, book debts, debts, deeds and contractual rights. Additionally, the agreement normally specifies the chattels owned by the farmer at the date of execution in a schedule attached to the agreement.

General security agreements may be used as a first charge over property, or as a secondary charge to cover the equity in an asset that has been previously secured by other creditors.

In liquidation, the general security agreement gives the lender the ability to seize and sell the farmer's assets. If the lender sells assets over which it has a first position, the lender is entitled to keep the entire proceeds of sale. If the lender sells security over which some other party has a prior charge, then the prior charge is paid in full before the lender receives any funds from the sale of that particular asset.

General Assignment of Accounts (GAA)

Like a general security agreement, a GAA covers the debtor's existing and future property, but in this case only the debts others owe to the debtor and other property that relates to those debts. A GAA gives the creditor access to whatever the debtor is owed, including payments a farmer may not normally think of as accounts receivable, such as support payments for produce, the sale price of breeding stock and the monthly milk cheque. Borrowers need to consider whether to exclude certain debts before signing a GAA.

Chattel Mortgage

This agreement is normally used to take security in a few specific items rather than in the entire debtor's collateral. Read it carefully. The security interest may extend beyond the specific items to their proceeds, to all other property that replaces or is added to them, and sometimes even to all other present and future property

of the debtor. This additional security interest can create a chattel mortgage that is, in effect, no different than a general security agreement.

Purchase Money Security Interest (PMSI)

A *Purchase Money Security Interest* (commonly called a PMSI, pronounced "pimsi") is designed to provide the supplier of goods with a security interest in that specific property. As the name suggests, this security interest is available to lenders of money to finance the purchase of personal property. PMSIs are very valuable to creditors because they have a super-priority over other security interests.

Creditors use PMSI's to enable borrowers to buy goods. This can be a conditional sale or a loan enabling the buyer to buy from someone else. Both enjoy the status of the conditional seller under the PPSA for priority and other purposes. The rationale is that since purchase money creditors give debtors a new asset they deserve first priority.

PMSI priority only applies when a specific and identifiable asset is bought with it. It does not give a priority if the money is used generally in the course of the debtor's business.

One very common type of PMSI is used to purchase crop inputs. Within the PMSI contract, the farmer agrees to pay for crop inputs and to provide a security interest over the crops produced. After receiving the security instrument from the farmer, the creditor can supply fertilizer, seed, herbicide and other products.

If a dispute arises between creditors as to priorities, the PMSI will provide a first charge over the crops produced, even if a financial institution holds other security that purports to place the institution in first place over all of the farmer's property.

PMSI Super-priority Example

A borrower who has given a GSA to his bank over all his present and future personal property wants to buy a combine and finance it with the dealer rather than the bank. If the dealer takes and registers a conditional sale agreement in the regular way, the bank will get the combine ahead of the dealer should the debtor default because the bank's security interest was perfected first. The dealer can get a super-priority over the bank's GSA by following the *Act's* special PMSI rules and registering his financing statement in the required manner.

PMSI Notification

On a practical basis, a secured party taking a PMSI in inventory who wants the special priority has to give all other secured parties who have registered financing statements over inventory, written notice of the PMSI, describing the inventory it affects.

Searches

The PPS computer and land registry records are public. Anyone who pays the fee can search them by debtor name. Obviously, the search turns up only registrations that match the debtor name requested. Getting the name right, whether in a search or a registration is critical.

Registrations

Registration protects the security interest against people who deal with the debtor. If a secured party doesn't register properly, that won't let the debtor out of his or obligations. A secured party registers under the PPSA by paying the government fee and filing a financing statement. This can be done by mail, in person at one of the PPS offices, or electronically. The financing statement includes the debtor's name, address, and birth date; how many years the registration is to last; the name and address of the secured party and any agent who registered the statement; the PPSA classifications for the collateral (one or more of consumer goods, inventory, equipment, accounts and other); whether or not the collateral includes any motor vehicles; and, sometimes, the principal amount owing, when it will be due or a specific description of the collateral.

SECTION 4 — BANK ACT SECURITY

Generally, property is the responsibility of the provincial government, and is governed by the *Personal Property Security Act (PPSA)*. Banks, however, are regulated by the federal *Bank Act*, which means both levels of government are involved in the security process affecting farmers.

The *Bank Act* gives banks the right to take security upon farm assets. This right is outlined in Section 427 of the *Act*, called *Section 427 Security*. This section authorizes the bank to lend money and make advances upon the security of property including crops, livestock and implements. The security covers property owned by the farmer when the documents are signed as well as property of the same kind acquired after signing.

For example: If security under the Bank Act is granted with regard to cows, the security will cover all calves produced by the cows.

The effect of *Bank Act* security is similar to that of a general security agreement. The bank is granted security over different types of personal property in exchange for loans provided to the farmer.

When Can A Bank Act on Section 427 Security?

Before a bank can act on section 427 security given by a farmer, the bank must give the farmer the notice and wait the 15 business days as required by the *Farm Debt Mediation Act*. The bank may also have to give a section 244 notice and wait for 10 days under the *Bankruptcy and Insolvency Act*.

SECTION 5 — PROMISSORY NOTES AND GUARANTEES

Although these two kinds of documents are often called security, they are not — as they do not give the creditor any interest in the property of the person who signs them.

PROMISSORY NOTE

A promissory note is a written promise by the person signing it to pay to another person a specific amount of money. The note can either be:

- a *demand note*, where the person who owes money must pay it whenever the person named in the note demands to be paid, or
- a *term* or *instalment* note, where money is paid at the particular time or times.

A note is only evidence of the debt it refers to, not security for that debt. If the person who signed the note does not pay on time, the person who then holds the note must sue in court to collect. A promissory note is a negotiable instrument. This means the person to whom it is given can sell it to someone else rather than keeping it until paid. That buyer can sell it again or collect under it and so on.

Although promissory notes do not provide security in any property to a financial institution, they are often used with security instruments as part of a financial package. One or more promissory note will outline the size of the debt at any given time, while a general security agreement, *Bank Act* security or other security instrument will provide the lender with security over farm property.

More than one person can sign a promissory note. If they sign "jointly and severally", the creditor is not forced to sue each of them for that person's share of the debt. Instead, the creditor can choose to collect the whole amount from any of them. Naturally, the creditor will choose the one who appears to have money (such as a bank account or salary) that can most easily be taken to pay the judgment. It will be up to that person to try to extract from the other debtors the shares they should pay.

GUARANTEES

A *guarantee* is a promise to accept responsibility for the indebtedness of the borrower. It is an agreement between a guarantor and a creditor in which the guarantor promises to pay the money that a particular debtor owes to the creditor if the debtor defaults.

Financial institutions often use guarantees when farm property is in the name of one spouse or a corporation, and the financial institution wants to ensure the other spouse or the corporation owners are legally bound to repay the indebtedness.

There are several issues concerning the extent of liability, the order of collection and the cancellation of a guarantee that the guarantor should understand.

Limited or Unlimited Liability

The liability granted in a guarantee can either be limited or unlimited in nature. A *limited* guarantee means the guarantor is liable only for the stated amount in the guarantee. The *unlimited* guarantee means the guarantor is liable for the entire indebtedness of the borrower. Obviously it is very important to know which type is being signed. As a guarantor, always attempt to negotiate a limit on the guarantee.

Order of Collection

Some guarantees state that the assets of the borrower must be liquidated in full before the lender may demand payment from the guarantor, while other guarantee contracts state that the lender shall not have to exhaust its remedies against the borrower before suing the guarantor. In the second case, the creditor can bypass the original debtor and proceed to collect from the guarantor right away.

Sometimes a guarantee also contains a security agreement. This means the guarantor gives the creditor security over the guarantor's property for the money owing if the creditor has to call on the guarantee. Usually, the security is an assignment of all debts the

original debtor owes the guarantor then or later, and a promise that the guarantor will not collect anything the debtor owes him or her until everything the debtor owes the creditor is paid in full. It could also be a mortgage on land or security in the guarantor's personal property.

Cancellation of a Guarantee

Guarantee agreements should contain a clause outlining how to cancel the guarantee. A guarantee is not cancelled automatically upon death. Most guarantees bind estates so cancelling the guarantee may mean the creditor can declare the debtor in default, or can cut back the amount of credit. The cancellation usually goes into effect within 30 days. You, or your estate, remain liable for all obligations the debtor takes on prior to that effective date. Be sure to get the cancellation in writing from the creditor. As soon as the debtor carries out the particular obligations you agreed to guarantee, contact the creditor for written confirmation that your guarantee has ended and you owe nothing under it. If you do not you may find the creditor will make a claim against you or your estate for some new obligation the debtor incurs, for which you may not have intended to provide a guarantee.

CO-SIGNED LOANS

A loan is co-signed when a person who is not receiving the money agrees to sign the loan documents as a debtor. A typical example of a co-signed loan is if a parent signs a promissory note to help a young farmer obtain funds. The signature makes the parent responsible for the loan.

A co-signee is liable to repay the debt in the same fashion as the person who actually borrowed the money.

ACCOMMODATING SECURITY

An alternative to the guarantee may be "accommodating security". Accommodating security describes property given as security by one person to a financial institution as part of the debt structure between another person and the institution. Usually, accommodating security occurs when a farmer's child begins farming but does not have sufficient equity to obtain credit. The parents may be asked to provide their property as security for their child's bank loans.

The benefit of pledging a specific asset instead of signing a guarantee is that the individual giving the accommodating security knows that their liability is limited to the value of the pledged asset. Be careful that the terms of the agreement outlining the accommodating security are accurate.

For example: If a parent is providing a mortgage over one parcel of land as accommodating security, the mortgage materials must state that the liability of the parent is limited to that piece of land.

SECTION 6 — ASSIGNMENTS AND DIRECTIONS

PRIORITY AGREEMENTS

Secured parties can agree to let other secured parties, whose security would normally come after their claim, have priority ahead of them. This is done by deliberately signing a subordination or postponement agreement, or adding a clause in their own security agreement that says certain kinds of security interests can go ahead of theirs.

For example: A farming child has given security to their parents as well as the bank for money borrowed from each of them. The bank will usually require the parents to agree to subordinate their security to the banks.

ASSIGNMENTS AND DIRECTIONS

Creditors use an assortment of assignments and directions to intercept a farmer's income. The documents permit the creditor to obtain payment for loans before the farmer is given access to the income. Assignments can deal with any form of income.

For example: Assignments used by lenders to obtain payment of income directly from marketing boards to the lender, directions to elevators instructing them to pay funds generated from the sale of crops to the holder of PMSI security, and assignments to AGRICORP dealing with funds generated from crop insurance or the Market Revenue Insurance Program.

Assignments and directions tend to be the most straightforward part of a farm security package because they are short documents written in plain English.

SECTION 7 — AGRICULTURAL QUOTAS

AGRICULTURAL QUOTAS

Three Ontario Court of Appeal decisions determined that quotas are not property but rather licenses to

produce commodities. Therefore, a lender cannot obtain a binding security interest in quota because quota is not property. As such the security agreement cannot be enforced.

While quota is not security as such, it is secured by financial institutions through other documents relating to property. Financial institutions can use letters of direction to marketing boards to prevent a farmer from selling quota without the consent of the institution (*see Section 6*). These are similar to other directions used by financial institutions that direct the payment of proceeds from the sale of milk to a lender. Some farmers are also asked to execute documents preventing them from transferring the quota to any other person without the lender's consent. These documents are valid security documents in favour of a lender — and create a situation where the quota itself is not subject to any security, but all monies earned from the quota are secured in favour of a financial institution.

The Issue Before the Court — Was Quota Property or a License?

The Ontario Court of Appeal had to determine whether quotas were property owned by the farmer or a license to produce a commodity owned by a marketing board and granted to the farmer.

The fact that agricultural quotas can be bought and sold on a market provided a strong argument in favour of describing quotas as property. However, the statutes and regulations governing marketing boards that use quotas usually state that the purpose of the legislation is to provide for the complete control of the production and sale of certain agricultural commodities in Ontario. The concept of complete control through a licensing system conflicts with the concept of quotas as property.

This issue had significant implications for farmers who produce commodities controlled through quotas because many financial institutions traditionally treated quotas as property and provided loans secured by quota. Quotas are often listed as property within general security agreements or chattel mortgages and financial institutions relied upon the quotas to provide security.

SECTION 8 — CONTRUCTION LIENS

CONSTRUCTION LIEN ACT

The *Construction Lien Act* provides security for construction contractors. A contractor can take a lien upon the interest of the owner of property that has been improved by the labour or materials supplied by the contractor.

A contractor may, within 45 days of the work begin substantially completed, register his construction lien against the title to a farmer's land if the contractor is not paid.

A registered construction lien remains registered on title until one of the following events happens:

- the contractor is paid in full and removes the lien
- a court orders the discharge of the lien following a trial or settlement if the farmer is disputing liability to pay the contractor
- the farmer places money in trust with the court or posts a construction lien bond.

A construction lien can pose a significant problem to farm finance. If a lien is registered during a major construction project for which a lender is providing financing as the construction proceeds, the lender will insist the lien be removed from title before advancing more funds. As well, any financial institution providing ongoing financing is likely to feel uncomfortable with a construction lien registered on title (even if that lien is behind valid mortgages) unless the institution realizes that the lien is arising from a dispute regarding the quality of the contractor's work as opposed to an inability to pay the bill.

Careful planning is the key to avoiding construction liens. Carefully analyze the cost of major construction projects before beginning construction, and make allowances for cost overruns or extras not foreseen in the initial budget. This should avoid costly litigation and prevent an order to sell the land to pay a contractor, if no other method of raising funds to satisfy the lien exists.

SUMMARY

There is no doubt that the issues around security can be complex. Nor is there any doubt that security arrangements are necessary in obtaining the significant financing agricultural operations need. Because of these realities it is important farm business owners manage and monitor their credit arrangements. One component of good management is reviewing and understanding in advance the security documents they sign.

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This publication is intended as general information and not as specific advice concerning individual situations. Although it outlines some of the legal considerations of security agreements it should not be considered as either an interpretation or complete coverage of the *Personal Property Security Act*, *the Bank Act* or the various law affecting security agreements. The Government of Ontario assumes no responsibility towards persons using it as such. All security agreements should be discussed with your lawyer before they are signed.

This Factsheet was written by **Rob Gamble**, Finance and Business Structures Program Lead, Guelph, OMAF and **G. Edward Oldfield,** Barrister and Solicitor, Hobson, Taylor, Oldfield, Greaves & D'Agostino, Waterloo.

References were taken from a publication called *"Legal Aspects of Farm Finance"* written by **B. Lynn Paul**, Barrister and Solicitor, and from a paper called *"Security Instruments – A Review"* by **G. Edward Oldfield,** Barrister and Solicitor.

APPENDIX 1 — DEFINITIONS

Financing agreements and their related legislation have specific language. Below are non-technical definitions of terms often used in security discussions.

creditor —a person who lends money to another person to be paid back later, or who supplies goods or services to another person to be paid for later.

debtor —a person who owes money to a creditor to repay a loan or to pay for goods or services supplied.

default — a person is "in default" or "defaults" by not doing something as promised in the agreement (like making a payment), or doing something he/she promised not to do (selling property without a creditor's permission), or when some other thing happens that the agreement said would be a default (a sheriff seizing some of the person's property).

encumbrance —an interest one person (the "encumbrancer") has in another person's property. The interest may be a security, such as a mortgage on land, or it may be another sort of interest, such as the lien the garage has on a tractor for the cost of repairing it.

person —generally means not just humans, but also corporations, partnerships, associations, and other entities.

personal property —all property is divided into two classes: real property, that is land or part of the land where it is located and personal property, which is everything else. Some examples of personal property are furniture, clothing, vehicles, cows, crops and debts people owe.

property —anything that a person can own. Property is either real property or personal property.

realize — when a debtor defaults, a secured creditor may recover some of the loss of that default by realizing, that is, selling or keeping, the debtor's property covered by the security agreement.

real property —is land and items the law says become part of it once put there, such as most buildings, trees and some crops.

secured creditor —is a creditor who has taken security from a debtor.

security —an interest in a debtor's property that the debtor gives to a creditor to protect the creditor from loss if there is a default by the debtor. Sometimes people call the *agreement* that gives the secured creditor this interest "security" too.

security agreement —is the document or combination of documents a debtor signs (sometimes the secured creditor signs too) to give the secured creditor security in the debtor's property described there. Security agreements can give security in real property, personal property or both.

unsecured creditor —is a person who gives a debtor credit without taking any security. An example is a storekeeper letting a customer run a tab on groceries on the understanding they will be paid when the next milk cheque comes. If the debtor does not pay, the unsecured creditor must sue to for the right to have the sheriff seize and sell the debtor's property.

TERMINOLOGY USED IN THE *PPSA*

The *Personal Property Security Act* (*PPSA*) applies to most security agreements, whatever form they take, that cover personal property or fixtures located in Ontario. Some special terminology is used in those agreements.

collateral —personal property (including fixtures) affected by the security. Do not confuse this meaning with common language where "collateral security" means security in addition to the main security for the debt.

consumer goods —tangible personal property used primarily for personal, family or household purposes, such as the dining room table, stereo and computer.

financing statement, financing change statement — the forms a creditor registers in the *PPSA* computer to protect the priority of the security.

fixture —personal property that has become part of land, either permanently or temporarily, by being installed there, such as a silo or stable cleaner.

PMSI or purchase money security interest —is the security a debtor gives in particular collateral for the purchase price of that property to the supplier or to the person who loaned the money the debtor used to acquire the collateral.

secured party — the *PPSA* name for a secured creditor.

security interest — the PPSA term for the interest in collateral a debtor gives to a secured party to protect that secured party if the debtor defaults.

FOR YOUR NOTES

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POD
ISSN 1198-712X
Également disponible en français
(commande n° 03-070)

*012101003