

Lessons Learned - Lesson Four: Always Register Your Lease if it is Greater Than One Year

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*Cassels developed this **Lessons Learned** series based on our experience with priority disputes between secured creditors and the realization that many secured parties make fundamental errors of law that cause them to lose priority in their collateral. Each lesson in the series will outline a basic mistake and the lesson to be learned...*

Lesson Four: Always Register Your Lease if it is Greater Than One Year

We have recently seen insolvency scenarios where the insolvent debtor company had a number of leased assets under leases which either by possession or by their term were for a duration of more than one year. Not all of the lessors registered their leases under the provisions of the relevant *Personal Property Security Act* (PPSA) and as a consequence, lost their collateral, in some cases worth millions of dollars, to secured parties who had a perfected security interest in all of the assets and property of the debtor. The lessors believed, incorrectly, that if their lease was either a true lease or a short term lease, being for less than one year, that they did not have to register under the PPSA. This approach by the lessors is incorrect, and was a lesson learned to all to register a lease of a term of more than one year.

In the common law provinces, the PPSA is clear that any lease of a term of more than one year is subject to the terms of the PPSA and must be registered under the PPSA in order for the lessor to have a perfected security interest and priority over subsequent secured creditors in the same collateral. This is the case if the lease is a true or a finance lease. There are no longer exceptions. This is also different than Article 9R of the Uniform Commercial Code and as such, many US lessors who do not seek advice of Canadian counsel are often left unsecured.

What a lessor must appreciate is how expansive the definition of “lease of a term of more than one year” is under the PPSA. The definition of “lease of a term of more than one year” includes not only a lease which at inception has a term greater than one year but also, among other scenarios, (i) an indefinite lease even if cancellable by one party, (ii) a lease that is less than one year but where the lessee has substantially uninterrupted possession of the leased asset for greater than one year with the lessor’s consent and (iii) a lease of less than one year, if the lease is renewable at the option of one of the parties and it is possible that the initial term and any renewal options together could exceed one year. Accordingly, care must be taken by lessors when entering into and reviewing leases, as simply having a lease of less than one year on its face

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is not a full and complete safe harbour against the requirement to register under the PPSA.

A few helpful examples we encountered are as follows:

- A lessor has leases for eleven months but the lessee retains possession of the leased equipment with the consent of the lessor for an additional two months after the expiration of the initial term. In this scenario, the leased asset has been in substantially uninterrupted possession of the lessee for a continuous period of more than one year. These leases have to be registered under the PPSA.
- A rental company rents month-to-month with the same debtor/lessee. The rental company contends it is simply a month-to-month rental and does not register under the PPSA. In this instance, the definition of 'lease of a term of more than one year' captures scenarios where the asset was in possession of the 'renter' for more than one year. Note that for the purposes of the PPSA this rental scenario is in fact a lease. Again, this scenario is subject to the PPSA and this rental arrangement must be registered.

Lesson Learned

Always read the full contents of the lease and not just the term and if the lease is greater than one year or fits under the other categories, register it. Contact Cassels for more information on when you need to register your leases and priority considerations not discussed in this lesson.

This publication is a general summary of the law. It does not replace legal advice tailored to your specific circumstances.