

Cash Collateral –Proposal for Amendments to Ontario PPSA

Part 1 – Discussion

Part 2 – Proposed Amendments

Part 3 – Explanatory Notes

PART 1 – DISCUSSION

The purpose of this document is to set out and explain a proposal (the “**Proposal**”) for amendments to the *Personal Property Security Act* (Ontario) (“**PPSA**”) that will allow a debtor to provide, and a secured party to obtain, a first priority security interest in certain types of cash collateral perfected by “**control**”.

Brief Description of Proposal

The central feature of the proposed amendments is to enable a secured party to perfect a security interest in a new class of collateral known as a “**financial account**” by registration, or by control. If perfection is by control, priority is conferred on the secured creditor that has or first obtains control. If the secured party is the financial institution with which the financial account is maintained or that is obligated under the financial account, then it has automatic control that will perfect any security interest it has in the financial account. That security interest will also automatically rank first unless another secured party is the customer for whom the financial account is maintained or to whom the financial account is owed, or unless the financial institution has expressly subordinated its interest.

“**Financial accounts**” are broadly defined to include any form of deposit account maintained by a financial institution, and any other monetary obligation of a financial institution in respect of funds held or received by that financial institution as security for an obligation, whether or not in the form of a deposit account. The definition of “**financial institution**” too is very broad so as to include every type of participant in financial markets that regularly receives cash collateral, whether or not that person establishes, or holds funds in, a deposit account. For example, if a secured party receives cash collateral and then uses that cash in its business, the secured party may have a monetary obligation to return that cash collateral or to apply it to the debtor’s obligations. That monetary obligation would be characterized as a financial account. If the parties (or a court) were to characterize the transaction as creating a security interest in that financial account, the security interest would be automatically perfected and have priority over any other security interest in that financial account, unless subordinated.

DRAFT - DECEMBER 21, 2011

“Consumer accounts” are excluded from the control regime. “Consumer accounts” are accounts maintained and used by a natural person primarily for personal, family or household purposes. Consumer accounts are excluded partly because the control regime in Article 9 of the UCC does not apply to consumer accounts and partly to allay some commentators’ fears that financial institutions would exploit their dominant position at the expense of consumers. We believe that consumers and financial institutions would actually both benefit if consumer accounts were included within the definition of financial account, and subject to the control regime; but we are concerned that critics of the Proposal may view consumers differently. Therefore, with a view to minimizing controversy, consumer accounts are excluded. But for those concerns (which we do not believe would be justified), we would have included consumer accounts in the control regime.

Operating accounts are not excluded from the regime. We considered the possibility of excluding operating accounts, and we worked on numerous drafts of the Proposal which excluded operating accounts. Those drafts were much more complex than the current draft, largely to deal with the possibility that the exclusion would be too broad or too ambiguous. For example, an operating account could be defined by reference to a customer’s ability to access funds in the account without the consent of the secured party. This type of definition is too broad because it is common for customers to be permitted to access funds in a blocked account provided certain conditions are met. Recognizing these drafting difficulties, we concluded that operating accounts should be included in the Proposal. In our view, this decision will not generally be significant in practice because: (a) there are usually no significant funds remaining in an operating account at the time of insolvency proceedings, (b) the financial institution which maintains the operating account typically has rights of set-off against that account, and (c) secured parties generally do not extend credit on the strength of funds held in an operating account, whether by way of proceeds or as cash collateral. The inclusion of operating accounts in the control regime is consistent with the approach taken in the United States in Article 9 of the UCC.

The Forms of Cash Collateral

To aid in assessing how effective the various options for a cash collateral solution may be, this section describes in general terms various types of cash collateral and some typical scenarios where cash collateral might be used.¹

1. **The 3P FI Scenario.** A debtor grants a security interest to a secured party in a deposit account maintained by a third-party financial institution in the name of the debtor to secure an obligation owed by the debtor to the secured party.

¹ The Proposal does not address credit balances in a securities account because the current legal regime adequately addresses the use of those credit balances as collateral.

2. **The SP FI Scenario.** A debtor grants (or under the reasoning in the *Caisse Drummond* case², is deemed to have granted) a security interest in a deposit account in favour of a financial institution that maintains the deposit account in the name of the debtor to secure the debtor's obligations to the financial institution.
3. **The SP Obligation Scenario.** A debtor transfers funds to a financial institution to secure obligations owed by the debtor to the financial institution, giving rise to an account receivable (which may be conditional or contingent) owed by that financial institution to the debtor; but no deposit account is established by the financial institution in the debtor's name. The secured party might hold the funds in its own deposit account at another financial institution; or it might use the funds in its own operations.
4. **The SP Account Scenario.** A debtor transfers funds to a deposit account of the secured party maintained at a third party financial institution. The funds in that account and other funds of the secured party may be transferred back and forth between the debtor and the secured party, depending on margin requirements.³

Under the current law, in all of these scenarios the secured party must rely on a PPSA registration to perfect its security interest even though as a practical matter in all but the 3P FI Scenario, its remedy would be to apply the funds in the account to the debtor's obligations by way of set-off or otherwise, rather than to sell, or foreclose on, the collateral.

1. **Possible Objections to the Proposal**

The following summarizes the main concerns that have been expressed in comments on earlier drafts of this Proposal, discusses areas of disagreement and explains how this Proposal addresses those concerns.

Concern: Not all arrangements addressed by this Proposal require a legislative response, at least at this time, and/or a special regime that favours cash collateral secured parties.

We believe that there is currently consensus on the need for reform to provide for a priority for certain cash collateral secured parties to facilitate capital and financial

² *Caisse populaire Desjardins de l'Est de Drummond v. Canada*, 2009 SCC 29.

³ For example, a derivatives counterparty (the debtor) is required to transfer cash collateral to the other counterparty (the secured party) as initial margin or as variation margin to secure the secured party's mark-to-market exposure, which may fluctuate day to day and may require transfers to and from the counterparties.

market transactions, including clearing of OTC derivatives transactions and repurchase agreements.

However, some commentators believe that the case for reform in other contexts, such as commercial lending and business to business arrangements, has not been made and requires further study. According to those commentators, all secured parties who rely on PPSA registrations to perfect their security interests face the same risks and inconvenience associated with registration (*i.e.* the need for searches, subordinations, delays, absence of opinions as to priority). Some commentators argue that there is no policy rationale for a new non temporal priority rule such as exists, for example, for PMSIs or investment property, that would justify special treatment of cash collateral in most cases.

However, in the case of global and domestic capital and financial market transactions (such as derivatives, repo, securities loans and transactions cleared with a central counterparty or clearing house) the certainty of priority with respect to cash collateral is critically important. Additionally, the delays and uncertainty associated with obtaining subordinations and acknowledgments are not acceptable or practical in capital markets and derivatives transactions. Furthermore, a secured party that is a regulated financial institution will not receive regulatory capital relief for collateral it receives from its counterparties if it cannot obtain an opinion as to the first priority of the security interest that secures its exposure. Lawyers do not give priority opinions based on registration. Such an opinion would in any event be impractical to give for many of the financial parties that participate in financial markets given the number of registrations a search report would typically reveal.

Response: The Proposal balances these concerns and goals in several ways:

While the need to provide a solution for financial market transactions is driving the timing of the Proposal and provides the most compelling reasons for reform, it would not be appropriate to design a solution for cash collateral that is specific to these types of transactions (such as a special regime for eligible financial contracts as defined in federal insolvency legislation).⁴ PPSA rules typically are not based on the type of transaction or obligation which is secured. For the most part the scheme of the Act does

⁴ Such a partial solution has (regrettably, in our view) been recently been adopted for derivatives in the Province of Québec. National Assembly, Bill 7, *An Act to amend various legislative provisions concerning the financial sector*, s. 24.2 (assented to on November 30, 2011), which amends the *Derivatives Act* to provide that: “An instrument under which a person is required to pay an amount of money to a party to a derivative, including as a margin or settlement deposit, and which allows that party, in all circumstances described in the instrument, to extinguish or reduce, by means of a set-off, its obligation to repay that amount to the person is enforceable against third persons without further formality.”

not depend on the nature of the secured obligation.⁵ Consequently, it is necessary to formulate a solution around the collateral type and this requires defining a subset of the “account” or “intangible” class of collateral wide enough to cover the types of accounts that are used in the market. That will require a certain over-inclusiveness because the accounts are not readily distinguishable.

The Proposal abandons the concept of the “secured party account” in a previous draft, which was designed to facilitate business-to-business collateral arrangements. While we continue to believe a simpler perfection and priority regime at least for title transfer types of cash collateral arrangements would benefit all commercial parties, in the interests of attempting to reach consensus, this aspect of the former Proposal has been dropped. However, a more limited form of this concept is retained: where the secured party is a financial institution, a transfer of funds to the financial institution for the purpose of securing an obligation to the institution will be covered by the control regime even if no formal deposit account is maintained for an account customer arising from that transfer. This is designed to cover title transfer credit support arrangements, namely the SP Obligation scenario.

The Proposal also excludes consumer accounts, for the reasons explained in the introduction to this Part. We did not exclude operating accounts. Some commentators expressed concern that permitting a secured party to perfect its security interest in an a debtor’s operating account through control and thereby gain automatic priority over any other PPSA security interests could give rise to difficult practical and policy issues of tracing, identifiability and priority with respect to PMSI secured parties and receivables financiers. However, we do not believe this concern is so significant that it must be addressed by limiting the Proposal to blocked accounts (i.e. by excluding operating accounts); and for the reasons outlined above and below, we have included operating accounts in the Proposal. Ultimately, this is a question of judgment about which reasonable people could differ; but after considerable debate, drafting and redrafting, we concluded that the exclusion of operating accounts would significantly undermine the commercial and regulatory objectives the Proposal is attempting to address by introducing complexity and uncertainty.

Concern: Depository institutions that are secured parties with respect to the financial account may abuse their priority position.

The Proposal grants the financial institution automatic control and super priority, even over other secured creditors with control other than a secured creditor that is the customer. The deposit bank need not cede this priority to a third party and need not

⁵ A PMSI is dependent on the type of transaction, but it is also fundamentally tied to the collateral type.

enter into a control agreement. It has been argued that this could result in banks extending their oligopoly over credit and exercising undue market power.

Response: The Proposal addresses this concern by excluding consumer accounts from the super-priority regime. In addition, the financial institution cedes priority to a secured party that acquires control by becoming the account customer of the financial institution. We also believe that this concern seems misplaced.

The enhanced priority given to financial institutions will not apply to consumer accounts. Also, like section 9-327(4) of the UCC, the Proposal now provides that a secured party that perfects its security interest in a financial account by becoming the account customer has priority over the financial institution with which the financial account is maintained. The concern that Canadian financial institutions will abuse their power by refusing to enter into control agreements or subordinate their security interest with respect to financial accounts maintained with them seems misplaced where clients wish to set up special security arrangements with their other creditors. Competitive pressures of the market will prevent this. Securities intermediaries enjoy a similar privileged status under the STA and PPSA and yet routinely enter into control agreements and subordinate their security interests in securities accounts maintained with them except with respect to a small class of obligations such as fees and overdrafts. Banks also regularly enter into blocked account agreements in favour of lending syndicates or PMSI financiers in which they typically subordinate or waive their rights of set-off with the same limited exceptions.

Concern: Perfection by control allows for secret liens, which is contrary to a fundamental policy of the PPSA.

The concern can be expressed as follows: Perfection by control, whether by control agreement, by virtue of the secured party's status as financial institution with which the account is maintained or by virtue of the secured party becoming the financial institution's account customer, necessarily lacks the element of publicity that is the hallmark of the PPSA registration system. There are no public searches that a third party can do to determine whether the debtor's cash is subject to a first priority security interest perfected by control. The fact that secret liens also exist with respect to perfection by possession or by control under the STA is not a complete answer: a Proposal to make an existing problem worse does not solve the problem.

Response: The policy reasons for discouraging secret liens with respect to tangible collateral and receivables do not apply to financial accounts.

The paradigm of the most objectionable form of secret lien is the situation where a debtor appears to own or possess property, such as inventory or the assets which appear on its financial statements, but another person, unknown to creditors, has a lien on the property. Without a registration system, creditors have no means of determining

DRAFT - DECEMBER 21, 2011

who might have a lien other than requesting that information of the debtor. With a financial account, however, any creditor relying on the balance of the account as a form of security or expression of the assets of the debtor will already know the identity of the financial institution. This is not similar to the case of a general assignment of receivables, where it would not be feasible to determine the identity of every account obligor. With a financial account, the only possible “secret” information is whether or not there is a security interest. A financing statement is not required to give another creditor information as to the identity of potential secured parties. While it might provide some information as to whether the financial institution has a security interest in accounts, it will not itself provide meaningful information on whether the financial institution has a security interest in a particular account. Inquiries have to be made in any event to determine whether that particular asset has value.

The Proposal deals with the legitimate interest of other parties in knowing whether a security interest perfected by control exists with respect to a financial account by requiring the financial institution to confirm the existence of its own security interest or a control agreement with another person on inquiry from a person with an interest in the account with the consent of the debtor or on request of the debtor. It also requires the financial institution to seek the consent of the debtor if it does not already have it. In addition the Proposal requires that the security interest be conferred in a written agreement.

In the SP Account scenario and the SP Obligation scenario, the policy objections to secret liens are not engaged because third parties are unlikely to be misled as to whether or not the debtor’s assets are subject to security interests. In the SP Account scenario the deposit account is in the name of the secured party, not the debtor, and the financial account is the debtor’s right to demand repayment of the funds transferred to the secured party’s account. In the SP Obligation scenario, the financial account again is defined by the collateral arrangement itself and there may be no deposit account at all. In neither case would the asset that functions as collateral appear on the books of the debtor as anything other than a contingent receivable, in respect of which the third party will need to make further inquiries of the debtor and the secured party in any event, nor would registration of a financing statement provide any useful information.

We would also note that public filing to perfect security interests in cash collateral is not required under Article 9 of the UCC in the United States, under the Directive on Financial Collateral Arrangements (2002/47/EC, amended 2009/44/EC) in the European Union⁶, or under the UNCITRAL Legislative Guide on Secured Transactions.⁷

⁶ Available on-line at < http://ec.europa.eu/internal_market/financial-markets/collateral/index_en.htm; http://ec.europa.eu/internal_market/financial-markets/collateral/index_en.htm#amending>.

Concern: Conflict of Laws - Allowing a financial institution to designate the governing jurisdiction in an account agreement gives the institution an unwarranted degree of autonomy in determining the applicable law.

The first version of the Proposal recommended adopting the place of the debtor's location to govern validity, perfection and priority of a security interest in a credit account. Those who commented on this approach believed that it would be preferable to choose an approach consistent with the approach for securities accounts, namely the "law of the financial institution's jurisdiction", which is determined chiefly by the terms of the agreement governing the account. The Proposal adopts the law of the financial institution's jurisdiction as the relevant connecting factor for validity, perfection and priority of a security interest in all financial accounts. The concern expressed with this approach is that using the financial institution's jurisdiction as the connecting factor in effect gives financial institutions the unfettered right to arbitrarily designate any jurisdiction in the account agreement without notice to third parties and without regard to the situs of the transaction or the physical location of either the debtor or the financial institution. This degree of party autonomy puts the secured party (if a bank) in control of the law that governs perfection, which is contrary to the principle that conflicts rules should be objectively based.

Response: The potential for abuse (if any) is outweighed by the benefits of the rule.

As with investment property collateral, flows between Canadian and U.S. counterparties are significant. Collateral providers and receivers are, in our experience, quite surprised to learn that security interests that U.S. institutions hold in accounts maintained in the U.S. are governed by Ontario law if the account holder is Canadian. The natural expectation is that the place of the account governs such matters. There are benefits in having a rule which is consistent with UCC Article 9 at least in terms of the conflict of laws rule given the cross-border collateral flows. It will avoid the multiple perfection and sometimes insoluble *renvoi* problems associated with one jurisdiction using debtor location and the other using local law of the bank and this may outweigh any drawbacks.⁸ This rule is also consistent with the PPSA/STA rule for securities accounts and futures accounts and will avoid any conflict between those two regimes. For example, security interests in credit balances in a securities account are governed by

⁷ Available on-line at < http://www.uncitral.org/pdf/english/texts/security-1g/e/09-82670_Ebook-Guide_09-04-10English.pdf>.

⁸ For example, where D is located in Ontario for PPSA purposes and the account is governed by New York law for UCC purposes, the security interest must be perfected in both jurisdictions. Conversely, where D is located in New York for PPSA purposes and the account is governed by Ontario law for UCC purposes, Ontario law says that the security interest must be perfected under New York, but New York law says it must be perfected under Ontario law. Since neither jurisdiction recognizes the method of perfection used in the other, neither one works.

the securities intermediary's jurisdiction, and if a separate financial account is established with the same intermediary that is not a securities account, it would be governed by the same law.

It seems highly unlikely that Canadian financial institutions will arbitrarily start amending their standard form account agreements to designate foreign laws as their local law in order to gain some marginal advantage over a debtor. This sort of rule arbitrage has not occurred in the context of securities accounts, and in our experience financial institutions will not choose a jurisdiction that is not connected to the location of the financial institution or the account to govern their standard form account agreements.

There is admittedly the transitional problem of how to deal with multiple PPSA jurisdictions with inconsistent conflicts rules until all of them have been amended. However, that problem will exist regardless of which rule is adopted.

Concern: A solution should be restricted to segregated or blocked accounts to avoid intractable priority disputes, such as disputes over PMSI proceeds.

Comments have been made that the UCC Article 9 approach creates intractable priorities issues with respect to security interests in general operating accounts, such as PMSI proceeds, that have no clear-cut policy driven solution. These problems can be avoided by restricting control to specific, segregated or blocked accounts that can be used for no purpose other than cash collateral. Professor Wood has proposed a new "blocked account security interest" that would require notice to third parties analogous to that required for inventory PMSIs.

Response: Not all agree that there are intractable priorities issues. Blocked account agreements are not feasible in financial markets transactions.

The proponents of this Proposal do not agree that it creates intractable priorities issues. The model appears to operate effectively in the United States. If the Proposal is implemented, PMSI holders can continue to make arrangements with their debtors for segregation of proceeds to designated accounts (as many do now) and thereby themselves take advantage of the clearer priority rules that the Proposal offers them.

Restricting control to segregated or blocked accounts would not provide a workable solution for cash collateral arrangements in capital and financial market transactions. In a typical derivatives transaction the party required to post cash collateral simply transfers the funds to the secured party as directed (e.g., the SP Obligation scenario) without regard to its ultimate destination. Funds will move back and forth between the parties depending on the estimated exposure to each other. At times a party may be a collateral receiver and at others a collateral provider, depending on their respective

exposures on the secured transactions. Where excess collateral has been provided, the collateral provider can request its repayment.

A collateral provider will often also have the right to substitute cash collateral with other acceptable forms of collateral, such as a letter of credit or securities, and will be entitled to a repayment of the cash collateral. The collateral provider may require the cash to fund other activities and prefer at various points to post securities or vice-versa. This flexibility increases liquidity and allows parties to make maximum use of their fungible assets. Any requirement that restricts a solution to funds in a third party account that are to remain blocked or segregated and which does not recognize substitution rights will not provide a workable solution and will certainly be viewed as no solution at all by market participants.

Also, it is extremely unclear what it means to have a segregated account where the secured party is the financial institution with the obligation that constitutes the financial account. By its nature, a deposit account creates a debtor/creditor relationship. The transferred funds are by definition used by the receiving financial institution as its own, as are any funds on deposit with a financial institution. Capital requirements (which take into account the right to net against transaction obligations as long as the priority is clear) protect the collateral provider.

A blocked account may be a substitute for the account control agreement where the account is with a third party institution. However, even there it is not a workable general solution for financial market transactions. Say, for example, that a bank-owned dealer, XYZ Securities has received cash into a Canadian customer's financial account to secure securities loans, and pursuant to the account agreement, it has granted a security interest to XYZ Securities to secure securities trading activities and margin requirements as well as to XYZ Bank to secure OTC derivatives transactions and other XYZ affiliates to secure other trading activities such as securities loans. This is a very common arrangement between prime brokers and their customers. The agreement is drafted to be a control agreement in favour of XYZ Bank and the XYZ affiliates with XYZ Securities as the financial institution and allows those entities to give orders on default subject to XYZ Securities' own security interest. Excess collateral in the accounts may also be used to fund settlements of trades. To require the financial account to be blocked and used only to secure the obligations with a particular party or only for purposes of collateral would defeat the efficiency and flexibility of these types of arrangements.

There may very well be policy reasons for requiring certain collateral arrangements to be restricted to segregated accounts. For example, in the context of central counterparties, regulators of those entities with responsibility for regulating so as to reduce systemic risk in the clearing system and protection of clearing clients might determine that a clearing house should maintain cash collateral it receives in a

DRAFT - DECEMBER 21, 2011

bankruptcy remote custodial institution account. However, these are not the policy imperatives of the PPSA.

The Principles upon which the Proposed Solution is Based

The Proposal is offered as a solution that balances the following principles and interests. Like any compromise solution it may not satisfy every interest. In our view, the optimal solution should:

- ensure that in the context of capital and financial market transactions, such as bilateral and cleared OTC derivatives transactions, and securities financing transactions such as securities loans, repurchase transactions and margin loans, the participants are able to provide and receive a security interest in cash collateral that is not subject to competing security of other consensual secured creditors;
- ensure that priority is not dependent on the filing of a financing statement and the order of registration of a financing statement;
- reflect methods of doing business in Canadian and global financial markets and not require adopting any new or special procedures or notice periods to create effective security that do not respond to the constricted time frames of transacting in financial markets. A repo for example, may be entered into and fully performed in the space of a few days;
- allow a debtor the right to substitute cash collateral with other forms of financial collateral, such as investment property, without compromising the effectiveness of the security interest;
- recognize that cash collateral balances may fluctuate on a frequent basis with a debtor being permitted to use those balances to secure a number of different transactions;
- recognize that a secured party receiving cash collateral is not required to segregate cash collateral unless the arrangement with the debtor requires it;
- ensure that active participants in the financial markets, including the Province of Ontario and other Crown participants, pension funds and mutual funds do not have to establish the existence of a deposit account in order to rely on the benefits of perfection by control; and
- clarify the conflict of laws rules applicable to cash collateral arrangements.

In our view the Proposal is an optimal solution which meets all of these criteria.

DRAFT - DECEMBER 21, 2011

PART 2 – PROPOSED AMENDMENTS TO THE PPSA

1. Add or amend the following definitions in subsection 1(1):

“**account**” means a monetary obligation not evidenced by chattel paper or an instrument, whether or not it has been earned by performance, but does not include investment property or a financial account;

“**consumer account**” means an account that is maintained for a natural person and is used by the natural person primarily for personal, family or household purposes;

“**customer**” means a person for whom a financial institution maintains a deposit account and a person to whom is owed a monetary obligation of the type described in clause (b) of the definition of financial account;

“**deposit account**” means an account maintained by a financial institution for a person identified in the records of the financial institution as its customer to which deposits to, or funds received or held by, that financial institution are or may be credited, including a deposit account in any form (whether demand, term, cash, chequing or savings, and whether or not evidenced by a certificate of deposit, account agreement, passbook or other document), an investment account, a custody account and a clearing or settlement account, but does not include investment property and a monetary obligation evidenced by chattel paper or an instrument;

“**financial account**” means:

- (a) a deposit account other than a consumer account; and
- (b) a monetary obligation, whether or not conditional or contingent, of a financial institution to any person, whether or not identified in the records of the financial institution as its customer, in respect of funds received or held by that financial institution for the purpose of securing an obligation to that financial institution or to another person, but does not include investment property, consumer accounts and any monetary obligation evidenced by chattel paper or by an instrument;

“**financial institution**” means:

- (a) a bank;
- (b) a savings bank;
- (c) a loan company;

- (d) a savings and loan association;
- (e) a treasury branch;
- (f) a trust company;
- (g) a caisse populaire, credit union, cooperative credit society or association of credit unions, caisses populaires or cooperative credit societies;
- (h) an insurance company;
- (i) a clearing or settlement agency or central counterparty;
- (j) a central bank;
- (k) an entity engaged in:
 - (i) brokering, dealing in, executing, clearing or settling securities, futures, options on futures or derivatives on behalf of others;
 - (ii) providing trustee or custodial services; or
 - (iii) otherwise engaged in the business of providing financial services or maintaining accounts for customers;
- (l) a pension fund, including a trustee, manager or administrator of a pension fund;
- (m) a trustee or an entity that is a mutual fund or other collective investment vehicle;
- (n) a municipal corporation in Canada, the Crown in right of Ontario or any other province, territory or other political sub-division of Canada, the Crown in right of Canada, or any agency thereof; and
- (o) such other entity or entity within a class of entities as may be designated by Order in Council to be a financial institution for the purposes of this definition;

regardless of the jurisdiction of organization or incorporation, except as specifically provided in clause (n);

2. Add to subsection 1(2):

- (f) a secured party has control of a financial account if:

(i) the secured party is the financial institution that is obligated to the customer under the financial account;

(ii) the customer, the secured party and the financial institution that is obligated to the customer under the financial account have agreed in writing that the financial institution will comply with instructions originated by the secured party directing disposition of funds from the financial account without further consent by the customer; or

(iii) the secured party is the customer with respect to the financial account; and

(g) a secured party that has satisfied the requirements of subparagraph (f) has control of the financial account even if the customer, a debtor or any other person retains the right to direct the disposition of funds from that financial account or substitute other collateral for those funds.

3. Amend subsection 7.1(5) as follows:

Matters governed by law of debtor's jurisdiction

(5) The law of the jurisdiction in which the debtor is located governs,

(a) perfection of a security interest in investment property or a financial account by registration;

(b) perfection of a security interest in investment property granted by a broker or securities intermediary where the secured party relies on attachment of the security interest as perfection; and

(c) perfection of a security interest in a futures contract or futures account granted by a futures intermediary where the secured party relies on attachment of the security interest as perfection.

4. Add to section 7.1:

Conflict of laws - validity of security interest in financial account

(8) The validity of a security interest in a financial account shall be governed by the law, at the time the security interest attaches, of the financial institution's jurisdiction.

Conflict of laws – perfection and priority of security interest in financial account

(9) Except as otherwise provided in subsection (5), perfection, the effect of perfection or non-perfection, and the priority of a security interest in a financial account shall be governed by the law of the financial institution's jurisdiction.

Determination of financial institution's jurisdiction

(10) For purposes of this section, the following rules determine a financial institution's jurisdiction in relation to a financial account:

1. If an agreement between the financial institution and its customer governing a financial account expressly provides that a particular jurisdiction is the financial institution's jurisdiction in relation to that financial account for purposes of the law of that jurisdiction, this Act or any provisions of this Act, the jurisdiction expressly provided for in the agreement is the financial institution's jurisdiction.
2. If paragraph 1 does not apply and an agreement between the financial institution and its customer governing the financial account expressly provides that the agreement shall be governed by the law of a particular jurisdiction, that jurisdiction is the financial institution's jurisdiction.
3. If neither paragraph 1 nor paragraph 2 applies and an agreement between the financial institution and its customer governing the financial account expressly provides that the financial account is held or maintained at an office in a particular jurisdiction, that jurisdiction is the financial institution's jurisdiction.
4. If none of the preceding paragraphs applies, the financial institution's jurisdiction is the jurisdiction in which the office identified in statements delivered by the financial institution to the customer is located.
5. If none of the preceding paragraphs applies, the financial institution's jurisdiction is the jurisdiction in which the chief executive office of the financial institution is located or, in the case of the Crown, in which its legislative branch is located.

5. Amend subsection 8(1) as follows:

Procedural and substantive issues

8. (1) Despite sections 5 to 7.3,

(a) procedural issues involved in the enforcement of the rights of a secured party against collateral are governed by the law of the jurisdiction in which the enforcement rights are exercised; ~~and~~

(b) substantive issues involved in the enforcement of the rights of a secured party against collateral are governed by the proper law of the contract between the secured party and the debtor; and

(c) other than the rights referred to in subparagraphs (a) and (b), the rights and duties of a secured party with respect to collateral in its possession or control and any rights or obligations arising from a breach of any of such rights and duties is governed by the proper law of the contract between the secured party and the debtor.

6. Amend subsection 11(2) as follows:

When security interest attaches to collateral

(2) Subject to section 11.1, a security interest, including a security interest in the nature of a floating charge, attaches to collateral only when value is given, the debtor has rights in the collateral or the power to transfer rights in the collateral to a secured party and,

(a) the debtor has signed a security agreement that contains,

(i) a description of the collateral sufficient to enable it to be identified, or

(ii) a description of collateral that is a security entitlement, securities account or futures account, if it describes the collateral by any of those terms or as investment property or if it describes the underlying financial asset or futures contract;

(b) the collateral is not a certificated security and is in the possession of the secured party or a person on behalf of the secured party other than the debtor or the debtor's agent pursuant to the debtor's security agreement;

(c) the collateral is a certificated security in registered form and the security certificate has been delivered to the secured party under section 68 of the Securities Transfer Act, 2006 pursuant to the debtor's security agreement; ~~or~~

(d) the collateral is investment property and the secured party has control under subsection 1 (2) pursuant to the debtor's security agreement; or

(e) the collateral is a financial account, the security agreement is in writing and signed by the debtor and the secured party has control under subsection 1(2) pursuant to that security agreement and it contains:

(i) a description of the financial account sufficient to enable it to be identified, or

(ii) a description of the financial account that describes it as such.

7. Add a new section 17.2:

Rights and duties with respect to financial account

17.2 (1) Unless the financial institution otherwise agrees in writing, a financial institution's rights and duties with respect to a financial account are not terminated, suspended, or modified by:

- (a) the creation, attachment, or perfection of a security interest in the financial account;
- (b) the financial institution's knowledge of the security interest; or
- (c) the receipt by the financial institution of instructions from the secured party.

Right to refuse to enter into control agreement

(2) This section does not require a financial institution to enter into an agreement of the kind described in subclause 1(2)(f)(ii) even if the customer so requests or directs.

Obligation to disclose existence of control agreement

(3) A financial institution that has been requested to confirm the existence or non-existence of an agreement of the kind described in subclause 1(2)(f)(ii) by a judgment creditor or other person who has an interest in the collateral shall:

- (a) request consent from the customer to confirm the existence or non-existence of the agreement to the person if it has not already obtained that consent as a term of the security agreement or otherwise; and
- (b) if it has or obtains the consent of that customer, confirm the existence or non-existence of the agreement to the person making the request.

8. Add to section 22.1:

(3) A security interest in a financial account may be perfected by control of the financial account under subsection 1(2).

(4) A security interest in a financial account is perfected by control from the time the secured party obtains control and remains perfected by control until the secured party does not have control.

9. Amend section 29 as follows:

29. The rights of a person who is,

(a) a holder in due course of a bill, note or cheque within the meaning of the *Bills of Exchange Act* (Canada); or

(b) a transferee from the debtor of money **or funds in any currency received by way of credit transfer,**

are to be determined without regard to this Act.

10. Amend section 30.1 as follows:

Priority rules for security interests in investment property and financial account

30.1 (1) The rules in this section govern priority among conflicting security interests in the same investment property **or financial account.**

Secured party with control

(2) A security interest of a secured party having control of investment property **or a financial account** under subsection 1(2) has priority over a security interest of a secured party that does not have control of the investment property **or financial account.**

Certificated security perfected by delivery

(3) A security interest in a certificated security in registered form which is perfected by taking delivery under subsection 22 (2) and not by control under section 22.1 has priority over a conflicting security interest perfected by a method other than control.

Rank by priority in time

(4) Except as otherwise provided in subsections (5), ~~and (6),~~ **(6.1) and (6.2),** conflicting security interests of secured parties each of which has control under subsection 1(2) rank according to priority in time of,

- (a) if the collateral is a security, obtaining control;
- (b) if the collateral is a security entitlement carried in a securities account,
 - (i) the secured party's becoming the person for which the securities account is maintained, if the secured party obtained control under clause 25(1)(a) of the *Securities Transfer Act, 2006*,
 - (ii) the securities intermediary's agreement to comply with the secured party's entitlement orders with respect to security entitlements carried or to be carried in the securities account, if the secured party obtained control under clause 25(1)(b) of the *Securities Transfer Act, 2006*, or
 - (iii) if the secured party obtained control through another person under clause 25(1)(c) of the *Securities Transfer Act, 2006*, when the other person obtained control; ~~or~~
- (c) if the collateral is a futures contract carried with a futures intermediary, the satisfaction of the requirement for control specified in subclause 1(2)(d)(ii) with respect to futures contracts carried or to be carried with the futures intermediary. ~~or~~

(d) if the collateral is a financial account,

(i) the secured party becoming the customer in relation to the financial account, if the secured party obtained control under subclause 1(2)(f)(iii), or

(ii) the financial institution's agreement to comply with the secured party's instructions with respect to funds in the financial account, if the secured party obtained control under subclause 1(2)(f)(ii).

Securities intermediary

(5) A security interest held by a securities intermediary in a security entitlement or a securities account maintained with the securities intermediary has priority over a conflicting security interest held by another secured party.

Futures intermediary

(6) A security interest held by a futures intermediary in a futures contract or a futures account maintained with the futures intermediary has priority over a conflicting security interest held by another secured party.

Financial institution

(6.1) Subject to subsection (6.2), a security interest held by a financial institution in a financial account that is an obligation of the financial institution has priority over a conflicting security interest in the financial account held by another secured party.

Same

(6.2) A security interest in a financial account in relation to which the secured party has obtained control under subclause 1(2)(f)(iii) has priority over a security interest held by the financial institution that is obligated under that financial account, except for any security interest granted by the secured party in favour of the financial institution.

Interests granted by broker, intermediary

(7) Conflicting security interests granted by a broker, securities intermediary or futures intermediary which are perfected without control under subsection 1 (2) rank equally.

Priority determined under s. 30

(8) In all other cases, priority among conflicting security interests in investment property **and a financial account** shall be governed by section 30.

11. Amend section 40 as follows:

Account debtor

40. (1) In this section,

“account debtor” means a person obligated on an account, **a financial account** or ~~on~~ chattel paper;

“assign” and “assignment” includes the creation of a security interest in any form;⁹

⁹ Many (perhaps most) security agreements that create a security interest in accounts do so by way of assignment of the account. There should not, however, be a distinction between the position of a secured creditor to whom an account is assigned and one to whom a security interest is granted. These amendments ensure that the account debtor defences apply to all persons who take an interest in an account regardless of the method of taking that interest.

“assignee” includes a secured party with a security interest in an account or a financial account, whether or not the security interest was granted by way of an assignment or otherwise; and

“assignor” includes a person that has granted a security interest in an account or a financial account, to an assignee whether or not the security interest was granted by way of an assignment or otherwise.

Defences available against assignee

(1.1) An account debtor who has not made an enforceable agreement not to assert defences arising out of the contract between the account debtor and the assignor may set up by way of defence against the assignee,

(a) all defences available to the account debtor against the assignor arising out of the terms of the contract or a related contract, including **contractual rights of set-off**, equitable set-off and misrepresentation; and

(b) the right to set off any debt owing to the account debtor by the assignor that was payable to the account debtor before the account debtor received notice of the assignment.¹⁰

Same

(1.2) For greater certainty, the priority rules in sections 20 and 30 do not affect the defences and rights of the account debtor referred to in subsection (1.1).

Payment by account debtor

(2) An account debtor may pay the assignor until the account debtor receives notice, reasonably identifying the relevant rights, that the account, **financial account** or chattel paper has been assigned, and, if requested by the account debtor, the assignee shall furnish proof within a reasonable time that the assignment has been made, and, if the assignee does not do so, the account debtor may pay the assignor.

Modification, etc., effective against assignee

(3) To the extent that the right to payment or part payment under an assigned contract has not been earned by performance, and despite notice of the assignment, any modification of or substitution for the contract, made in good

¹⁰ Part (b) relates to legal set-off, not contractual or equitable set-offs. Legal set-off is cut-off once notice of assignment is received. That is not true of contractual or equitable set-off. Hence, the distinction between (a) and (b).

faith and in accordance with reasonable commercial standards and without material adverse effect upon the assignee's right under or the assignor's ability to perform the contract, is effective against an assignee unless the account debtor has otherwise agreed, but the assignee acquires corresponding rights under the modified or substituted contract.

Prohibition or restriction on assignment

(4) A term in the contract between the account debtor and the assignor that prohibits or restricts the assignment of, or the giving of a security interest in, the whole of the account, **financial account** or chattel paper for money due or to become due or that requires the account debtor's consent to such assignment or such giving of a security interest,

(a) is binding on the assignor only to the extent of making the assignor liable to the account debtor for breach of their contract; and

(b) is unenforceable against third parties.

12. Amend subsection 56(7) as follows:

No outstanding secured obligation

(7) Where there is no outstanding secured obligation, and the secured party is not committed to make advances, incur obligations or otherwise give value, a secured party having control of investment property under clause 25(1)(b) of the *Securities Transfer Act, 2006* or subclause 1(2)(d)(ii) of this Act **or control of a financial account under subclause 1(2)(f)(ii) of this Act**, shall, within 10 days after receipt of a written demand by the debtor, send to the securities intermediary or futures intermediary with which the security entitlement or futures contract is maintained, **or to the financial institution that is obligated under the financial account**, a written record that releases the securities intermediary, ~~or~~ futures intermediary **or financial institution** from any further obligation to comply with entitlement orders, ~~or~~ directions **or instructions** originated by the secured party

13. Amend section 61 as follows:

Collection rights of secured party

61. (1) Where so agreed and in any event upon default under a security agreement, a secured party is entitled,

(a) to notify any person obligated on an account, **a financial account** or ~~on~~ chattel paper or any obligor on an instrument to make payment to the

DRAFT - DECEMBER 21, 2011

secured party whether or not the assignor was theretofore making collections on the collateral;~~and~~

(b) to take control of any proceeds to which the secured party is entitled under section 25; and

(c) to apply the balance of an account or a financial account to the obligation secured by that collateral.

Idem

(1.1) Unless otherwise agreed by the parties, a secured party may exercise a right of recoupment, compensation, set-off or consolidation against an account or a financial account to satisfy an obligation owed to the secured party whether or not the security interest in that collateral has been perfected by control.

Idem

(2) A secured party who by agreement is entitled to charge back uncollected collateral or otherwise to full or limited recourse against the debtor and who undertakes to collect from a person obligated on an account or on chattel paper or an obligor on an instrument shall proceed in a commercially reasonable manner and the secured party may deduct the reasonable expenses of realization from the collections.

14. Amend section 63(7) as follows:

Notice not required

(7) The notice mentioned in subsection (4) is not required where,

(a) the collateral is perishable;

(b) the secured party believes on reasonable grounds that the collateral will decline speedily in value;

(c) the collateral is of a type customarily sold on a recognized market;

(d) the cost of care and storage of the collateral is disproportionately large relative to its value;

(e) for any reason not otherwise provided for in this subsection, the Superior Court of Justice, on an application made without notice to any other person, is satisfied that a notice is not required;

(f) after default, every person entitled to receive a notice of disposition under subsection (4) consents in writing to the immediate disposition of the collateral; ~~or~~

(g) a receiver and manager disposes of collateral in the course of the debtor's business; or

(h) the collateral is a financial account.

DRAFT - DECEMBER 21, 2011

PART 3 - EXPLANATORY NOTES

New Class of Collateral

The amendments propose creating a new class of collateral – the *financial account*. While “financial accounts” are excluded from the definition of “account”, this new class of collateral is in effect a sub-type of that existing broader class of collateral.¹¹ An account is essentially a monetary obligation, although one that is not within other defined collateral classes, such as investment property, chattel paper or instruments.

A *financial account* is either a deposit account maintained by a financial institution for a customer (other than a consumer account), or a monetary obligation of a financial institution related to any funds received or held by the financial institution as security. The second branch of the definition ensures that all cash collateral arrangements in which a financial institution receives or holds cash can be perfected by control, even if the financial institution does not formally maintain a deposit account and even if the funds received or held by the financial institution are used by it in its business.

Financial institution is defined widely to include any type of financial entity that would maintain deposit accounts for customers, or would otherwise receive or hold cash collateral as security. It is important not to restrict the definition to Canadian regulated institutions because Canadian debtors deal with institutions outside of Canada from their operations outside of Canada, contexts in which Canadian regulatory jurisdiction does not apply. It is not necessary in the case of a financial account that the account be established specifically for the purpose of providing or holding cash collateral.¹² The definition of “financial institution” intends to encompass all of the significant players in Canadian financial markets transactions, including the Crown, pension funds and mutual funds. While these types of entities would not typically maintain deposit accounts for customers, they do receive or hold cash collateral to secure obligations.

Consumer accounts are excluded from the definition of financial account. This exclusion parallels a similar exclusion from the scope of Article 9 of the UCC¹³.

¹¹ PPSA, s.1(1).

¹² The financial account is a wider class of collateral than the deposit account collateral class defined by Revised Article 9 of the Uniform Commercial Code. It covers a wider class of account and a wider class of financial institution.

¹³ UCC §9-109(d)(13) provides that Article 9 does not apply to “an assignment of a deposit account in a consumer transaction”.

Attachment

A cash collateral arrangement will usually be provided for in a security agreement that will describe the collateral by reference to the transferred or deposited funds or the financial account itself. Attachment will in those circumstances arise in the normal fashion.

The amendments provide that attachment with respect to a financial account will occur upon the secured party obtaining control.¹⁴ A requirement has been added with respect to a financial account that the security agreement creating the security interest in the account be in writing.¹⁵

Perfection by Control

The amendments provide that a secured party may perfect a security interest in a financial account in two ways – by registration (as already provided for in the PPSA)¹⁶ and by control.¹⁷ The definition of control with respect to a financial account parallels the definitions of control with respect to a securities account and a futures account.

With respect to a financial account, there will be three means of obtaining control.

Automatic Control. First, the secured party will automatically have control if it is the financial institution that is obligated to a customer to pay the financial account.¹⁸ This parallels the means of control for a securities account in which the securities intermediary maintaining the account has a security interest or a futures account in which the futures intermediary has a security interest.¹⁹

Control Agreements. Second, if the financial account is with a third party financial institution (or the financial institution is acting in more than one capacity), the secured party, debtor and financial institution may agree in writing that the financial institution will comply with instructions originated by the secured party directing disposition of the funds from the account without further consent of the customer.²⁰ This parallels a means of control with respect to a securities

¹⁴ New subclause 11(2)(e).

¹⁵ New subclause 11(2)(e).

¹⁶ This requires one minor amendment to section 7.1(5)(a) to add financial accounts.

¹⁷ New subsection 22.1(3).

¹⁸ New subclause 1(2)(f)(i).

¹⁹ STA, s.26; PPSA, s.1(2)(d)(i).

²⁰ New subparagraph 1(2)(f)(ii).

account and a futures account maintained with a third party securities intermediary and futures intermediary respectively.²¹ It will validate blocked account agreements, already in widespread use in Canada, as a means of perfection. Further, this means of perfection will allow, for example, a debtor that has entered into derivatives contracts and securities loans with a Canadian bank to use its financial account balances with the bank's related U.S. subsidiary bank or securities dealer as collateral.

Transfer to the Financial Institution's Account. Third, a secured party will have control if it is the customer with respect to the financial account.²² This parallels a means of control with respect to a securities account.²³ The secured party will have control if funds are transferred to a financial account of the secured party at a third party financial institution.

In certain circumstances the debtor will have the right to direct the disposition of funds from the financial account or to substitute a different form of collateral. To ensure that conferring or exercising this type of right does not compromise the secured party's control of the financial account, the PPSA would include a provision acknowledging that such actions do not compromise control.²⁴ This provision would parallel the similar provision with respect to certificated and uncertificated securities and securities accounts.²⁵

Priority

A secured party with control of a financial account will have priority over a secured party that does not have control.²⁶

If the financial account is an obligation of a financial institution which is itself the secured party, then that financial institution will have priority over a conflicting security interest of any other party,²⁷ other than a secured party that attains control by becoming the financial institution's customer.²⁸

²¹ STA, s.25(1)(b) and PPSA, s.1(2)(d)(ii).

²² New subclause 1(2)(f)(iii).

²³ STA, s.25(1)(a).

²⁴ Subparagraph 1(2)(g).

²⁵ STA, s.23(2), s.24(2) and s.25(2).

²⁶ Amendment to subsection 30.1(1) and 30.1(2).

²⁷ New subsection 30.1(6.1).

²⁸ New subsection 30.1(6.2). The priority over the financial institution given in this subsection to a secured party that obtains control by becoming the financial institution's customer (which follows a corresponding provision in UCC Article a) is included for greater certainty since

Otherwise, the temporal order of obtaining control will determine priority between secured creditors with control of financial accounts.²⁹

These provisions substantially parallel the similar provisions with respect to investment property.³⁰

Finality of Transfers of Funds

Section 29 is intended to indicate that the rights of any transferee of money subject to a security interest will be determined under the common law and without regard to the provisions of the PPSA. While the common law with respect to transfers of electronic funds is not as developed as for currency, there is support for the position that the same common law rule that applies to transfers of currency applies to the transfer of electronic credits.³¹ The rule is that a transferee of funds takes free of any adverse claims to the funds (including any security interest) if it acted in good faith and did not have notice of the adverse claim. If this rule did not exist, the certainty and reliability of money as a means of payment would be substantially eroded. The PPSA could be amended to clarify that the common law rules applicable to money (i.e., currency) apply also to electronic funds transfers, but further study of this may be required, so it is not recommended at this time. The expectation is that the common law will eventually develop to create a consistent rule for currency and electronic funds transfers.³²

Conflict of Laws – Validity, Perfection and Priority

The proposed conflict of laws rule for validity, perfection and priority is that these matters will be governed by the law of the financial institution's

ordinarily two security interests will be in different accounts if the financial institution has a security interest in the account of a customer that is also the debtor of another secured party. A new asset is created if the secured party becomes the customer of the financial institution.

²⁹ New subclause 30.1(4)(d).

³⁰ PPSA section 30.1.

³¹ Case law and commentary supporting the application of the common law rule with respect to currency to other electronic credit transfers is: *R. v. Canadian Imperial Bank of Commerce* (2000), 51 O.R. (3d) 257 (C.A.); *Bank of Montreal v. iTrade Finance Inc.*, 2009 ONCA 615, 252 O.A.C. 291; Bradley Crawford, Q.C., *The Law of Banking and Payment in Canada*, looseleaf (Aurora, Ont.: Canada Law Book, 2008) at 3:20.10(2) and para. 3:40.10(4)(d)(i); *Indian Head Credit Union v. Andrew* (1992), 97 D.L.R. (2d) 196 (Sask. C.A.); *Transamerica Commercial Finance Corp., Canada v. Royal Bank of Canada* (1990), 70 D.L.R. (4th) 627 (Sask. C.A.); *Flexi-coil Ltd. v. Kindersley District Credit Union Ltd.* (1993), 113 Sask. R. 298 (C.A.).

³² The proposed rules with respect to financial accounts deal with security interests in the accounts themselves, not the funds that were transferred to the accounts.

jurisdiction, as determined by a cascade of rules that look chiefly to the terms of the agreement that governs the financial account. The advantage of this approach is that the rule parallels that which applies to securities accounts and futures accounts and consequently credit balances in a securities account will be dealt with in a fashion similar to credit balances in a financial account. It may not always be easy to distinguish between a financial account and a securities account that is used primarily to hold cash margin. A consistent conflict of laws rule would therefore be helpful. Also, it is consistent with the Article 9 approach and therefore will not lead to two different applicable jurisdictions with respect to accounts held outside of Canada. These rules will apply to financial accounts generally.

Conflict of Laws – Care and Custody of Collateral

There is no conflict of laws rule in the PPSA to determine the law governing the types of issues referred to in sections 17 and 17.1. Given the importance of rehypothecation rights in international financial markets, particularly with respect to cash collateral and investment property, it would be helpful to have an express conflict of laws rule for these issues. We recommend the proper law of the contract between the secured party and the debtor (which currently applies to substantive issues involved in the enforcement of the security interest against the collateral).

Rights of the Secured Party

The Proposal does not amend section 17.1 to refer to financial accounts because we consider that the secured party would have the right to deal with funds received by it as it sees fit, unless it has otherwise agreed with the debtor.

Financial Institution's Rights and Duties

Unless the financial institution otherwise agrees, its rights and duties with respect to a financial account it maintains or owes should not be affected by a security interest in the financial account.³³ For example, if the financial institution otherwise has a right of set-off against the account, it will be permitted to exercise that right unless it has waived it.

A financial institution would not be obligated to enter into a control agreement with a secured party. This rule parallels the STA approach to securities accounts and futures accounts.³⁴

³³ New subsection 17.2(1).

³⁴ New subsection 17.2(2).

A financial institution will be required to confirm the existence of the control agreement with respect to a financial account to another person if requested to do so by the account customer with respect to the account.³⁵ It will also be obligated to request that consent from the account customer if it is requested by a judgment creditor or other person with an interest in the financial account. These provisions deviate somewhat from those with respect to a securities intermediary and a securities account in order to address concerns raised regarding secret liens, but they balance that concern against the financial institution's confidentiality obligations.³⁶

Enforcement

In the case of a financial account where the financial institution is the secured party, the means of enforcement is to apply the balance of the account to the secured obligations. Although practically speaking this closely resembles the financial institution's right of set-off or consolidation of accounts, it is a conceptually distinct remedy (assuming the *Caisse Drummond* analysis is applied to the right) when applied to realization of a security interest. In the case of a financial account at a third party financial institution, the means of enforcement is to allow the secured party to direct the disposition of the account balance. Amendments will recognize that these are permitted means of enforcement regardless of the method of perfection.³⁷

Secured Party's Right of Set-off

New subsection 61(1.1) will recognize that a secured party with an existing right of set-off against a financial account will be entitled to exercise that right without being required to demonstrate that it had a security interest perfected by control. This provision confirms the common-law understanding that rights of set-off, consolidation of accounts and similar rights exist apart from, and are not to be regarded as, security interests; and the amendments are not intended to interfere with such otherwise enforceable rights.

³⁵ New subsection 17.2(2).

³⁶ STA, s.28(2) and (3).

³⁷ New subclauses 61(1)(c) and (d).