

# STIKEMAN ELLIOTT

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## Toronto Memorandum

**To:** ISDA Canadian Legal and Regulatory Affairs Committee  
**From:** Margaret Grottenthaler  
**Re:** Filing of Financing Statements re Cash/Credit Support  
**Date:** May 4, 2010

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Attached is a revised set of guidelines reflecting the comments made in our meeting in February regarding developing a consensus on best practices with respect to protecting the Collateral Taker's interest in Cash in light of the Supreme Court of Canada decision in *Caisse Desjardins de l'Est du Drummond v. Canada*.

The subcommittee which was struck at the February meeting met to consider alternative structures for Cash collateral. That committee met and decided to further examine a potential solution that may work for Canadian institutions as collateral takers that would involve investment of cash collateral in debt securities of the Canadian institution. A report on this potential solution is being prepared and will be distributed separately.

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## ISDA Canadian Legal and Regulatory Affairs Committee

### Endorsed Practices with respect to Cash Credit Support for Collateral Providers located in Canada ("Cash Providers")

These guidelines have been endorsed by the Canadian Legal and Regulatory Affairs Committee of ISDA. No member is bound to agree to or implement these guidelines. They are intended to express a reasonable approach to the issue of perfection with respect to Credit Support in the form of Cash in light of certain uncertainties under Canadian personal property security law.

1. With respect to any Cash Provider located in Canada, it may be advantageous<sup>1</sup> to continue to make the Canadian amendments with respect to Cash under the New York law form of Credit Support Annex (NY CSA) as recommended by the Canadian ISDA Opinion on the Credit Support Documents dated December 31, 2009 (the **Canadian Collateral Opinion**), and to otherwise be consistent in the documentation with the debtor/creditor and set-off characterization of the relationship that exists with respect to Cash.
2. In light of the increased characterization risk arising from the Supreme Court of Canada decision in *Caisse Desjardins de l'Est du Drummond v. Canada*<sup>2</sup> it is recommended that a financing statement be filed in *Personal Property Security Act* (PPSA) jurisdictions in which the Cash Provider is located, whether using the NY CSA (with the recommended amendments to the CSA)<sup>3</sup> or Transfer Annex.
3. Registration of a financing statement is recommended for new and existing relationships.<sup>4</sup>
4. If the recommended amendments are made to the CSA, the risk of characterization of the Cash arrangements (not in a securities account) as creating a movable hypothec without delivery or any other Quebec law equivalent of a security interest which would require registration in order to be opposable to third parties (perfected) is not material. Therefore it is not necessary to create a Quebec form of hypothec or to register in

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<sup>1</sup> Retaining the ability to argue that the *Drummond* case is distinguishable and that no security interest is created in the cash is advantageous even if the collateral taker files a financing statement and has the first relevant registration. Parties will be able to argue that the interest is not subject to statutory lien claims that would otherwise have a priority and not being subject to the PPSA avoids the realization procedures of and other potential limitations under the PPSA.

<sup>2</sup> [2009] 2 S.C.R. 94 (S.C.C.)

<sup>3</sup> It also continues to be necessary to file a financing statement if the recommended amendments are not made.

<sup>4</sup> In Ontario the appropriate collateral types would be Accounts and Other.

Quebec. See the more detailed analysis of this issue in the Stikeman Elliott Quebec law opinion with respect to the CSAs.

5. Where a description of the collateral is included in the registration statement it would be appropriate in Ontario to frame it in such a way that it would not add weight to the argument that a security interest was created in the Cash.<sup>5</sup> In Ontario, an acceptable description is:

filed as a precaution only [with respect to certain classes of property]<sup>6</sup> without prejudice to the agreement of the parties that no security interest has been created in [the/certain classes of]<sup>7</sup> personal property under the Credit Support Annex to the ISDA Master Agreement dated as of [●], as amended, supplemented, restated or replaced from time to time.<sup>8</sup>
6. Alternatively or additionally, a similar acknowledgment could be included in the CSA to the effect that any financing statement filed with respect to Other Eligible Support is filed as a precaution only without prejudice to the agreement of the parties that no security interest has been created in the Other Eligible Support. For provinces that require collateral descriptions in specified formats (e.g. Alberta), it may be preferable to include the description only in the CSA.
7. Given the lack of legal certainty, the Collateral Taker will have to decide based on its assessment of legal risk and business expediency whether it will take the additional steps of obtaining PPSA search reports and waivers or estoppel letters from prior registrants disclosed by the reports

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<sup>5</sup> While there is a provision in the Ontario PPSA that provides that the registration of a financing statement does not give rise to a presumption that the PPSA applies (s.46(5)(b)), in light of the factually sensitive nature of the characterization exercise, it may potentially be of some benefit to the "secured party" to make clear its intention that no security interest is intended. Also, other provincial PPSAs do not include the equivalent of s.46(5)(b).

<sup>6</sup> This [ ] language may be deleted if Cash is the only form of eligible credit support. Include it if you also have a security interest in securities. While a security interest in that type of collateral may be perfected by control, a secured party is also permitted to perfect by registration and if a registration is being made in any event this description should not preclude reliance on the registration should that prove to be advantageous.

<sup>7</sup> Use "the" if Cash is the only form of eligible credit support and "certain classes of" if you also have a security interest in securities collateral or other collateral.

<sup>8</sup> Other provinces specifically require collateral descriptions. The description for Alberta for example would not include the cautionary language, except in the Agreement, and the description would be:

"Intangibles, Accounts, Money

Proceeds: goods, chattel paper, investment property, documents of title, instruments, money and intangibles"

who potentially have a security interest in accounts. We refer members to Question 16 of the Canadian Collateral Opinion and its conclusion that section 40(1.1) of the Ontario PPSA and s.41(2) of the Alberta PPSA should be effective as against any competing consensual secured creditors, including secured creditors with prior registrations.<sup>9</sup>

8. With respect to existing relationships, Collateral Takers intending to file financing statements may find it useful to communicate their intention to make the filing to the Collateral Provider.<sup>10</sup>

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<sup>9</sup> Registration is recommended for a number of reasons (eg. effectiveness as against non-consensual secured creditors, a trustee in bankruptcy or other creditor representative that may not be an “assignee”) and consequently it would not be logically inconsistent to file, yet not do searches or obtain waivers with respect to consensual PPSA type secured creditors.

<sup>10</sup> A communication along the following lines could be provided:

“As you may know, the decision of the Supreme Court of Canada in *Caisse Desjardins de l’Est du Drummond v. Canada* from June of 2009 characterized a set-off arrangement as creating a security interest for certain purposes. In light of the case we have determined that it is advisable, as a precaution, to file a financing statement under the Personal Property Security Act registration system in the jurisdiction of your chief executive office in order to ensure that our rights with respect to cash collateral are fully protected. This is a step endorsed by [the Canadian Legal and Regulatory Affairs Committee of] ISDA. We propose to file a financing statement in [insert relevant province] with respect to [insert agreement]. In order not to compromise the position that our title transfer arrangement with respect to cash does not create a security interest, the financing statement will state in the description that it is filed with respect to our agreement with you and as a precaution only, without prejudice to our agreement that no security interest has been created in any or certain classes of personal property under the agreement. Please let us know if we should send the verification statement with respect to the filing to a person other than the addressee for notices under the agreement. We have assumed that your chief executive office is located in [insert province]. Please advise if this is not the case.”