

<b><i>SUMMARY OF CURRENT DOCUMENT</i></b>	
<b>Name of Issuing Party or Person:</b>	<b>John Deere Limited and John Deere Credit Inc.</b>
<b>Date of Document:</b>	<b>7 February 2003</b>
<b>Summary of Order/Relief Sought or Statement of Purpose in filing:</b>	<b>Reply Memorandum of Fact and Law of John Deere Credit Inc. to the Interlocutory Application (Inter Partes) of Contract Funding Group Inc.</b>
<b>Court Sub-File Number:</b>	<b>7:42</b>

**2002 01T 0352**

**IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR**

**IN THE MATTER OF**

A Court ordered Receivership  
of Hickman Equipment (1985) Limited  
("Hickman Equipment") pursuant to Rule 25  
of the *Rules of the Supreme Court, 1986*  
under the *Judicature Act*, RSNL 1990,  
c. J-4, as amended

**AND IN THE MATTER OF**

the *Bankruptcy and Insolvency Act*,  
RSC 1985, c. B-3, as amended

**MEMORANDUM OF FACT AND LAW OF**  
**JOHN DEERE CREDIT INC. ("JDCI")OR "DEERE")**

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**MEMORANDUM OF FACT AND LAW OF**  
**JOHN DEERE CREDIT INC. ("JDCI")OR "DEERE")**

1. Deere files this Memorandum of Fact and Law in response to the Interlocutory Application (Inter Partes) of Contract Funding Group Inc. ("CFG"), for (i) a determination of its priority and entitlement, vis-à-vis other claimants, to the proceeds from the sale of the following assets (the "Claimed Unit") of Hickman Equipment, and (ii) for an order that the Receiver pay the auction proceeds from the sale of the Claimed Unit to CFG:

<b>Make</b>	<b>Serial #</b>	<b>Proceeds</b>
John Deere Excavator	FF892EX012643	\$145,000.00

2. A Final Determination has been issued by the Trustee in respect of the claims of CFG (the “CFG Final Determination”).

**Reference:** Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit “U”.

3. JDCI has a valid security interest in the Claimed Unit, as further described below, and asserts a right, in priority to CFG, to receive the auction proceeds in respect thereof.

### **SUMMARY OF THE MAIN ASPECTS OF DEERE’S POSITION**

#### **CFG Has Not Established a PMSI in the Claimed Unit**

4. Deere submits that, if CFG wants to claim a purchase money security interest (“PMSI”) in the Claimed Unit, whether as original collateral or as proceeds, the onus is on CFG to prove entitlement to rely on section 35(2) of the Personal Property Security Act, SNL 1998, c. P-7.1 (the “PPSA”) to assert priority of its security interest over other creditors of Hickman Equipment.

**Reference:** Dubé v. Bank of Montreal (1986) 27 D.L.R. (4<sup>th</sup>) 718 (Sask. C.A.);

Canadian Imperial Bank of Commerce v. Marathon Realty Co. (1987), 40 D.L.R. (4<sup>th</sup>) 326 (Sask. C.A.).

5. In order to claim that a security interest is a PMSI, CFG must first prove that the security interest meets the definition of purchase money security interest contained in s. 2 (hh) of the PPSA. Then, in order to avail itself of the special priority that is potentially available for a PMSI, CFG must also establish that

it has met the requirements of section 35(2) of the PPSA with respect to that security interest.

**Reference:** PPSA, sections 2(hh) and 35(2).

6. In respect of the Claimed Unit, CFG has provided no evidence whatsoever to demonstrate that its security interest meets the definition of a “purchase money security interest” in section 2(hh) of the PPSA. In addition, CFG has provided no evidence whatsoever that it complied with the requirements of section 35(2) of the PPSA. It is therefore submitted that CFG cannot claim priority over the Claimed Unit as a holder of a purchase money security interest.

**Reference:** PPSA, sections 2(hh) and 35(2).

### **Residual Priority Rules**

7. Section 36(1) to 36(5) of the PPSA reads:

*“36.(1) Where this Act provides no other method for determining priority between competing security interests in the same collateral, the following priority rules apply:*

*(a) priority between perfected security interests is determined by the order of the occurrence of the following:*

*(i) the registration of a financing statement under section 26 without regard to the time of attachment of the security interest,*

*(ii) possession of the collateral under section 25 without regard to the time of attachment of the security interest, or*

*(iii) perfection under sections 6, 8, 27, 30 or 75,*

*whichever is the earliest;*

*(b) a perfected security interest has priority over an unperfected security interest; and*

*(c) priority between unperfected security interests is determined by the order of attachment of the security interests.*

(2) *For the purpose of subsection (1), a continuously perfected security interest shall be treated at all times as if perfected by the method by which it was originally perfected.*

(3) *For the purpose of subsection (1) and subject to section 29, the time of registration, possession or perfection of a security interest in original collateral is also the time of registration, possession or perfection of a security interest in its proceeds.*

(4) *A security interest in goods that are equipment and are of a kind that are prescribed as serial numbered goods is not registered or perfected by registration for the purpose of subsection (1), (7) or (8) or 35(1) unless a financing statement relating to the security interest that includes a description of the goods by serial number is registered.*

(5) *Subject to subsection (6), the priority which a security interest has under subsection (1) applies to all advances, including future advances.*

**Reference:** PPSA, sections 36(1) to 36(5).

8. The security interest of JDCI was perfected by the registration of a financing statement on 14 December 1999. Unless CFG otherwise establishes an entitlement to rank ahead of JDCI, the date of registration by JDCI is, in respect of the Claimed Unit, earlier than the date of registration of CFG, and pursuant to section 36, JDCI has priority over CFG.

#### **JDCI's PMSI**

9. JDCI has a valid purchase money security interest in the Claimed Unit.

**Reference:** Final Determination of the Trustee in respect of the claims of JDCI (the “JDCI Final Determination”), in particular, sections 2, 9B and 17, Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit “S”.

10. Purchase Money Security Interest Notices (“PMSI notices”) were sent by registered mail by JDCI on 14 December 1999 to CIBC Equipment Finance Ltd., Bombardier Capital Leasing Ltd., ABN Amro Bank Canada, Canadian Imperial Bank of Commerce and General Motors Acceptance Corporation of Canada, Limited.

**Reference:** Affidavit of Ernest G. Reid, Q.C., sworn 16 October 2002; PPSA, s. 70(2).

11. JDCI has priority over all other creditors as a holder of a purchase money security interest in respect of the Claimed Unit.

**Reference:** PPSA, s. 2(hh) and s. 35(2).

**Conclusion**

12. JDCI therefore requests that the Court declare that (1) the security interest of CFG in the Claimed Unit does not have priority, (2) the security interest of JDCI in the Claimed Unit has priority over CFG, and, (3) JDCI is entitled to payment of the auction proceeds therefrom.

**CLAIMED UNIT: JOHN DEERE EXCAVATOR S/N FF892EX012643****CFG's Security Interest**

13. CFG claims a security interest in the Claimed Unit as original collateral. The earliest date of perfection of CFG's security interest in the Claimed Unit is 31 January 2000.

**Reference:** CFG Final Determination, Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit "U".

14. Cyber Lease Corp. and Hickman Equipment entered into a sale and leaseback transaction in respect of the Claimed Unit. Although a registration was made by CFG on 11 June 1998, as Number 697920 under the Conditional Sales Act, RSNL 1990, c. C- 28 (repealed) (the "Conditional Sales Act"), no registration of the sale or chattel mortgage from Hickman Equipment to Cyber Lease Corp. was registered under the Bill of Sale Act, RSNL 1990, c. B-3 (repealed). Deere submits that CFG did not comply with the mandatory requirements of prior registration law, and that the transaction was therefore void against other creditors of Hickman Equipment.

**Reference:** CFG Final Determination, Affidavit of Bruce C. Grant, Exhibit "U";

Grand River Motors Ltd. v. Commercial Finance Corp.  
(1993) Carswell Ont 49 (S.C.C.).

15. In accordance with section 74(4) of the PPSA, the validity of a prior security interest is governed by prior law. A prior law security interest may only be continued under the PPSA if the requirements of prior registration law were complied with.

**Reference:** PPSA, sections 74(4) and 75(4).

16. It is submitted that CFG did enter, and intended to enter, into a sale and leaseback arrangement with Hickman Equipment, in circumstances in which there was no actual or continued change in possession of the collateral. CFG has provided no evidence that it ever took possession of the Claimed Unit and, in fact, for CFG to have taken possession of the Claimed Unit would have been contrary to the intent of the sale/leaseback arrangement, whereby CFG would finance the Claimed Unit and Hickman Equipment would maintain possession.
17. The bill of sale in respect of the Claimed Unit was not evidenced by a registered bill of sale and is therefore void as against a creditor and as against a subsequent purchaser or mortgagee claiming from or under Hickman Equipment in good faith for valuable consideration without notice whose conveyance or mortgage has been registered or is valid without registration.

**Reference:** Bills of Sale Act, section 5(1).

18. A “sale” under the Bills of Sale Act, and to which section 5(1) applies, is stated to include “a sale, assignment, transfer, conveyance, declaration of trust without transfer, or other assurance of chattels ***not intended to operate as a mortgage***, or an agreement, whether or not intended to be followed by the execution of another instrument, by which a right in equity to chattels is conferred, but does not include... (ii) a transfer or sale of goods in the ordinary course of a trade or calling” (emphasis added)

**Reference:** Bills of Sale Act, section 2(o).

19. A “mortgage” under the Bills of Sale Act, and to which section 5(1) applies, is stated to include “an assignment, transfer, conveyance, declaration of trust without transfer, or other assurance of chattels, ***intended to operate as a mortgage or pledge***, or a power or authority or licence to take possession of

chattels as security, or an agreement, whether or not intended to be followed by the execution of another instrument, by which a right in equity to a charge on chattels is conferred..." (emphasis added)

**Reference:** Bills of Sale Act, section 2(j).

20. It is submitted that the sale and lease documents in respect of the Claimed Unit (together referred to herein as the "Financing Documents") should not be characterized as "sales" under the Bills of Sale Act that are not intended to operate as a mortgage. On the contrary, the purpose of the Financing Documents was so that CFG would have a charge over the Claimed Unit, such that, upon payment of the amounts contemplated in the lease (including the nominal option purchase price) and fulfilling the other obligations secured, title would revert back to Hickman Equipment. The Financing Documents taken as a whole were intended to act as a mortgage. It is therefore submitted that the bill of sale in respect of the Claimed Unit, for the purposes of sections 2 (j) and 5(1) of the Bills of Sale Act, ought to be characterized as a "mortgage" in respect of which registration was required so as to be valid against creditors or subsequent purchasers or mortgagees of Hickman Equipment.

**Reference:** Grand River Motors Ltd. (Trustee of) v. Commercial Finance Corp, [1933] S.C.R. 591, 1933 CarswellOnt 49 (S.C.C.)

21. In the alternative, it is submitted that a sale to a finance company, accompanied by a lease back to the seller is not a sale in the ordinary course of the trade or calling of a dealer of heavy equipment, such as Hickman Equipment. Whether a transaction is in the ordinary course of a trade or calling is a question of fact and will therefore depend on all the circumstances of the sale.

**Reference:** Fairline Boats Ltd. v. Leger et al. (1980) 1 P.P.S.A.C. 218 (Ont. S.C., H.C.J.);

Misener Financial Corporation v. General Home Systems Ltd. et al. (1984) 27 B.L.R. 247 (Ont. S.C., H.C.J.).

22. It is submitted that, if the buyer is not an ordinary customer, but a financial institution, this may take the sale out of the ordinary course of business. It is further submitted that sales of equipment to finance companies by dealers, followed by the lease by the finance company to a third party (as in the Misener case) ought to be distinguished from the fact scenario in respect of the Claimed Unit. In respect of the Claimed Unit, the Financing Documents resulted in a mortgage, and were intended to operate as a mortgage, to CFG with no change in possession of the Claimed Unit. The Claimed Unit remained on the premises of Hickman Equipment in its inventory.

**Reference:** Misener Financial Corporation v. General Home Systems Ltd. et al. (1984) 27 B.L.R. 247 (Ont. S.C., H.C.J.).

23. It is submitted that if this Honourable Court determines that the bill of sale in relation to the Claimed Unit is not a “mortgage” but is a “sale” under the Bills of Sale Act, then the bill of sale is not in the ordinary course of the trade or calling of Hickman Equipment and was required to be registered under the Bills of Sale Act in order to be validly asserted against creditors, or subsequent purchasers or mortgagors of Hickman Equipment.

24. It is further submitted that CFG has therefore not established that the security agreements upon which it relies to assert a security interest in the Claimed Unit are valid.

25. CFG has not properly registered its security agreements pre-PPSA so as to protect its security interest in the Claimed Unit from the claims of other creditors and buyers in the ordinary course of business. Registration of a sale,

which was in substance a mortgage without a change of possession, was mandatory under the Bills of Sale Act and was, unless the Act was complied with, void against creditors and subsequent purchasers or mortgagees of the debtor.

26. Registration of the lease in respect of the Claimed Unit under the Conditional Sales Act was not sufficient in and of itself to protect the security interest asserted by CFG in the Claimed Unit against creditors and subsequent purchasers or mortgagees of Hickman Equipment.
27. It is therefore submitted that CFG cannot rely on the filing made at the Registry of Bills of Sale, Conditional Sales and Chattel Mortgages, in respect of the Claimed Unit under prior registration law as the date for determination of priority.

#### **JDCI's Security Interest**

28. JDCI's security interest in the Claimed Unit and the auction proceeds therefrom is pursuant to the Inventory Security Agreement dated 9 May 2000 and its Floor Plan Note dated 15 November 2001.

**Reference:** Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit "O";  
Affidavit of David R. Bugaresti, sworn 7 February 2003, Exhibit "A".

29. JDCI has a valid purchase money security interest in the Claimed Unit.

**Reference:** JDCI Final Determination, in particular, sections 2, 9B and 17, Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit "S".

30. JDCI has caused a financing statement, registration no. 5504, to be registered in the Personal Property Registry ("PPR") on 14 December 1999. By this financing statement, JDCI perfected the security interest it has in the Claimed Unit.

**Reference:** Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit "R".

31. PMSI notices were sent by registered mail by JDCI on 14 December 1999 to CIBC Equipment Finance Ltd., Bombardier Capital Leasing Ltd., ABN Amro Bank Canada, Canadian Imperial Bank of Commerce and General Motors Acceptance Corporation of Canada, Limited.

**Reference:** Affidavit of Ernest G. Reid, Q.C., dated 16 October 2002; PPSA, section 70(2).

### **Priority**

32. If CFG has a security interest in the Claimed Unit, the security interest of CFG in the Claimed Unit was not perfected until a financing statement was registered on 30 January 2000. The security interest of JDCI, however, was perfected earlier, upon registration of JDCI's financing statement on 14 December 1999.
33. The CFG Final Determination did not conclude that CFG held a purchase money security interest in the Claimed Unit.

**Reference:** CFG Final Determination, Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit "U".

34. The onus is on the party claiming priority as the holder of a purchase money security interest to establish that it has met the requirements of sections 2(hh) and 35(2) of the PPSA.

**Reference:** Dubé v. Bank of Montreal (1986) 27 D.L.R. (4<sup>th</sup>) 718 (Sask. C.A.);  
Canadian Imperial Bank of Commerce v. Marathon Realty Co. (1987), 40 D.L.R. (4<sup>th</sup>) 326 (Sask. C.A.).

35. CFG has provided no evidence whatsoever of meeting the requirements of sections 2(hh) of the PPSA. In fact, the transaction between Cyber Lease and Hickman Equipment was a sale and leaseback, which is specifically excluded from the definition of a purchase money security interest under the PPSA. It is submitted that CFG's claim, if any, to priority in respect of the Claimed Unit as the holder of a purchase money security interest must be dismissed.

**Reference:** PPSA, sections 2(hh).

36. It is submitted that in accordance with each of sections 35 and 36 of the PPSA, JDCI's perfected security interest in the Claimed Unit ranks ahead of the security interest of CFG and the claims of any other secured creditor.

**Reference:** PPSA, sections 35, 36.

37. JDCI did not provide a "no interest" letter to Cyber Lease with respect to the Claimed Unit, as seems to be alleged by CFG. However, JDCI did provide a "*holds no interest in*" letter to Cyber Lease in respect of the Claimed Unit, dated 11 June 1998 (the "The Claimed Unit JDCI No Interest Letter").

**Reference:** Affidavit of Ginter Baca, sworn 15 January 2003, Exhibit 4.

38. The Claimed Unit JDCI No Interest Letter simply confirms that, as at the date of the letter, JDCI held no interest in the Claimed Unit. JDCI submits that the Claimed Unit JDCI No Interest Letter must be construed in accordance with its terms as of its date. It was not given to CFG, and does not state that it is assignable or that it extends to the assigns of Cyber Lease. JDCI submits that it is not estopped by the Claimed Unit JDCI No Interest Letter from asserting a security interest in the Claimed Unit, which JDCI *subsequently* acquired and perfected after the date of the letter, being 11 June 1998.
39. JDCI also submits that, in order to take advantage of any alleged subordination of a security interest, the party alleging the subordination must show that the subordination was clear and unequivocal and made with the full knowledge of the circumstances. CFG has not established, and cannot establish that JDCI did or intended to subordinate future security interests which JDCI obtained at a later date (indeed, almost three and one-half years later).

**Reference:** Re Sun Life Assurance Co. of Canada and Royal Bank of Canada et al. (1995), 129 D.L.R. (4<sup>th</sup>) 305 (Ont. Gen. Div.);  
Bank of Montreal v. Kimberley Brewing Co. [1999] B.C.J. No. 2547 (B.C. S.C.);  
Federal Business Development Bank v. Steinbock Development Corp. Ltd. (1983), 42 A.R. 231 (A.C.A.);  
Engel Canada Inc. v. T.C.E. Capital Corp. [2002] O.J. No. 2361 (Ont. S.C.J.).

40. It is therefore submitted that pursuant to each of sections 35 and 36, JDCI has a perfected security interest in the Claimed Unit, which ranks ahead of CFG and the claims of any other secured creditor.

**Reference:** PPSA, section 35 and 36.

**Limited Return of Proceeds to CFG, if successful**

41. If this Honourable Court should determine that CFG does have priority in respect of the Claimed Unit, it is submitted that CFG is only entitled to return of auction proceeds in the amount of \$61,410.37, being the amount stated to be due and owing by CFG from Hickman Equipment in respect of Lease #11-889-0, by which CFG was granted a security interest in the Claimed Unit.

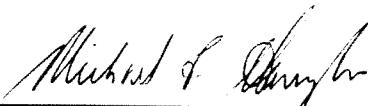
**Reference:** CFG Final Determination, Affidavit of Bruce C. Grant, sworn 7 February 2003, Exhibit "U";

Proof of Claim of CFG, Affidavit of Ginter Baca, Exhibit 1.

**Conclusion**

42. JDCI therefore requests that the Court declare that (1) the security interest of CFG in the Claimed Unit does not have priority, (2) the security interest of JDCI in the Claimed Unit has priority over CFG, and, (3) JDCI is entitled to payment of the auction proceeds therefrom.

**DATED AT** St. John's, in the Province of Newfoundland and Labrador, this 1<sup>st</sup> day of February 2003.



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