



## **Commercial Lessors and the New Motor Vehicle Sales and Dealership Regime in Ontario**

On January 1<sup>st</sup>, 2010 the long awaited Ontario *Motor Vehicle Dealers Act, 2000* (the “MVDA” or the “Act”) and its two Regulations will come into force.<sup>1</sup> The Act was anticipated to come into force on April 1<sup>st</sup>, 2009 but the Ministry has agreed to delay implementation after a number of requests for delay were received from the industry as a whole. The impact of this legislation is far reaching to any person who sells, leases or finances motor vehicles (consumer or commercial) in the Province of Ontario. The legislation is both a quasi-consumer protection act and a regulatory document combined into one. It is complex. A complete summary is beyond the scope of this article. This article focuses on some of the broad concepts that are applicable to all persons dealing in motor vehicles but with a particular emphasis on commercial finance. As will become clear, the Act while having some helpful consumer protection provisions, may have a strong negative impact on dealers and the finance market generally.

### **Background and Overview**

The new MVDA can be traced back to 1998. The genesis of the MVDA was to protect consumers from unethical car dealers and finance companies. As such, the Act provides consumers with much broader rights than they have ever had in a motor vehicle transactions with respect to disclosure and rights to return the vehicle for significant misrepresentations by the dealer. Some of these changes either intentionally or unintentionally have crept into commercial transactions and have placed certain hurdles in commercial financing that may

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<sup>1</sup> *Motor Vehicle Dealers Act*, S.O. 2002, c.30, *Sched.B, Motor Vehicle Dealers Act*, O.Reg 332/08, and *Motor Vehicle Dealers Act*, O.Reg 333/08



have unexpected consequences. Some of the changes to the MVDA will ease some of the burden on commercial lessors while other amendments may make certain types of traditional financing less attractive.

The most fundamental change under the MVDA is to eliminate a single class of dealers and to replace the single class with seven different classes of registrants. Each class has its own set of obligations and exemptions under the Act with the most complex and most highly regulated being the general dealer.

## **1. General Background**

### **Significant Changes under the MVDA**

The MVDA applies to anyone who wishes to “trade” under the Act, namely, to buy, sell, lease, advertise or exchange an interest in a motor vehicle, and will be administered by the Ontario Motor Vehicle Industry Council (OMVIC). The most noteworthy implications of the MVDA are contained in the two Regulations associated with the Act. A series of groups who are exempted from the Act. Most notably secured creditors, auctions houses (who are regulated but otherwise exempt) and insolvency professionals.

#### **A. Introduction of Code of Ethics**

The MVDA introduces a new Code of Ethics Regulation to be adhered to by all motor vehicle dealers.<sup>2</sup> Under the Code of Ethics, disclosure obligations are required and enforced by the implementation of disciplinary procedures which will include a discipline committee.

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<sup>2</sup> *Motor Vehicle Dealers Act, O.Reg 332/08*



## **B. Advertising**

The MVDA will increase the rules that motor vehicle dealers will be compelled to follow when advertising. A notable change is the requirement that the advertised price of vehicles quote the full cost of the vehicle, including all charges associated with the purchase of the vehicle (e.g. freight charges). Advertisements will be required to include the registered name and contact information of the selling dealer. Additionally, all advertisements must disclose past use of the vehicle if that past use includes the vehicle being used as a taxi, police cruiser, limousine or a daily rental.<sup>3</sup>

## **C. Right to Rescind Transaction**

One of the most significant changes is the enhanced remedies available to consumers to rescind transactions if certain disclosures are not made. According to the new provisions of the Act, consumers, other than commercial lessees, will be afforded the right to rescind a contract for purchase or lease within 90 days, if a dealer fails to comply with a number of critical disclosure requirements.<sup>4</sup> Where a motor vehicle dealer fails to, or inaccurately discloses the distance the car has travelled, the prior relevant uses of the vehicle, that the vehicle was leased on a daily basis, the make, model, or trim of the vehicle or any major repairs done to the vehicle, the consumer will be provided with the right of rescission under the MVDA. This right allows the motor vehicle purchaser or lessee 90 days to cancel the contract and return the vehicle for a refund. It is important to note that this right is available to consumers whether or not the motor vehicle dealer sold the

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<sup>3</sup> For advertising requirements see: *Motor Vehicle Dealers Act*, O.Reg 333/08, s.36

<sup>4</sup> *Motor Vehicle Dealers Act*, O.Reg 333/08, s.50



vehicle in good faith or had knowledge of the information that was not disclosed.<sup>5</sup> The most problematical of the above-noted list is that certain of the information such as trim level and major repairs may not readily be available to dealers and have the unintended consequence that even acting in good faith, transactions may be rescinded. For instance, Ontario does not have a “beyond reproach” search system for major repairs that can be relied upon by dealers and as such, the dealer would in effect become an “insurers” of the bad acts of former car owners. Our firm has made representations to OMVIC that certain safer harbour rules should have been built into the Act to protect honest dealers but as of the date of writing this article, no response has been received.

#### **D. Dealer Classification**

Likely the most significant change to the regulatory regime comes in the implementation of a new classification system of motor vehicle dealers. The Regulations set out seven defined classes and sub-classes of motor vehicle dealers. All motor vehicle dealers in Ontario will be required to register and become licensed under one (or more) of these defined classes.<sup>6</sup> The seven classes are as follows: (1) general dealers (divided into two sub-classes: new and used; and used dealers); (2) brokers; (3) wholesalers; (4) exporters; (5) outside Ontario dealers; (6) lease finance dealers; and (7) fleet lessors (divided into two sub-classes: commercial lessors and short-term lessors).

The distinction between the classes of motor vehicle dealers is significant, as each class is subject to different requirements under the MVDA. The General Dealer class is the “catch-all” category for dealers who sell and/or lease motor

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<sup>5</sup> *Ibid* at s.50(2)

<sup>6</sup> *Ibid* at s.18



vehicles directly to the end consumer. The burdens imposed by the Act fall primarily on them. Alternatively, fleet lessors and wholesalers, who typically deal with other commercial dealers, are afforded numerous exemptions under the Act.

### **E. Required Changes to Sale and Lease Documents**

The MVDA Regulations will drastically alter contracts for the sale or lease of motor vehicles by creating specific contractual requirements for each class of dealer. The purpose of these contractual requirements is to protect the consumer by clarifying contracts for the sale or lease of motor vehicles, rendering them easier for the consumer to understand. Under the MVDA, there are contractual requirements that apply to every class of registered dealer. For example, all contracts for the sale or lease of a motor vehicle under the Act must include the name and address of the contracting parties, the colour of the vehicle, the vehicle identification number, the body type of the vehicle, along with numerous other requirements applicable to all contracts. Accordingly, all bills of sales and lease documents will have to be amended.

In addition to the mandated changes under the MVDA there are a number of more subtle changes that, while not mandated, should be reflected in the document including a requirement that the lessee provides the lessor with a disclosure statement at the lessor's request, a requirement to provide a listing of any major repairs and that all costs associated with any audit at the end of lease will be borne by the lessee. In cases of the mere sale of the motor vehicle, these issues are not as complex but in an on-going relationships such as a lease, then these changes are strongly recommended. Further, if a trade-in occurs there will be specific information that the dealer will need to obtain from the owner.



## F. Disclosure Statement

All sales and leases (except commercial) will require disclosure statements where applicable, or general declarations designed to inform consumers of their rights under the Act.<sup>7</sup> This disclosure statement is one of the hallmarks of the MVDA as it provides the consumer with basic information about that which they are about to purchase. This statement will be appended to all sales documents. This disclosure statement sets out 25 factual points about the vehicle that must be disclosed to the consumer. The issue of course is how does the dealer obtain this information. When the motor vehicle is a new car it is relatively easy (although there are still potential problems describing trim etc.) but for used cars, the best information comes from the former owner and as such the dealer must have a method of obtaining this information. As noted above, there are no searches which a dealer can rely upon so an inherent risk is being taken on by the dealer. What is most problematical is when the car is being repossessed as it is likely that the former owner will not be co-operative. Absent a disclosure statement, a dealer can only sell through an auction and this reduces the value of the car.

### 2. Fleet Lessor Obligations and Exemptions

The remainder of this discussion will focus primarily on the impact the MVDA has on fleet lessors. The fleet lessor classification is further divided into two sub-classes under the MVDA: commercial lessors and short-term lessors. As prescribed by the Act, a fleet lessor under the commercial lessor sub-class is

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<sup>7</sup> For example: section 39(2)(24) of *Motor Vehicle Dealers Act*, O.Reg 333/08 requires motor vehicles under the New or Used class to include the following statement: “**Sales Final:** Please review the entire contract, including all attached statements, before signing. This contract is final and binding once you have signed it unless the motor vehicle dealer has failed to comply with certain legal obligations.”



able to buy motor vehicles; lease motor vehicles as a lessee; lease motor vehicles to a non-consumer; sell a previously leased motor vehicle to prescribed persons under the Act<sup>8</sup>; and advertise the motor vehicle to be sold or leased.

To be classified as a short-term lessor under the Regulations, a motor vehicle dealer must follow the same restrictions as a commercial lessor, with the additional requirement that the length of the lease be for a fixed term of less than four months.<sup>9</sup>

### **A. Regulatory Matters**

Registering under one of the two fleet lessor sub-classes allows the motor vehicle dealer to take advantage of certain exemptions under the MVDA. From a regulatory standpoint, the Fleet lessor is exempt, i) from hiring registered sales people. This is a significant change from the old act and makes it far easier for commercial finance companies to transact business, ii) from disclosing to the registrar the identity of shareholders or a change of an officer or director of the entity,<sup>10</sup> iii) from the stay imposed on a debtor by the appointment of a receiver and manager, or a freeze order,<sup>11</sup> iv) from a requirement under the Act which mandates the filing of financial statements with the registrar upon request.<sup>12</sup>

These changes reduce the burden on commercial finance companies and should increase the number of companies providing financing to the market.

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<sup>8</sup> *Motor Vehicle Dealers Act*, O.Reg 333/08, s.25 establishes that a fleet lessor is able to sell a previously leased motor vehicle to (i) the lessee, (ii) an individual who drove the motor vehicle during the term of the lease, (iii) an officer or director of the lessee, if the lessee is a corporation, (iv) a partner of the lessee, if the lessee is a partnership, or (v) a registered motor vehicle dealer, or (vi) at an auction.

<sup>9</sup> *Ibid* at s.26

<sup>10</sup> *Ibid* at s.4 and 6

<sup>11</sup> *Ibid* at s.5

<sup>12</sup> *Ibid* at s.6



Many U.S. lessors have resisted entering the Ontario market due to the requirement of having a registered sales person.

## **B. Disclosure Requirement and Sale Issues**

The most significant of the exemptions provided to fleet lessors under the Act is the exemption to comply with the vast disclosure requirements for lease documents as established by an explicit carve-out under the “Leases” section of the Act.<sup>13</sup> Due to this carve-out, fleet lessors are not required to provide the otherwise obligatory information under the contract disclosure section of the Regulations in their lease documents when selling or leasing motor vehicles to a lessee who is not another registered motor vehicle dealer<sup>14</sup>. This is a particularly noteworthy exemption, as the aforementioned section enumerates twenty-five mandated contractual requirements. It is equally significant that the fleet lessor carve-out from the disclosure requirements also renders those registered as fleet lessors exempt from the rescission provisions under the Act when selling or leasing a motor vehicle to a lessee who is not another registered motor vehicle dealer.<sup>15</sup>

The implication of this is that a fleet lessor can transact business much as it had in the past and no longer needs a registered sales person. The only tricky part as discussed in the next section is that if the fleet lessor has a residual lease and it takes back the vehicle at the end of the term. It needs to have a method to sell the vehicle.

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<sup>13</sup> *Ibid* at, s.41(1)

<sup>14</sup> *Ibid* at, s. 42

<sup>15</sup> *Ibid* at s.42 and 50



## **The Commercial Lessor and the Sale of a Motor Vehicle**

It is important to note that unlike the old Ontario *Motor Vehicle Dealers Act*<sup>16</sup>, the MVDA does provide some assistance to a leasing company who is selling a vehicle at the end of the term of a lease. As mentioned above, motor vehicle dealers registered under the Act as commercial lessors are exempt from the rigorous disclosure requirements when administering leases to non-dealer lessees. Practically speaking, what this means is that under circumstances where the leasing company is not realizing on its security or the commercial lessor does not wish to re-lease or re-sell the vehicle once the original lease has terminated, the motor vehicle may be sold by the commercial lessor at the end of the term without any special disclosure. The Act has broadened the category of who the vehicle can be sold to include an individual who drove the vehicle during the term of the lease, officers, directors, or a partner of the lessee or to a person who arranges for and conducts an auction of motor vehicles as prescribed by the Act<sup>17</sup>, while still remaining within the contract disclosure exemption.

The circumstances change when a commercial lessor wishes to sell a motor vehicle at the end of the term of a lease to another registrant under the Act. Here, the commercial lessor must comply with the Code of Ethics Regulation to the Act and must provide a contract for sale to the purchasing registrant that includes the twenty-five mandated disclosure requirements. Such requirements include revealing whether the motor vehicle is a used motor vehicle, the total distance the vehicle has been driven, whether the vehicle has

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<sup>16</sup> *Motor Vehicle Dealers Act*, R.S.O. 1990, Chapter M. 42.

<sup>17</sup> *Ibid* at s. 2(1)1. and 2(3) Persons who arrange for and conduct auctions of motor vehicles are exempt from registering as motor vehicle dealers under the Act. In order to qualify for this exemption, the person arranging and conducting the auction must meet the enumerated conditions set out in the Regulations. Note that a person may only sell a motor vehicle at such an auction if they are a registered motor vehicle dealer under the Act.



been previously used as a police cruiser, taxi, limousine or for rental purposes, among other requirements. In order to obtain such information, commercial lessors will need to survey their lessees prior to the return of the leased vehicle in order to accurately reveal the required contractual information to the purchasing registrant. As noted above, there are no “safe harbour” rules. While these disclosure statements are mandatory only when selling to another registered motor vehicle dealer, it will be prudent practice for commercial lessors to obtain such statements from all lessees in order to protect future purchasers of the motor vehicle in question.

If the dealer is not able to obtain the disclosure statement, which would typically occur if there is an insolvency, then the fleet lessor could only sell at auction.

### **Securitization and on-going sale problems**

If a fleet lessor simply leases to its lessee and ultimately sells the vehicle to the lessee, then the new Act is more helpful than prior legislation. However, this is simply not commercial reality in the modern finance market. Most lessors need to obtain financing in some manner to expand their businesses. The most typical method, prior to the recent credit crunch was the securitization market whereby the fleet lessor would sell its lease and often the vehicle to a special purpose entity (“SPE”) that would then issue notes into the market. The problem with the MVDA is that the transfer to the SPE would be seen as a “trade” and require disclosure. Accordingly, the fleet lessor would during the term of the lease be required to ask the lessee to provide a disclosure document that a lessee would likely be slow to comply with and perhaps be reticent to fill out as it



may not want to disclose problems. This concern also exists if companies sell portfolios to each other from time to time.

The major consequences to banks lending to fleet lessors would be enhanced due diligence to ensure compliance with the Act and underlying documentation. The most significant problem may be the structure of loan will be limited to classic loans and security which exposes the bank to insolvency risk of the lessor which would not be the case in a private or public securitization market. Pricing would likely increase.

### **Options Outside the Scope of the Act**

Needless to say, the new rules governing the motor vehicle dealer industry are significant and quite cumbersome. An alternate for a commercial finance company may be to provide equipment financing by way of a loan and security agreement as opposed to becoming a licensed motor vehicle dealer under the MVDA. A loan and security agreement provided by a financial institution to a borrower for the purposes of financing the purchase of a motor vehicle does not fall within the definition of a “trade”<sup>18</sup> under the MVDA, and as such, the financial institution’s compliance with the Act is not required. One issue with this alternative option arises when the borrower-lessee acts on its rescission right under the Act. How then will the financial institution ensure its security under the loan?

As a potential remedy to this issue, the lending financial institution can build a provision into its loan and security agreement prohibiting the borrower

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<sup>18</sup> *Motor Vehicle Dealers Act, 2002* S.O. 2002, Chapter 30, Schedule B s.1.(1) defines a “trade” to include “buying, selling, leasing, advertising or exchanging an interest in a motor vehicle or negotiating or inducing or attempting to induce the buying, selling, leasing or exchanging of an interest in a motor vehicle.”



from exercising its rescission right under the MVDA to ensure its security over the loan. While this appears to be a fairly simple remedy, it is uncertain whether a court would uphold such a provision. As the Act has yet to come into force, there is no case law to examine whether such a clause would be enforceable by a registered fleet lessor. It appears from the Act that a provision of the sort would be enforceable by the lending financial institution as the MVDA specifically provides for an exemption to creditors who are not registered under the Act.<sup>19</sup> This exemption however, does not extend to the registered motor vehicle dealer leasing the vehicle to the borrower-lessee. As well, it is unclear from the Act whether a registered motor vehicle dealer under the MVDA is able to contract out of the rescission rights prescribed under the Regulations to the Act.

The lending financial institution may also wish to consider entering into agreements directly with the registered motor vehicle dealer whereby the commercial finance company will hold funds in escrow for the dealer until the 90-day rescission period is over in order to secure the institution's loan to the borrower-lessee. Agreements of this nature will enhance the need for financial institutions to have vendor programs with motor vehicle dealers.

Another potential issue institutional lenders may face when issuing loan and security agreements to borrower-lessees arises when there is an early termination of the motor vehicle lease. In this case, the financial institution may repossess and dispose of the motor vehicle by way of an auction without having to become registered under the MVDA. As previously mentioned, the financial institution, as a non-registrant creditor, is exempt from the provisions of the Act and as such, may sell the vehicle to a person arranging an auction of motor

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<sup>19</sup> *Motor Vehicle Dealers Act*, O.Reg 333/08, s. 2(1) 14.



vehicles to dispose of the vehicle. The greater problem with this is that it tends to lower the value of the vehicle in those circumstances.

### **Summary**

The MVDA commercial stated intention of protecting consumers may have some rather inadvertent consequences. Loans may no longer be available as the right to rescind may be too much of a risk for a commercial finance company to undertake. From the commercial lessor's standpoint, the regime should be helpful. They no longer need a registered sales person which should provide for some welcome relief to finance professionals who do not see themselves as car sales persons. On the other hand, more care needs to be taken in the actual lease document and the ability to sell the vehicle at the end of the term of a residual lease. Further, the lack of safe harbour rules and the likely chilling effect on the securitization market may have material adverse effects that more the offsets the gains made under the Act.

This article is written by Jonathan Fleisher, Lydia Salvi, David Budd and Dahlia Tessler in the Financial Services Group at Cassels Brock & Blackwell LLP. Should you have any questions in connection with the foregoing, you may contact Jonathan Fleisher at (416) 860-6596, Lydia Salvi at (416) 869-5409, David Budd at (416) 869-5392, or Dahlia Tessler at (416) 860-6772.