

# THE COMMON LAWYER

## Repair Loans – Useful Tools, or a Nuisance?



By Justin M. Jakubiak

Vehicle repair loans are gaining popularity in Ontario, as are the legal issues and headaches surrounding them.

Repair loans are typically advertised as the solution to unexpected costly car repairs that a consumer may not be able to afford. Once approved, the mechanic is paid in full for the repairs, and the consumer can take her car away and repay the repair loan over time by way of fixed monthly installments. What if the customer already has a loan registered against her car? No worries - the repair loan takes priority!

Sounds like a great tool; unless you are an automotive lender and previously lent money to the same consumer to purchase her vehicle. In the event of a default by the customer, you as lender may have a significantly reduced equity interest in the customer's vehicle. Also, if you want to challenge the amounts being claimed by the repair lender, you will

likely have to tie-up money by paying it into Court in order to secure the release of the vehicle from the repair lender.

Repair loans are tools which can be abused by dealers, mechanics and repair lenders. It is therefore vitally important that repair lenders understand the relevant legislation, that automotive lenders understand their rights, and that dealerships/mechanics train their staff to ensure that any type of lending facility is used appropriately and ethically.

### *Repair and Storage Liens Act*

Typically, when an automotive lender makes a decision to lend money to a consumer, it does so based on (amongst other things) the value of the vehicle in question, and on the condition that the vehicle's title is "clean"; meaning free from any other encumbrances. At the time of purchase, the automotive lender will register a security interest against the vehicle and as a result there will be notice to the world that the automotive lender has a first-ranking financial interest in the vehicle.

This first ranking priority interest is paramount, except for the exceptions granted to repairers and storsers under Ontario's *Repair and Storage Liens Act* ("RSLA"). The RSLA gives repairers and storsers lien rights which are in super priority to any other interests in the vehicle. Historically, this has made sense - Why should a repairer who has invested his time and skill into a vehicle (and has thereby improved it) remain unpaid?

The RSLA, in addition to protecting the repairer (and storsers), also provides a

mechanism where the rights under the RSLA can be assigned. This is where repair lenders have come in and some difficulties have arisen.

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In my practice, I am seeing recurring concerns surrounding repair loans in which the lender has taken an assignment of the repairers' rights under the RSLA. I am often contacted by my lending clients after they have received notice from a repair lender that it has repossessed one of their vehicles. The reaction is often significant frustration over the fact that the asset which is securing their automotive loan is now encumbered with a significant repair loan and other fees - about which the repair lender is saying take priority to the interests of my client. Yes and no. It is important to note that the RSLA only pertains to certain expenses and the repair lender has certain notice obligations to abide by. I suggest always reviewing such notice documents with suspicion to ensure that the claimed fees and expenses are valid. If you are concerned, review the notice received from the repair lender with your lawyer and consider challenging the repair lender in court.

To add to the frustration felt by many car loan companies, borrowers sometimes misuse repair loans, with the participation of repair shops or dealerships, to get money for unperformed work. Some dealerships have also been known to use repair loans in order to get a customer additional financing in order to purchase a vehicle. The misuse of repair loans can cause significant legal hurdles down the road for the repair lender, the dealership (including potential problems with OMVIC!) and the automotive lender.

### Overview of repair loans

Getting a repair loan is relatively straightforward. The difficulties arise in collecting money when the borrower cannot pay.

The mechanism for collecting the money owed is based on the repairer's lien. Traditionally, a repairer's lien allows the repairer to keep possession of the vehicle until the owner pays for the work done. Under the RSLA, a repairer may also repossess a vehicle that is no longer in its possession. After appropriate procedure is followed, the repairer may sell the car to satisfy the debt.

How does this connect to a repair loan? Essentially, the loan documents involve the repairer agreeing to give (assign) the lender its lien rights for repairs done to the vehicle. The lender then pays the repairer for the work performed. If the

borrower defaults on the loan, and the appropriate procedure for the repairer's lien is followed, the lien allows the lender to repossess the vehicle and sell it to satisfy the unpaid debt.

But what happens when, as is often the case, the borrower has other loans for the car? When a borrower defaults, it usually means they do not have money to pay either the repair loan or the outstanding loan for the purchase of the car. Often, the vehicles in question are worth less than the total amount of the loans. Legal disputes arise since repossessing and selling the car is not enough to satisfy both lenders. The lenders end up competing for who gets their money first ... or at all.

### Defaulting on the loan

Since the repair loan is secured by a lien under the RSLA, it has priority over the purchase loans, which are secured under Ontario's *Personal Property Security Act*. The priority means that if the lender for the repair follows the appropriate procedure in enforcing the lien, they will be able to satisfy their debt before the other lenders can. In other words, the repair lender gets its money first. Often, selling the vehicle leaves very little, or no money left over to go towards the loan that is second in line.

What options does the car purchase lender have in this scenario? A lien claimant has to follow the procedure set

out in the RSLA. This means that both the original repairer must have satisfied the procedure, as well as the lender claiming under the RSLA.

The car purchase lender may be able to challenge the repair lender's entitlement to a lien. One common example I have encountered in my practice is where evidence indicates the loan was for work that was not actually performed. Another example is that the loan was used to pay for car parts instead of repairs. The below cases are illustrations of these situations.

### 1. Lovats Acceptance Corp v Advantagewon Inc. ("Lovats")

In this case, the court found that the repair lender, Advantagewon Inc., ("Advantagewon"), did not have a lien claim, whereas the lender for the purchase of the vehicle did. The repair loan related to the purchase of summer and winter tires and rims. However, the only 'repair' work done was that the repair shop installed the winter tires. As such, the only possible lien that could arise was in relation to the installation of the winter tires. The court found that no lien arose since the owner of the vehicle immediately paid for the tire installation using his loan. The owner was never indebted to the repairer and there was never any lien that the repairer could assign to Advantagewon. As a result, the lender for the purchase of the vehicle was able to enforce its rights to satisfy the debt of the unpaid loan.

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## 2. Connolly v Advantagewon Inc. ("Connolly")

This is a leading case on the issue of repair loans and also deals with the purchase of rims and tires. In this case, the owner of the vehicle admitted that the repairer never installed the tires and that the repairer never had possession of the vehicle. Instead, the owner bought the tires from the 'repairer' and installed them himself. One of the prerequisites for a lien claim is for the repairer to have possession of the vehicle at some point during the repairs. As such, the repairer never had a valid lien that it could assign to Advantagewon. Again, since the repairer never had a lien on the vehicle, there was no lien it could assign to the lender.

The above cases point to some potential arguments a lender can make in seeking to enforce its security and collect its money before the repair lender. The situations in which a repair loan may become an issue vary and there may be other arguments to make, depending on the circumstances of each case.

### Consequences for Repair Shops and Dealerships

As the cases above show, repair loans are sometimes granted despite only a portion, and sometimes none, of the loan going towards actual repair work. While this may open up a potential argument in favour of the car purchase lenders, what about the repair shops and dealerships that participate in such activity? Should they be concerned?

Unfortunately, there is no straightforward answer – time and future legal cases will tell.

In the loan approval documents, the repair shop agrees to assign its lien rights to the lender. Further, there is usually a clause in one of the loan documents requiring the repairer to acknowledge that it performed the work in its invoice. But this does not necessarily mean that the repair shop has an obligation to ensure it has a valid repairer's lien when it accepts money from such a loan.

Nevertheless, there may be potential consequences for repair shops that facilitate such loans. At the very least, repair shops should not make invoices for work knowing that it will not be performed, as this would open a potential claim for fraud. Doing so could also be a breach of contract, if there is a clause in the loan documents signed by the repairer stating that it has performed the invoiced work. Such practices could expose shops and dealerships to potential legal claims, license revocations, sanctions from OMVIC, fines, and even criminal charges.

### Conclusion

Repair loans are an increasingly popular financing method and the legal issues surrounding them continue to be defined. If you are a lender that is

frustrated by a repair lien that has priority over your security in the vehicle, there may be grounds for you to nevertheless enforce your security. Repair shops and dealerships should also practice diligence in signing loan documents. Invoices should be accurate and reflect the work that is actually performed on the vehicle.

Lastly, regardless of whether you are an automotive lender, a repair lender or a dealer, well drafted documents and well-designed processes are key. Making sure your documents and process comply with the law is paramount in ensuring success in court. Especially important is making sure your staff are well trained and know what is appropriate and what is not.

