

Bulk Sales Act: Non-Compliance



By **Brian Madigan LL.B.**

You might wonder about the application of the *Bulk Sales Act* in Ontario.

What is the purpose of the legislation? Who is it designed to protect?

What impact does it have on a transaction? Why is it often ignored?

And, why is “just let the lawyers worry about it; the incorrect answer?”

The *Bulk Sales Act* is rather old legislation. Generally, it is designed to protect unsecured creditors when a business is sold. If a transaction does not comply with the provisions of the Act, then creditors can have the transaction set aside. That’s a very powerful remedy!

Realtors should be concerned, since there is a specific requirement under the *Real Estate and Business Brokers Act, 2002*, to have them obtain certain information in an effort to comply with the Act. Who are the creditors? How much is owed to each of them and are they secured or unsecured.

While the legislation applies in Ontario, most Provinces and States do not have similar protective legislation. It still exists in Newfoundland, but all other Provinces have repealed the legislation.

The term “stock” is a defined term under the Act. Frequently, in business and commercial terms, stock is simply another word for inventory. However, that is not the case under the *Bulk Sales Act*. There is an expanded definition.

Stock comprises three categories:

- 1) commercial products, (goods ordinarily resold in the market)
- 2) production of the facility, (manufactured goods)
- 3) fixtures, goods and chattels used in the business.

In a bulk sale, the Act will also apply to everything else that goes with the sale both real and personal. So, the lease of the premises and the lease of the delivery truck would be included.

The question, in terms of application of the Act is whether the sale itself is usual, as being in the ordinary course of business, or a bulk sale which would be “out of the usual course of business”:

Usual sale ~ Act does not apply

Out of the Usual sale ~ this is a bulk sale, Act applies

The frequency in turnover of inventory is one item. If you are in the car business, and you sell a car on the lot to a consumer, that would be expected. If you sell 10 cars on a Saturday at your advertised deep discount festival, then that's still "usual".

However, if you have 100 cars in your inventory and you sell 90 to another dealership, then, that's unusual and the bank which holds security over your inventory needs to be notified. The bank is expecting that you will ordinarily have 80 to 120 cars on your lot. If they arrive to realize on their security and find that you sold 10 to consumers and 90 to the other dealership, then there is a *Bulk Sales Act* compliance issue. Failure to comply with the Act could result in forfeiture of the 90 cars to the bank by the second dealership.

In order to determine whether a sale is usual or out of the ordinary, you would have to look at the facts in each particular case. Certainly, what's usual for one business might be unusual for another.

The substantial concern in a bulk sale is the risk of non-compliance. If the transaction does not comply, then the transaction can be set aside.

Recently, the Courts set aside a transaction because it failed to comply with the Act. All the money had been paid to the secured creditors. Had the transaction been completed in compliance with the Act, then, all the money paid on closing would have been paid to the secured creditors. And, that's just what happened! But, with one little exception, there was no compliance with the *Bulk Sales Act*.

You might think that is just a technicality, but, the Courts set aside the transaction at the instance of the unsecured creditors and forced the purchaser to "re-buy" the business. Remember, that the first time the purchaser bought the business, they paid off all the secured trade creditors. So, now they're gone; and you can't use that money as a setoff. The result was simple: the purchaser bought the business twice, the second time paying off all the unsecured trade creditors.

In our car dealership example, other unsecured creditors would have been similarly protected. That means if there were additional unsecured creditors, (not just the bank as a secured party), then they may have to right to set aside the transaction. So, make sure that you comply with the *Bulk Sales Act* if you are buying a business, or advising someone who is buying a business.

Brian Madigan LL.B., 905-796-8888
www.OntarioRealEstateSource.com