Selected Problems under the Quebec Law of Conditional Sale

Richard W. Pound*

Introduction

The Articles in the *Civil Code* relating to the conditional sale of moveable property are comparatively recent. Articles 1545*a* and *b* were enacted in 1933[1] but were restricted in scope to provisions dealing with the right of the purchaser in a conditional sale contract to pay the balance of the purchase price and thus obtain title to the property, as well as to the right of the purchaser to pay what was due and recover the object, in the event that the vendor repossessed the property, provided the right was exercised within twenty days and the seller was reimbursed the expenses of repossession and preservation of the thing sold. The scope of these provisions was broadened in 1947 by the enactment of the *Instalment Sales Act,* the provisions of which added Articles 1561*a* to *j* as a separate heading forming Chapter VI A, "Of Instalment Sales", to the *Code.*[2] This legislation was among the first of its type in Canada, with the result that its draftsmanship is somewhat primitive and, in 1970, probably outdated.[3]

There are a number of aspects of this legislation which have remained virtually unintelligible to the instalment creditor, instalment purchaser and practitioner alike. It is proposed to examine three such matters.

1 *Operation of Article 1561i CC.*

Article 1561*i* CC reads in part as follows:

> Every sale of moveable property, promise of sale of moveable property with delivery and possession or any contract having the effect of a sale of

* Member of the Bar of Montreal.

1 23 Geo. V, c. 107, 1933 S.Q.

2 11 Geo. VI, c. 73, 1947 S.Q.

3 All provinces, with the exception of Quebec and Manitoba, now have Conditional Sales Acts: Alberta, R.S.A. 1955, c. 54; British Columbia, S.B.C. 1961, c. 9; New Brunswick, R.S.N.B. 1952, c. 34; Newfoundland, S. Nfld., 1955, c. 62; Nova Scotia, R.S.N.S. 1967, c. 48; Ontario, R.S.O. 1960, c. 61; Prince Edward Island, R.S.P.E.I. 1951, c. 28; Saskatchewan, R.S.S. 1965, c. 393.

> moveable property, which admits of the deferred payment of the price or of a part of the price of sale and which does not comply with the requirements of articles 1561*a* to 1561*e* inclusively, is a sale on terms, subject to the ordinary provisions of obligations with a term, which transfers to the buyer the property[4] of the thing sold, notwithstanding any stipulation or declaration te the contrary.

Assume that a sale has taken place which proports to be a conditional sale but which for some reason violates or fails to comply with a provision of Articles 1561*a* to 1561*e*. It is clear that in such case the conditional vendor is no longer the owner of the property, that title will be deemed to have passed and that he will no longer have a right *in rem* against the moveable property. A *saisie-revendication* has been disallowed on the ground that the conditional sales contract in question did not conform to the requirements of Article 1561*d* as to the calculation of finance charges.[5] Similarly a seizure before judgment has been disallowed on the ground that conditions of Article 1561*a* and following had not been observed.[6] The correctness of the holdings in these two decisions cannot be seriously questioned, insofar as refusal to recognize a right *in rem* is concerned.

A more difficult problem relating to Article 1561*i* is the interpretation to be given to the words "subject to the ordinary provisions of obligations with a term".[7] Does this mean, for example, that any clauses in such contracts[8] relating to finance charges, default charges and other matters will also fail? In other words, does the failure to observe the requirements of Articles 1561*a* to 1561*e* not only cause title to the goods to pass but also operate to set aside any other terms and conditions in the contract between the vendor and purchaser?

The jurisprudence on this point is best described as mixed. In *Canadian Family Food Plan Ltd.* v. *Cosgrove*,[9] the Court was prepared to allow the plaintiff, the conditional vendor, to claim for the amount due for the goods sold and delivered as well as costs of a *mise en demeure* to the purchaser from its attorneys, but held that the vendor had no right to claim the finance charges nor the interest at 9% stipulated in the contract in question.[10] A similar

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[4] French: *propriété*.

[5] *Circle Acceptance Co.* v. *Kerr*, [1968] P.R. 305. (Provincial Court).

[6] *M. Aber Inc.* v. *Deneault*, [1968] P.R. 385 (Provincial Court).

[7] French: «sujette aux dispositions ordinaires des obligations à termes.»

[8] *i.e.* to which the provisions of Art. 1561*i* apply.

[9] [1956] S.C. 439.

[10] Reference was made to *H. Laflamme Limitée* v. *Côté*, reported in summary at [1954] Q.B. 253 and *Pâquet* v. *Plammondon*, [1954] R.L. 223 (Court of Queen's Bench (Appeal Side)).

holding is found in *Le Syndicat St-Henri Inc.* v. *Ross Barklay.*[11] The decision in this case provided that if the requirements of Articles 1561*a* and following are not fulfilled, the contract is placed under the sole operation of law and, in addition to title to the goods passing, any other special condition in the contract would be lost. The case was heard in Magistrate's Court by Judge Gérard Trudel and although inscribed by default, it appears that witnesses were called and likely some argument made by plaintiff.[12] The particular deficiency in the contract in question was the amount of the down payment, which was considerably less than the 15% required by Article 1561*b*. Given this deficiency, the learned judge regarded the provisions of Article 1561*i* as imposing a double sanction on the conditional sale vendor, the first being the transfer of title to the property (a sanction attaching to the *jus in re*, presumably on the ground that the claim as owner is opposable against all persons) and the second nullifying the other clauses in the contract which are not concerned with the property itself but which relate to the private obligations between the contracting parties themselves. This latter sanction is regarded by the learned judge as attaching to the *jus ad rem* as being entirely between the parties and not directly affecting the property itself.[13] It is the idea of a double sanction that separates this case from other cases which simply hold that title to the property passes in the event of a breach of the terms of Articles 1561*a* and following.

A further decision to the same effect is the case of *La Compagnie Légaré Limitée* v. *St-Amant*,[14] in which, due to non-observance of the requisite formalities, title to the goods was held to have passed. The Court, relying on the *St-Henri* case, held that the contract, once invalid as a conditional sale contract, became automatically a contract of sale with a term, regulated solely by Articles 1089 to 1092 C.C., and any special conditions in the contract thus became inoperative. In *Sunrise Industries (Mtl.) Limited* v. *Robert*,[15] the contract in question was also held to become a contract of sale on terms subject to the ordinary provisions of law and, in this case, the interest on the contract was limited to 5% per annum on instalments

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[11] [1957] R.L. 35.

[12] Argument may not have been heard on this point, however, as the learned judge appears to have been unaware of the decisions in *H. Laflamme Limitée* v. *Côté, (supra), Pâquet* v. *Plammondon, (supra)* and *Canadian Family Food Plan Ltd.* v. *Cosgrove (supra)*, all of which had been reported prior to his decision.

[13] For the development of this thesis, [1957] R.L. 35 at pp. 39-41.

[14] [1962] S.C. 29.

[15] [1964] S.C. 678.

due. The most recent reported case in this line of jurisprudence is *Federal Acceptance Corporation* v. *Di Loretto*,[16] a decision of the Provincial Court in Montreal, which relies on the decision in *St-Henri, Sunrise* and *Cosgrove*.

The opposite view has been taken in a decision of the Superior Court; in *Commodity Discount Limited* v. *Dame Gagnon*,[17] an action taken by the assignee of a conditional sale contract and a promissory note attached thereto against the purchaser under the contract. While the action was based primarily on the note rather than the contract, matters relating to the contract were raised by the defendant purchaser. The operation of Article 1561*i* had been invoked because of the failure to require a down payment of at least 15%. The Court held, that notwithstanding this failure a special clause relating to the annulment of the sale was not invalid, in spite of the fact that the sale was no longer a conditional sale. In giving judgment, the Court allowed the full interest of 9% per annum on the amount of the note, even though it was clear that the conditional sale giving rise to it did not conform to the provisions of Articles 1561*a* and following. A more explicit decision on this question is to be found in the Provincial Court decision in *American Music Corporation Ltd.* v. *Malette*,[18] in which, although the conditional aspect of the sale was clearly disqualified, the Court was not prepared to conclude that other terms of the contract, such as penalty clauses, stipulated interest and the like were annuled for the sole reason that the conditions required by Articles 1561*a* and following had not been met. The Court went on to state that it was necessary to consider the contract as if the chapter on instalment sales did not exist and to give effect to all the conditions as to payment, interest and penalties so long as they were not contrary to good morals nor prohibited by any other law.

> Peut-on raisonnablement dire que les conditions de la vente, les clauses pénales, l'intérêt stipulé, etc., sont annulés — par le seul motif que les conditions requises pour bénéficier des avantages accordés par la vente à tempérament n'ont pas été rencontrées ? Le tribunal ne le croit pas. — Ce serait aller bien au-delà de la loi. — Il faut alors considérer le contrat comme si le chapitre de la vente à tempérament n'existait pas et donner effet à toutes les conditions quant au paiement, aux pénalités et aux intérêts stipulés pourvu qu'elles ne soient ni contraires aux bonnes moeurs, ni prohibées par une autre loi.
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> Dans la présente cause, il est clair que la venderesse n'est pas dans les conditions pour réclamer la propriété de sa chose comme dans la veute à tempérament, parce que le paiement initial est inférieur à 15%.

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[16] [1969] R.L. 561 (Provincial Court).
[17] [1960] S.C. 675.
[18] [1967] R.L. 552 (Provincial Court).

> Rien ne l'empêche de réclamer le prix de sa chose et le coût de financement que le défendeur a librement consenti à payer.[19]

It is submitted that the decision in *American Music Corporation Ltd.* is the better view of the meaning of the provisions of Article 1561*i*. It is doubtful that the words "subject to the ordinary provisions of obligations with a term"[20] are sufficiently broad to permit the Courts to disregard all of the conditions and terms of a contract freely agreed upon between a purchaser and vendor.

Even the cases headed by *St-Henri*,[21] are in general agreement that the provisions governing obligations with a term are to be found at Articles 1089 to 1092 C.C. An examination of these articles discloses nothing which relates to agreement on special conditions in such obligations, such as finance charges, penalty clauses and other commercially necessary provisions. Article 1089 explains that an obligation with a term is not an obligation which has been suspended, but only one whose execution has been delayed. Article 1090 provides that payment cannot be exacted before the expiry of the term, but that voluntary payment in advance is perfectly acceptable. Article 1091 states that the term is presumed, in the absence of express stipulation or circumstances indicating the contrary, to be stipulated in favour of the debtor. Article 1092 sets forth situations in which a debtor may not claim the benefit of the term. These articles would appear, therefore, to be "the ordinary provisions of obligations with a term".

Considerable emphasis is placed, in the *St-Henri*[22] case, on the wording of Article 1561*i* as giving rise to two separate and distinct sanctions which apply in cases where the parties have not respected the provisions of Articles 1561*a* and following. This was discussed briefly without comment as to the extent of each sanction.[23] The sanction which is obvious is that relating to the passing of title and can be seen from the words "is a sale on terms... which transfers to the buyer the property of the thing sold...". It is not, however, clear that the words "subject to the ordinary provisions of obligations with a term" impose a separate sanction or whether they merely flow from the surrounding provisions as a corrolary to the main proposition. Even if a separate sanction is imposed thereby, it is doubtful if it is sufficiently express to warrant the pervasive effect given to it by the *St-Henri* line of cases.

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[19] *Id.*, at pp. 554-555.
[20] French: see n. 7.
[21] *Supra*, n. 11.
[22] *Supra*, n. 11 at pp. 39-41.
[23] *Supra*, p. 314.

It is submitted that the proper view of this provision is that a separate sanction is not imposed by Article 1561*i* over and above that of causing title to the property to pass to the purchaser. The only separate effect of the words "subject to the ordinary provisions of obligations with a term" might be to override any contractual provision aiming at depriving the purchaser of the benefit of the term in the absence of a default by him in any of his obligations. Nowhere in the provisions of the *Civil Code* concerning obligations with a term or in the rules of sale generally is there a suggestion that parties cannot agree on matters such as penalties, interest and similar items. Even Judge Trudel, in *St-Henri,* agrees that the solution proposed, namely the loss of finance charges, among other things, as well as the passing of title, is a sanction "évidemment draconienne",[24] although he suggests that it is one "... qui ne conduise pas à des conséquences pratiques, injustes ou inexplicables".[25]

The economic facts of life underlying conditional sales should not be overlooked.[26] Reduced to its simplest terms, the purpose of a conditional sale is to enable a vendor to make a sale on credit to a purchaser who cannot, or chooses not to, pay the entire sale price at the time of purchase. To reduce the risk of a loss on the transaction, the vendor reserves title to the property in question until the final payment is made by the purchaser. By so reserving title to the property, the vendor attempts to ensure that if a purchaser defaults in his obligations he can repossess his merchandise and recover or limit his loss. The property, therefore, remains a type of security for the vendor. Security is a concept separate and distinct from interest or finance charges, although from a commercial point of view it is obvious that the adequacy of security will have an effect on the cost of credit to a borrower. That this type of security may be subject to abuse is quite obvious and one need look no further than the many *Conditional Sales Acts* in force to deduce the practices which have had to be remedied by legislation. The general effect of legislation in this field has been to require certain formalities to be observed in contracts governed by the particular statute, in default of which the vendor loses his security and is placed in the same position as if he had been unable to take security under the conditional sale contract.

Looking again at the provisions of the *Civil Code,* there is no overt suggestion that the conditional vendor loses more than his

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[24] *Supra,* n. 11 at p. 41.

[25] *Supra,* n. 11 at pp. 41-42.

[26] See: Lubin Lilkoff, *Aspect social et technique de la vente à tempérament,* (1967) 27 R. du B. 1.

security as a result of non-compliance with the provisions of Articles 1561*a* and following; that he is placed in the same position as if he had contracted to advance money to the purchaser at the legal rate, with no provisions relating to default and other special conditions; or that he is to be worse off than a vendor who chooses not to take such security. One should not look beyond the express wording of the *Code* in order to obtain such a result, and Article 1561*i* contains no such provision. It would appear that the language of Article 1561*i* justifies only withdrawing the security of the conditional vendor and does not extend to voiding clauses in the contract not specifically related to the passing of title to the property.

Many of the provisions of the *Code* relating to conditional sales are unclear, whether by reason of conflicting jurisprudence, language or commercial practice. In some cases a conditional vendor simply may not know whether the goods he sells will come under the mandatory provisions of Articles 1561*a* and following. If in the future it becomes necessary for the vendor to enforce his rights, he may find that the contract is governed by the provisions of the *Code* and that the contract in question fails to conform fully with those provisions. If the present trend in the jurisprudence (to which exception has been taken herein) continues, the vendor will find that not only has his security disappeared, but also his finance charges have been reduced to the legal rate of interest, usually a rate considerably below that which the vendor has had to pay in order to obtain the use of the same money he now seeks to collect. In view of this, it is suggested that the inclusion of the following clause in the conditional sale contract itself might well be prudent:

> In any contract hereunder where the regular cash sales price as defined in Article 1561*c* of the *Civil Code* does not exceed $800 (other than sales under $800 to which reference is made in Article 1561*j* (*a* to *f*) of the Civil Code), title to the goods shall pass to the purchaser and this contract shall become a sale on terms. All other conditions of this contract (including without limitation the cost of borrowing and charges for default and deferment) shall remain in full force and effect, with the exception of those conditions which purport to grant to the vendor or its assigns any title to or real rights in the goods.

Even the most militant subscribers to the line of jurisprudence above referred to should have difficulty in refusing to give effect to such a clause.

2. Calculation of Finance Charges.

Until fairly recently there has been considerable doubt as to how the maximum allowable finance charges for contracts governed by the *Civil Code* articles on conditional sales should be calculated. The

matter is a crucial one, since failure to observe the provisions could result in the conditional vendor losing his security and, according to the majority of cases discussed above, the finance charges themselves, to the extent that the effective rate of interest of such charges exceeds the legal rate of 5% per annum. The calculation of finance charges is also a matter for considerable commercial analysis on the part of the conditional vendor or finance company, since these charges must be sufficient to cover his risks, losses and additional administration costs resulting from instalment sales. If the allowable rate under the legislation is not sufficient, the vendor must refuse instalment sale business or else sell outright and increase his finance charges to cover the increased risk resulting from having no security on the property which has been sold.

Assuming the contract in question is governed by the provisions of Articles 1561*a* and following, the applicable provision relating to the calculation of finance charges is Article 1561*d*, which reads as follows:

> The price of sale on the instalment plan consists in the regular cash sale price increased in a proportion not exceeding three-quarters of one percent of the total of the deferred payments for each month of the duration of the term, such increase being in lieu of the interest and compensation for the risks, losses and additional administration costs which may result to the seller by the sale on the instalment plan. The latter shall not be entitled to any other compensation or increase of the cash sale price, except interest on the deferred payments from the time they become due, at a rate not to exceed three-quarters of one percent per month.

It has been suggested that this Article would permit interest of 9% per annum on the total of the deferred payments at the commencement of the term. The proponents of this view base their interpretation on the words "of the total of the deferred payments", without, it seems, giving any meaning to the words immediately following, namely "for each month of the duration of the term". Some comfort was also gained from Faribault, who gives the following example of the calculation of finance charges:

> Un ameublement est vendu pour $500, prix régulier du marchand. Ce prix est payable à raison d'un paiement initial de $100; et le solde de $400 en vingt-quatre versements. A ce solde de $400 on ajoute pour frais de finance $0.75 centins par cent dollars, soit $3.00 par mois, ce qui forme un total de $82 *(sic)* pour le terme de vingt-quatre mois. Cette somme de $82 ajoutée à celle de $400 forme un total de $482, qui sera payable en vingt-trois versements égaux de $20.08 et un dernier versement de $20.11.[27]

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[27] *Traité de Droit civil du Québec*, Vol. 11, p. 410.

The Courts have not, however, (and correctly so) accepted this view of the wording of Article 1561*d*.[28] The earliest reported case is that of *Ferron* v. *Belisle*,[29] and the remarks of Caron, J., on the commercial treatment of the provisions of Article 1561*d* are of interest:

> Le commerce en général a décidé que trois quarts de un pour cent par mois équivalent à 9% par année (ce qui est vrai mathématiquement) et que le coût de finance doit être fixé en prenant 9% par année du solde dû lors de la vente. Si là eut été l'intention du législateur, il aurait été beaucoup plus simple pour lui de dire que le prix de vente à tempérament sera «le prix régulier plus 9% par année du solde dû lors de la vente». Ce n'est pas ce qu'il a dit.
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> Trois quarts de un pour cent doivent se calculer sur le total des versements différés pour chaque mois de la durée du terme. S'il s'agit d'un terme de dix mois à $8 par mois, le total des versements différés pour le premier mois sera de $80 et pour ce mois on calculera trois quarts de un pour cent de $80. Une fois l'intérêt ajouté, on déduira le premier paiement. Le résultat sera le total des neuf versements différés pour le deuxième mois. Encore là, calcul d'intérêt, déduction du deuxième paiement, et l'on a le total des versements différés pour le troisième mois. Ainsi de suite pour chaque mois.
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> Ce calcul sera de beaucoup plus compliqué que la simplification faite par le commerce en général, mais il sera d'après la loi et rien de plus ne peut être réclamé.[30]

A further and more recent decision on the point is *La Compagnie Légaré Limitée* v. *St-Amant*[31] which, without referring to *Ferron* v. *Belisle*, arrives at the same conclusion, that the maximum allowable finance charge is ¾ of 1% per month on the total deferred payments remaining unpaid at the end of each month of the term. A general statement of the relevant facts is sufficient to illustrate the method followed in calculating the charges and the view taken by the Court.

> Le prix de vente régulier a été majoré de beaucoup plus que de ¾ de 1%, tel que le veut l'art. 1561*d* C.C. En fait, cette majoration est de plus de 1% par mois et ce, en calculant le pourcentage non pas sur le «total des versements différés pour chaque mois» comme le veut encore l'art. 1561*d* C.C., mais sur le solde initial, sans teuir compte des versements mensuels effectués. Non seulement donc la majoration a été calculée à 9% par année du solde dû lors de la vente, comme le font la plupart des commerçants — ce qui

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[28] At least in cases where the court has specifically considered the point. See, however, *Commodity Discount Limited* v. *Dame Gagnon* (*supra*, n. 17) where the court allowed interest at 9% per annum on the note attached to a conditional sale contract. In *Canadian Family Food Plan Ltd.* v. *Cosgrove* (*supra*, n. 9) the rate of interest was expressed as 9% per annum, but no finding was made as to the method of calculation.

[29] [1958] S.C. 645.

[30] *Id.*, at p. 647.

[31] *Supra*, n. 14.

n'est pas moins illégal puisque le législateur a pris soin de spécifier non pas 9% par année du total des versements différés mais « ¾ de 1% du total des paiements différés pour chaque mois de la durée du terme» — mais à au moins 12% par année du solde dû lors des différentes ventes.[32]

This latter decision has been followed on this point in *M. Aber Inc.* v. *Deneault*[33] and *Circle Acceptance Co.* v. *Kerr*.[34]

Expressed as a rate per annum based on the original amount financed, the amount thus calculated amounts to 4½%. Even on the more accurate figure of 9% per annum on the amount outstanding from time to time, many vendors and finance companies find the maximum rate thus allowed insufficient to cover the cost of money, risk, administration costs and related matters. Care should now be taken, pending a revision of the legislation, to adjust, as suggested in Section 1 *(supra)*, what appear to be conditional sale contracts in order to provide that title to the goods passes, thus risking only a personal recourse against the purchaser in return for a more reasonable rate of return through finance charges.

3. The $800 Limit.

Article 1561*j* provides that the provisions of the chapter on Instalment Sales apply to commercial sales only at retail and not exceeding, in each case, eight hundred dollars. There are certain exceptions to this rule and also certain provisions which apply to all conditional sales and similar arrangements regardless of amount or type of moveable property involved. Would the provisions of the *Code* apply to a conditional sale in which the regular cash sale price was $750 before 8% sales tax, or in which the instalment plan sale price was $750 before such sales tax? Does Article 1561*j* refer to the cash sale price or the instalment sale price when it speaks of $800? Can a vendor argue that if the sale price plus sales tax equals $810, the contract is not governed by Articles 1561*a* and following?

The point was raised in *M. Aber Inc.* v. *Deneault*[35] in which it was held that the sales tax did not form part of the sale price and could not be added to the price in order to take the contract from the operation of the provisions of the *Code*. The ground for the decision was that the *Retail Sales Tax Act*[36] provides that the

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[32] *Id.*, at pp. 30-31.
[33] *Supra*, n. 6.
[34] *Supra*, n. 5.
[35] *Supra*, n. 6.
[36] R.S.Q. 1964, c. 71.

tax is payable by the purchaser, although it is collected by the vendor as agent for the Crown in right of the Province. This amount does not form part of the sale price; it is merely calculated with reference to it.

The *Aber* case did not raise the issue as to whether the cash sale price or the instalment plan sale price was the relevant consideration in determining the effect of Article 1561*j*. Suppose the regular cash sale price of goods purchased by conditional sale is $700, and the finance charges are another $150, bringing the sale price on the instalment plan of $850. Would this be a contract governed, in the absence of an exception under Article 1561*j*, by Articles 1561*a* and following? Would an initial payment of 15% be required under Article 1561*b*? The issue, of course, is whether or not a commercial sale at retail "not exceeding... eight hundred dollars" refers to the market value of the goods as expressed by the regular cash selling price or whether the governing figure would be the market value of the goods increased by the finance charges, or the sale price on the instalment plan.[37] In a chapter dealing with conditional sales it might be reasonable to assume that the decisive consideration would be to relate the provisions thereof to the amount of the obligation undertaken by the instalment purchaser, namely the instalment plan sale price. Whatever the merit of this approach, it is likely that the view which would be taken by the Courts if they are fixed squarely with the problem would be to extend the protection granted by the *Code* to the purchaser as far as possible and regard the regular cash sale price of the goods as determining. An indication of this approach may be gleaned from the *Aber* case, in which the discussion related to whether the addition of sales tax to the regular cash sale price of the merchandise in order to bring the total price over the $800 limit was permissible.[38]

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[37] To date, no reported decisions deal directly with this point.
[38] *Supra*, n. 6, at p. 390.