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Backgrounder

LRC 8—Report on Deficiency Claims and Repossession

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In this report, the commission is focussed on analyzing and evaluating one particular aspect of the law that governs debtor–creditor relationships, that of deficiency claims and repossessions. The commission makes recommendations, which would, if enacted, effectively limit and regulate remedies available to creditors that finance consumer purchases.

The report contains an introduction and six substantive chapters. The Report begins with a description of the buyer–seller relationship and mechanisms available to the seller to secure future payment and available remedies if the buyer defaults on payment. Typically, the security comes in the form of a security agreement, whereby the seller (or “secured party”) has an interest in the goods until the goods are paid for in full. If the buyer defaults on payment, the seller may repossess and sell the goods in question. If the proceeds of this re-sale are insufficient to satisfy the outstanding balance, the law in British Columbia permits the secured party to bring an action to claim the deficiency. This report examines those laws and their effects and makes a number of recommendations for reform, both in respect of the substantive rights of the secured party and of the procedure for enforcing its rights.

In chapter one, the report begins by examining a particular form of security agreement known as a conditional sales contract. The commission then examines three remedies available to the seller in the case of non-payment under a conditional sales contract: (1) action for the price; (2) repossession of the goods; and (3) deficiency claims. The commission also observes that in some instances, sale of the goods in questions will yield a surplus of funds. The commission observes that under the common law, an argument could be made that a re-sale constitutes a rescission of the original contract, and hence the buyer loses any further interest in the goods and cannot claim any part of the surplus in re-sale; in practice, most conditional sellers do in fact turn over surpluses to the buyer and express provisions to this effect are included in the contract.

The next chapter examines the law governing chattel mortgages and identifies remedies available to the seller and buyer in case of default. The report defines *chattel mortgage* as being, in principle, similar to a mortgage in respect of land, whereby legal ownership vests

in the seller, while equitable ownership (and usually possession) vests in the buyer. The commission noted that at common law courts concentrated on purely contractual aspects of the relationship. Hence, if even one payment was missed, the buyer, being in breach of contract, lost the benefit of any payments made thus far, as well as any rights to the property itself. The report then identifies three equitable remedies, which were effectively superimposed upon the common-law rules: (1) a mortgagor's right to redeem; (2) foreclosure; and (3) deficiency claims and surpluses. The commission identifies a fourth remedy—a contractual power of sale, which is commonly inserted into the chattel mortgage itself, providing the mortgagee with the power of sale and re-sale.

Chapter three contains an analysis of the present law governing concerning deficiency claims and repossession. In particular, the commission observes the potential for abuse inherent in the repossession and re-sale process; so long as a secured party has a re-sale judgment for the deficiency it has little incentive to maximize the re-sale price. Typically, security agreements provide a right of redemption, but no requirements exist that a secured party in possession give the debtor notice of this right of redemption. The commission also observes the inequity of circumstances insofar as no redemption period exists in respect of chattel mortgages; the mortgagee in a chattel mortgage may re-sell immediately upon repossession. While the courts are given wide discretion pursuant to the *Consumer Protection Act* to control the seller's right of repossession and sale, the law does not require debtors be notified of these powers.

In the following chapter, the commission observes the lack of reliable empirical studies in Canada concerning repossession and sale. The commission then notes it must rely on specific incidents brought to its attention as well as the experience of other jurisdictions. For example, the commission observes that in a California study of automobile sales there is a high incidence of what is termed as a "sweetheart deal." The commission points out that while California statistics may not be a completely accurate measure of British Columbia statistics, there is nothing indicating the practices governing deficiency claims and repossessions in California is significantly different from that of British Columbia. Thus, the high incidence of "sweetheart deals" is in fact a concern. The commission also notes that court records in British Columbia are not organized in such a manner that court records may be accurately assessed. The commission concludes by observing that certain aspects of the current law encourage the unscrupulous to extend credit and tempt debtors to avail themselves of it, and the necessity of remedial measures.

In chapter five, the commission set out the following four objectives that any amendments relating to the law of possession should achieve: (1) it should modify the repossession and re-sale procedure to eliminate potential abuse; (2) it should discourage the extension of credit to the "high risk" creditor who is likely to default; (3) it should give all debtors in default an adequate opportunity to redeem and notice of the right to redeem; (4) it should give the debtor notice of the court's jurisdiction to give relief from a repossession which is harsh and unconscionable. The commission notes that an appropriate method of achieving these aims lies in restricting remedies available to the secured party and observes that the remedial legislation falls broadly into two categories: (1) restricting the remedies of the secured party to the enforcement of his security; (2) requiring the secured party to choose

between enforcing his security, or suing on his debt. Alberta, Manitoba, and Newfoundland have adopted the latter approach; the commission recommends British Columbia adopt Alberta legislation to this effect. The commission also recommends implementing legislation which would allow a debtor under a chattel mortgage the right of redemption, similar to that given to a debtor under a conditional sales contract as well as a mandatory notice requirement to the debtor in all cases involving a security interest in consumer goods. The commission then recommends legislation stipulating the purchaser be entitled to any further surplus. Further, the commission recommends that where two thirds or more of the purchase price has been paid, a secured party may only re-possess upon court order, and that the court may direct the mode of sale to ensure that a realistic price is obtained.

Finally, in Chapter six, the commission provides a summary of its recommendations.

Further Developments

See *Conditional Sales Act, 1961 (Amendment) Act*, S.B.C. 1973, c. 19, ss. 5–7; *Bills of Sale Act, 1961 (Amendment) Act*, S.B.C. 1973, c. 7, s. 4 (both now *Personal Property Security Act*, R.S.B.C., 1996, c. 359, ss. 55–62).