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**Paul J. Omar**

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International Insolvency Institute

PMB 112

10332 Main Street

Fairfax, Virginia 22030-2410

USA

Email: [info@iiiglobal.org](mailto:info@iiiglobal.org)

# **Retention of Title Clauses in French Law**

by  
Paul J. Omar  
of Gray's Inn, Barrister

## **Introduction**

The principal text dealing with the law and institutions of insolvency in France is the Insolvency Law of 1985, introduced as the apex of the reforms thought necessary during the financial crisis of the middle 1980s.<sup>1</sup> This law did, however, not escape criticism, particularly by creditors who felt their rights declining in favour of the debtor. A new reform law was introduced in 1994 to redress some of these rights, including the rights of creditors to reclaim goods in the possession of the buyer.<sup>2</sup>

## **General Legal Provisions**

The Civil Code provides that a sale is complete between two parties where the legal interest in the property has been transferred from the seller to the buyer upon agreement as to the property to be transferred and the sale price whether the property has been delivered or the price paid or not.<sup>3</sup> The rule set out in the Civil Code is not mandatory and the parties are free to agree to alternative arrangements for the transfer of ownership in property, for example by delaying the transfer of ownership until payment has been made, through the use of a retention of title clause.<sup>4</sup>

Early case-law decided that a retention of title clause would be unenforceable in cases where the buyer went bankrupt. It was thought that possession of the goods might lead creditors to believe the buyer to be solvent and that such clauses could not be relied on in defence of creditors' claims so as to guard against the possibility of fraud and collusion.<sup>5</sup> French legislation stepped in later to permit the application of the clause despite the buyer's insolvency.<sup>6</sup> The clause now allows the seller to claim after the opening of insolvency proceedings either restitution of the goods or payment in lieu.

## **Drafting Conditions**

Title clauses may satisfy certain requirements as to form. The clause may generally be in writing. If the clause is not in writing, the seller's claim for the return of goods may be

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<sup>1</sup>Law no. 85-98 of 25 January 1985 on judicial administration and liquidation of businesses, implemented by Decrees no. 85-1388 of 27 December 1985. (References below to articles of a Law ('L') or Decree ('D') will be to this legislation).

<sup>2</sup>Law no. 94-475 of 10 June 1994 on the prevention and treatment of business difficulties, implemented by Decree no. 94-910 of 21 October 1994, which entered into effect the next day.

<sup>3</sup>Article 1583, Civil Code.

<sup>4</sup>Clause de Réserve de Propriété.

<sup>5</sup>Cassation requêtes, 21 July 1897.

<sup>6</sup>The provision appearing in early insolvency legislation was re-enacted as L. Art. 121.

rejected.<sup>7</sup> The clause may be clear and unequivocal so that the buyer could not be unaware of its existence.<sup>8</sup> The clause need not appear in a particular format and its use in any commercial document is sufficient for the purposes of the law. The clause should not be printed using small or illegible typefaces or be hidden among other generic clauses. The use of bold or underlined print is recommended so as to catch the buyer's attention.<sup>9</sup>

The use of a foreign language is allowed if the language is commonly used and is that of one of the contracting parties.<sup>10</sup> A reservation of title clause was previously enforceable only if it appeared in every document constituting a sale between the parties. Following the reforms in 1994, reference to a single document containing a clause and which governs a series of commercial transactions between the parties is permitted.<sup>11</sup>

### **Agreement to the Clause**

The contracting parties may agree a method for the transfer of title to property,<sup>12</sup> though this need not be subject to any formality or made in any particular manner. The party who wishes to enforce the contract bears the burden of proving the existence of an agreement. Agreement may be express or tacit. Agreement has been held express where a qualified representative of the buying company acknowledged receipt of the goods on a form mentioning the clause,<sup>13</sup> where the buyer acted through a legal representative,<sup>14</sup> or where the buyer's stamp placed on a delivery confirmation containing the clause.<sup>15</sup>

Tacit agreement may be shown to be certain and incontestable.<sup>16</sup> The seller may prove the buyer agreed to the contract with knowledge of the existence of the clause.<sup>17</sup> It is essential that the clause form part of a contract which is concluded no later than the time of delivery of the goods.<sup>18</sup> This condition may be satisfied when the clause is found in the delivery invoice signed by the buyer at the time of delivery.

### **Conditions relating to the Goods**

Retention of title clauses previously applied only to "merchandise", defined to mean goods sold in the course of business. The 1994 reforms use the term "goods", which covers not only merchandise, but also other chattels such as equipment. The owner of the property is entitled to bring an action for repossession. To establish ownership, the seller may prove that the goods in the buyer's possession at the time of the judgment

<sup>7</sup>Cassation commerciale, 16 October 1990.

<sup>8</sup>Cassation commerciale, 3 March 1992.

<sup>9</sup>Cassation commerciale, 15 July 1987.

<sup>10</sup>CA Paris, 28 January 1986.

<sup>11</sup>L. Art. 121.

<sup>12</sup>Article 1583, Civil Code.

<sup>13</sup>Cassation commerciale, 11 July 1983.

<sup>14</sup>Cassation commerciale, 12 December 1984.

<sup>15</sup>CA Paris, 20 June 1990.

<sup>16</sup>CA Versailles, 21 October 1987.

<sup>17</sup>Cassation commerciale, 27 June 1989.

<sup>18</sup>L. Art. 121(2).

opening insolvency proceedings are those that were delivered by the seller,<sup>19</sup> the price of which remains unpaid.<sup>20</sup> The goods may be either found *in specie* (*en nature*) at the date of the judgment opening insolvency proceedings or they may be bulk goods. The seller may reclaim goods incorporated in other items if removal may be done without causing damage.<sup>21</sup> The law in relation to the repossession of goods *in specie* now also applies to bulk goods found in the possession of the buyer, which may be of same type and quality as those delivered.<sup>22</sup> The onus is on the seller to prove that these conditions are satisfied for a claim to succeed.<sup>23</sup>

## **The Rules in Insolvency**

### **Recovering Property from the Debtor**

An action claiming an interest in property of the debtor may be brought by a third party within three months of the judgment instituting judicial administration or winding-up.<sup>24</sup> The reforms of 1994 modified many of the requirements for a creditor to prove an interest in property including, where the property is the subject of a contract between the third party and the debtor, extending this period to run from the date of the resolution of the contract.<sup>25</sup> Another important reform is the dispensation for any creditor, whose interest in the property has been advertised, from having to prove again his interest in the property in the insolvency proceedings.<sup>26</sup> A creditor in this situation has merely to address himself to the administrator to request the return of the property.<sup>27</sup>

In case of dispute, the *juge-commissaire* will pronounce on the interest of the creditor in the property.<sup>28</sup> Where the owner of the property does not come forward within a month of notice being given to claim an interest, the administrator may sell the property, proceeds from which will be held for the benefit of the owner, less any fees involved in the disposal.<sup>29</sup> Goods sold to the debtor under a contract which was dissolved prior to judicial administration being pronounced, whether by operation of law or according to the terms of the contract, may be reclaimed if they are still in existence at the time of the request.<sup>30</sup> Where judgment was obtained after the opening of judicial administration, the goods may be claimed if proceedings had been commenced prior to the judicial administration.<sup>31</sup>

<sup>19</sup>Cassation commerciale, 15 December 1992.

<sup>20</sup>Cassation commerciale, 6 March 1990.

<sup>21</sup>L. Art. 121(3).

<sup>22</sup>L. Art. 121(3).

<sup>23</sup>L. Art. 85-2.

<sup>24</sup>L Art 115(1).

<sup>25</sup>L Art 115(2) (inserted by the Law of 1994).

<sup>26</sup>L Art 115-1 (inserted by the Law of 1994)

<sup>27</sup>D Art 85-4(1) (inserted by the Law of 1994).

<sup>28</sup>D Art 85-4(2).

<sup>29</sup>D Art 85-4(3),(4).

<sup>30</sup>L Art 117(1).

<sup>31</sup>L Art 117(2).

Goods received by the debtor at his warehouse may be claimed by the vendor unless before they had arrived a sale was made to a third party without there being evidence of fraud or deception involved.<sup>32</sup> Goods which have not been expedited to the debtor may also be retained.<sup>33</sup> Merchandise delivered to the debtor on bail or for sale on behalf of the vendor may also be reclaimed.<sup>34</sup> The reforms of 1994 added several new instances where a third party could exercise rights over property in the hands of the debtor. Where goods sold subject to a clause retaining title, title to pass only in the event of the whole of the price being settled, are still in existence at the time of insolvency proceedings, they may be reclaimed, provided the clause was contained in a contract or written document bearing a date not later than the date of delivery of those goods.<sup>35</sup>

Where the contract provides for a retention of title clause, a seller may reclaim his goods as long as they exist *in specie* at the time of the judgment which initiates insolvency proceedings.<sup>36</sup> If a contract, which relates to a specific item of property, is the subject of publication to third parties, the seller is dispensed from having to prove his ownership of the property.<sup>37</sup> The claim for repossession of goods may be made within three months of the publication of the insolvency judgment by registered mail with a request for acknowledgment of receipt by the administrator.<sup>38</sup> An exception is made for goods the subject of a contract which is still running at the date of the insolvency judgment when the delay runs from the date of expiry or termination of the contract.

### **Mixed Goods: Incorporated**

There are two situations where goods may have been mixed. In the first instance, the vendor's goods may have been incorporated in goods belong to the debtor. In this situation, provided the vendor's goods may be detached from the ensemble without damage to either the vendor's or the debtor's goods, they may be reclaimed.<sup>39</sup>

### **Mixed Goods: Bulk**

In the second situation, goods supplied by the vendor may have been mixed with other goods so that a bulk is produced. Provided that goods similar in quality and nature to those supplied by the vendor are still in the debtor's hands, a quantity of the bulk equal to that supplied may be reclaimed. In either case, restitution may be avoided by the payment of the price of the goods, which may be subject to a delay approved by the *juge-commissaire*, who will also decide in situations where there is doubt as to the

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<sup>32</sup>L Art 118.

<sup>33</sup>L Art 119.

<sup>34</sup>L Art 121(1).

<sup>35</sup>L Art 121(2) (inserted by the Law of 1994).

<sup>36</sup>L. Art. 121.

<sup>37</sup>L. Art. 115-1.

<sup>38</sup>L. Art. 115-2.

<sup>39</sup>L Art 121(3) (inserted by the Law of 1994).

identity of the goods. This payment is treated as if it were a debt arising in the course of business after the opening of insolvency proceedings.<sup>40</sup>

### **Procedure for Recovery**

The administrator is empowered to deal directly with third parties in the event of claims for the return or restitution of goods and may agree terms, subject to the approval of the debtor. Where approval is not forthcoming, the *juge-commissaire* will decide after hearing the observations of all parties.<sup>41</sup> In the case of a sub-sale, the vendor may claim against the third party if the goods, sold to the debtor subject to a retention of title clause, have not yet been paid for,<sup>42</sup> even where the goods are no longer in the possession of the debtor.<sup>43</sup> If the price of the goods has been paid by the third party, the vendor may recover it from the debtor as a priority.<sup>44</sup>

The administrator may oppose the seller's claim to repossession by paying the price immediately. The law does not provide for any further extensions of time for payment of the price other than with the seller's consent. This payment is treated as a debt which occurs after the judgment initiating insolvency proceedings and may be paid in priority to other debts. By this means, the company may continue production through the regular supply of required materials. Sellers are protected in this instance by the requirement for prompt payment for any further supplies, unless other terms are agreed.

If the administrator does not agree to the restitution within one month as from receipt of request, the seller may file an order within one month as from the expiry of the time limit within which the administrator may reply. A claim for repossession of goods is treated in effect as a claim for restitution of the goods in question.<sup>45</sup> Conversely, it may be up to the administrator to act by notifying the seller of goods that goods exist over which a claim ought to be made. Goods which are not reclaimed within a month of notice being sent to the seller may be sold, the proceeds being deposited for the benefit of the seller.<sup>46</sup>

### **Recovery from a Third Party: Subsales**

Recovery of goods may be complicated if the buyer resells them to a third party. In general, the seller may not recover unpaid goods if these have been sold and delivered to a bona fide third party.<sup>47</sup> The seller may only recover goods where these have not yet been delivered to a third party. If the buyer has received bills of exchange or other payment for the goods from the third party, the seller may no longer exercise an action to recover the price from the third party. Any sums received by the buyer from a third party

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<sup>40</sup>L Art 121(4).

<sup>41</sup>L Art 121-1 (inserted by the Law of 1994).

<sup>42</sup>L Art 122.

<sup>43</sup>Cassation commerciale, 27 May 1986.

<sup>44</sup>D Art 85-3 (inserted by the Law of 1994).

<sup>45</sup>Cassation commerciale, 13 Feb. 1990.

<sup>46</sup>D. Art. 85-4.

<sup>47</sup>Article 2279, Civil Code.

may be deposited with the administrator in cases of insolvency for the benefit of the creditor.<sup>48</sup> Where the third party has not paid for the goods, the seller has the right to claim payment directly from that party. The seller has the right to claim only the original sales price, not the price at which the goods were resold.<sup>49</sup>

### **Recovery from a Third Party: Bailees**

The seller may expect problems where other third parties are in possession of and lay claim to the goods. This may occur in the situation of a mortgagee, a lessor, a secured creditor, or a bailee creditor, defined as a creditor holding on to goods while awaiting payment for services effected in connexion with the goods. A general rule is that where the third-party is acting in good faith, his claim prevails and the goods may be sold to acquit this debt in priority, especially where this debt is sufficiently important. The rules are not however clearly established and the problem may need to be approached on a case by case basis.

### **Incidental Costs**

A seller may repossess goods that have been altered as long as they remain *in specie*. the buyer may need, however, to be compensated for any increase in value due to the buyer's alteration. The calculation of reasonable costs should avoid calculating both the cost of the alterations and the corresponding increase in value to the goods. Credit should be given for the cost of alterations.

### **Insurance**

The agreement should provide for which party will bear the risk of loss and it is recommended that the parties insert a clause as to who bears the cost of insurance. In the absence of any agreement, the general principle in contract law is that the burden of loss falls with the party in possession of the goods. An exception applies to contracts for the sale of goods under retention of title clause where the burden of loss falls with the owner of the goods. In this instance, the seller will remain responsible for insuring against loss.

Where goods sold with a retention of title clause are destroyed and where the seller remains the owner, any proceeds from an insurance policy are not paid into the buyer's estate, but to the seller.<sup>50</sup> It has been held that where the seller receives insurance proceeds for the destroyed goods, the seller must reimburse the buyer for any partial payments that have previously been made.<sup>51</sup>

### **Transfer of the Contract to a Third Party**

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<sup>48</sup>D. Art. 85-3.

<sup>49</sup>Cassation commerciale, 15 January 1991.

<sup>50</sup>Cassation commerciale, 6 July 1993.

<sup>51</sup>Cassation commerciale, 20 November 1979.

### **Subrogation by the Seller**

Subrogation may occur when the seller receives payment from a third party, which extinguishes the debt owed to the seller.<sup>52</sup> The consent of the buyer is not necessary for subrogation to take place.<sup>53</sup> The act which, although not subject to the civil code formalities in respect of transfers of debt,<sup>54</sup> may not occur after the date of payment.<sup>55</sup> In situations where the buyer becomes insolvent, there is no need to distinguish between cases where a claim is exercised by a seller or by a subrogated third party. The third party is able to exercise all those rights which the seller could exercise against the buyer.<sup>56</sup>

### **Subrogation by the Buyer**

Where the buyer takes out a loan to pay for the goods and wishes to subrogate the lending institution to the seller's rights, the loan agreement must be notarised and mention specifically the fact that the loan was taken out for the purposes of paying for the goods.<sup>57</sup> The debtor does not need the permission of the seller to negotiate this type of agreement.<sup>58</sup>

### **Conflict of Law Rules**

#### **Traditional Rules**

The rules which apply reservation of title clauses may be divided into three categories. Contract law favours the *lex contractus*, the law chosen by the contracting parties at the formation of the contract of sale although these rules have been supplemented by the choice of law rules set out in the Rome Convention.<sup>59</sup> Property law, and the law of real property especially, favours the *lex rei sitae*, the law of the country in which the goods are situated at the time of the claim. The law of insolvency applies the *lex fori*, which is generally that of the debtor's domicile.

Where the buyer becomes insolvent, the seller may wish to sue for recovery of the goods. However, the buyer may have resold the goods to a third party while the goods were still in transit to him or while in his possession, despite any retention of title clause which forbids disposal of the goods until full payment is made. A claim may be complicated by two factors. In the first instance, there may be no direct contractual tie between the seller and the third party and the seller may not be able to subrogate himself to the position of the buyer. Furthermore, the law applicable may have changed, either because the buyer

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<sup>52</sup>Article 1250(1), Civil Code.

<sup>53</sup>Cassation civile 1, 23 October 1984.

<sup>54</sup>TGI Seine, 28 January 1965, declining to apply Article 1690, Civil Code.

<sup>55</sup>Cassation commerciale, 14 December 1965.

<sup>56</sup>Cassation commerciale, 15 March 1988.

<sup>57</sup>Article 1250(2), Civil Code.

<sup>58</sup>Cassation civile 1, 13 February 1963.

<sup>59</sup>Official Journal of the European Communities L 266/1 of 9 October 1980.



and third party have agreed on a different contractual law or because the application of one of the principles above leads to a different law being applied.

Because it is generally the law of the forum which applies to insolvency proceedings, the application of the law chosen by the parties to a retention of title may be subject to conditions imposed by French law. In cases of conflict, and where the debtor is normally resident within the jurisdiction, courts will apply their procedural and substantive laws to proceedings within their own jurisdictions to the exclusion of other systems of law. This rule may result in the recognition of those retention of title clauses which comply with the forms requirements of French law. Other typical clauses in use in other jurisdictions, especially those which provide for retention of title to apply even to goods transformed beyond recognition or incorporated into other goods, such as exist in German law, may not be recognised as having any effect.<sup>60</sup>

### **Vienna Convention (International Sale of Goods)**

A seller who has taken the precaution of inserting a reservation of title clause into a contract expects the clause to be effective, whether or not the goods are to be shipped to a buyer resident in a different legal jurisdiction. Despite the best efforts of legal reformers, there are to date no uniform laws within the European Union with regard to title clauses. Similarly, the Vienna Convention, which sets out a code for the international sale of goods, conspicuously fails to mention any rules governing the transfer of property over and title to goods, referring any disputes to the application of the relevant domestic law.<sup>61</sup>

### **The European Bankruptcy Convention**

The European Bankruptcy Convention is the product of the deliberations of one of the working parties were set up to consider the extension of the Treaty of Rome by way of convention, in line with the undertakings "to secure the simplification of formalities governing the reciprocal recognition and enforcement of judgments of courts or tribunals."<sup>62</sup> This working party, set up in 1963, produced a report in 1970, together with a draft convention annexed. Successive drafts have not met with any greater enthusiasm though commentators have continued to argue the case for a convention throughout the years.<sup>63</sup> Despite receiving the approval by the Council of Ministers in late November 1995, the final draft version has not to date been translated into a formal convention.

The convention applies to the insolvency of debtors where divestment of assets may occur subsequent to the appointment of a liquidator and which may involve the liquidation of these assets.<sup>64</sup> In cases of reservation of title, insolvency proceedings

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<sup>60</sup>Cassation commerciale, 8 January 1991.

<sup>61</sup>See Bassindale and Fletcher, The Vienna Convention [1992] 1 ICCLR 10.

<sup>62</sup>Article 220, Treaty of Rome.

<sup>63</sup>See Muir Hunter, The Draft EEC Bankruptcy Convention: A Further Examination (1976) 25 ICLQ 310.

<sup>64</sup>Draft Article 1(1).

may not affect the rights of a seller where the assets are situated at the time proceedings are opened in another convention state. Where it is the seller who is the subject of insolvency proceedings, this fact may not be used as grounds for the resolution of the contract and does not prevent the acquisition of title by the purchaser where the goods are in another convention state.<sup>65</sup>

However, it is the law of this main jurisdiction that will govern many of the substantive issues during proceedings.<sup>66</sup> These issues are defined to include the identity of the debtors against whom proceedings may be brought, the identification of the assets which will form part of the estate as well as the treatment of assets the debtor acquires or inherits after proceedings are opened. Furthermore, the powers of the debtor and liquidator during proceedings, the rules governing set-offs, the effects of insolvency on current contracts and other proceedings, with the exception of pending lawsuits (which fall to be judged according to the laws of the place they were instituted), are all governed by the substantive law of the main jurisdiction. There is potential for conflict between these substantive rules and the rules relating to retention of title clauses, a situation that will have to be resolved by the decisions of the European Court of Justice.

### **Conclusion**

The retention of title clauses meets some of the issues raised by the questions involving transfer of property and risk. Nevertheless, in the absence of uniform rules at a supranational level, domestic courts are still required to deal with these clauses. In France, the courts adopt an orthodox approach to the formalities governing the nature, content and effect of a reservation of title clause, which may result in clauses drafted by a foreign seller being ineffective. These conflicts may be aggravated by further issues arising from the transfer of title to the goods or rights under the contract to third parties, which may involve conflicts of law.

The production of a convention which sets out a rule to govern the use of retention of title clauses in insolvency is overdue. Similarly, it is perhaps time that consideration is given at an international level to the production of a uniform set of rules governing the creation, validity and enforcement of retention of title clauses. This would do much to settle the often vexing problems that these clauses create.

**20th February 1996**

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<sup>65</sup>Draft Article 5.

<sup>66</sup>Draft Article 3.