# LAY-BY AGREEMENTS IN NEW ZEALAND

## I INTRODUCTION

There has been little written on lay-by transactions, probably because of the apparent simplicity of the lay-by contract. Lay-by is mentioned in only three legal texts[1], has not been the subject of litigation in this country, and is not defined in any judicial dictionary. But this does not mean that no legal problems arise in lay-by trading. Uncertainties arise as to the risk in lay-by goods, and also as to the purchaser's position in the case of the vendor's bankruptcy. These uncertainties basically arise because it is not settled when property passes in a lay-by contract. Another problem is the great variety of terms found in lay-by contracts. Terms are often extremely harsh, especially those applicable in the case of default by the purchaser.

It is for these reasons that this paper is essentially reform-orientated. Particular reference will be made to the Lay-By Sales Act of New South Wales (hereinafter referred to as the N.S.W. Act)[2], an Australian Act which specifically regulates lay-by sales.

## II NEW ZEALAND LAY-BY PRACTICE

### 1. The Nature of Lay-By Transactions:

A lay-by transaction will normally fall within section 3 of the Sale of Goods Act 1908 as either a "sale of goods", or an "agreement to sell goods". Which it is depends upon the passing of property under the agreement. A lay-by sale is very similar to a credit sale by instalments, the essential difference being that in lay-by the vendor retains possession of the goods until the whole of the sale price has been paid by the purchaser.[3] The retention of the lay-by goods by the vendor is an extremely important feature of a lay-by transaction.[4]

Unlike New South Wales, New Zealand has no legislation specifically governing lay-by sales. Sales will, however, be subject to two important pieces of legislation which generally regulate the sale of goods in New Zealand. Lay-by agreements will be subject to the Sale of Goods Act, unless the agreement excludes the operation of that Act. Agreements will also be subject to the Hire Purchase and Credit

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1. Yorston & Fortesque, "Australian Mercantile Law", 1965, p. 235; Sutton "Sale of Goods in Australia and New Zealand", p. 23; Else-Mitchell & Parsons, "Hire Purchase Law", 1968, p. 24.
2. Act no. 36, 1943. See also legislation note, (1944) 17 A.L.J. 281.
3. In some rare cases, the purchaser might only have to pay a portion of the sale price before receiving the goods. Such an agreement would still come within the definition of a "lay-by sale" under section 2 of the N.S.W. Act.
4. For discussion on the appropriation of goods to lay-by contracts see p.13.

Sales Stabilisation Regulations 1957,[5] unless the instalments are to be paid over a period of less than nine months. Under Regulation 2

> "Credit Sale Agreement" means an agreement for the sale of goods under which the whole or part of the purchase price is payable by instalments, other than such an agreement that provides for the instalments to be spread over a period of less than nine months.

What constitutes an "instalment", the Regulations do not say. Dictionary definitions of the word are very general. Mozley and Whitley[6] say it is a sum of money less than the whole sum due, paid by a debtor in partial liquidation of the debt. Osborne and Grandage[7] define it simply as a payment on account. It would seem that this is the correct approach. When a contract comes within the purview of the Regulations, instalments under that contract must be of approximately equal sums paid at approximately equal intervals.[8] By inference, then, an "instalment" as ordinarily defined will not necessarily have these characteristics. Thus, although instalments under lay-by agreements are often paid in unequal amounts at irregular intervals, it would seem that the agreements still constitute sales by instalments under the Regulations.

It will be noticed that Regulation 2 does not mention possession in defining a "credit sale agreement". Therefore, a lay-by transaction falls within that definition. On the same ground, it is also possible to say that a lay-by sale falls within the definition of a "hire purchase agreement" under the Hire Purchase Agreements Act 1939. Section 2 of that Act includes within the definition of a hire purchase agreement, an "agreement for the purchase of goods by instalments". Once again, no mention is made of possession of the sale goods. However, in the case of the Hire Purchase Agreements Act this is an interesting, but academic point. The provisions of that Act are clearly designed to apply to the case where the purchaser has possession of the goods, and are of no use in the lay-by situation.

## 2. Different types of Lay-By Transaction:

In preparing this paper the writer studied a large number of lay-by agreements used by retail stores. These included four large department stores, and a number of shops dealing in diverse ranges of goods such

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5. S.R. 1957/170 (reprinted with amendments: S.R. 1967/192). Since the reprint and up to 31st August 1970 there have been the following amendmends: 1967/205 of 11 September 1967 (Amendment No. 15); 1968/37 of 18 March 1968 (Amendment No. 16); 1968/75 of 13 May 1968 (Amendment No. 17); 1968/230 of 5 December 1968 (Amendment No. 18); 1969/119 of 30 June 1969 (Amendment No. 19); 1969/187 of 15 September 1969 (Amendment No. 20).
6. "New Zealand Law Dictionary", 1964, p. 15.
7. "Concise Commercial Dictionary", 1966, p. 115.
8. First schedule clause 4.

as furniture, menswear, jewellery, electrical equipment, women's fashions, shoes, groceries, and several travel agencies. This study disclosed that there are three different types of lay-by agreement.

The first type of transaction involves the sale of a specific chattel. At the time of the agreement the chattel is selected by the purchaser, and although the chattel remains in the possession of the vendor, it is appropriated by him to that particular lay-by sale. Most stores have a special "lay-by room" where such appropriated goods are set aside. These goods are tagged with the lay-by contract number, and are ready for delivery to the customer immediately upon the completion of payments. This type of transaction is by far the most common for goods of all types, and is used almost without exception by retail stores. Where the lay-by agreement provides that property immediately passes to the purchaser, this will be a "sale of goods" under section 3 of the Sale of Goods Act. Usually, however, the agreement does not mention the passing of property. In such a case this will only be an "agreement to sell goods" under the Act.[9]

The second type of transaction involves not a specific chattel, but rather a specific kind of chattel. The actual chattel to be sold to the purchaser is not selected at the time of the agreement, but the type and make are agreed upon by the parties (e.g. a "Conway heater", costing $20). This will always be an "agreement to sell" under section 3 of the Sale of Goods Act.

The third type of transaction involves neither a specific chattel nor a specific kind of chattel. The purchaser simply agrees to "lay by" money with the vendor. He selects his goods at a later date. An example of this is the so-called "Christmas Club". It is to be noted that in the New Zealand Lay-by Sales Report[10] such a transaction is regarded as an "unsecured deposit", rather than as an example of lay-by. Indeed, such a transaction simply amounts to an agreement to buy and sell an undetermined number of undetermined goods (which may or may not be "future" goods) for an undetermined price. As such, it might be questioned whether the agreement amounts to "an agreement to sell goods" under section 3 of the Sale of Goods Act. It is, however, "lay-by" within section 17(1) of the N.S.W. Act, a point which takes on further importance later in the paper.[11]

### 3. Prevailing Terms of Standard Agreements:

Most retail stores do not have written documents for lay-by sales. In most cases an ordinary sales docket is written out, and the words "Lay-by Sale" added to transform it into a lay-by document. This

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9. See p.16 et seq.
10. Submitted to the Minister of Justice by the Contract and Commercial Law Reform Committee in August 1969. See also article on the Report by Coote [1970] Recent Law 177.
11. See p.25.

means, of course, that with no terms and conditions written down neither party will have a clear idea as to his rights and obligations under the contract. Often no regular payments are required, and such agreements which are not of less than nine months duration will therefore be void under the Hire Purchase and Credit Sales Stabilisation Regulations 1957. Regulation 10 allows the purchaser to recover money paid over in such a void agreement. In most cases stores claim that a full refund will be given where the purchaser defaults on payment. This will, however, vary with different types of goods. For example, if a carpet has been cut for a lay-by sale, the defaulting purchaser would rightly forfeit a substantial amount. It is only in the case where the vendor recovers more than his actual loss on the uncompleted sale that real objection can be taken.

Two important exceptions to stores using unwritten lay-by agreements are those which deal in women's fashions, and the large department stores.

Most women's fashion stores use a cash sale docket which has printed on it the conditions of any lay-by sale. On their face, these conditions are often extremely harsh. Generally a deposit amounting to half the price of the goods must be made at the time of the agreement; payments have to be made at least once a fortnight, and the purchase must be completed within two months. In the case of purchaser's default, money will not normally be refunded, nor will it be credited towards other goods.[12]

On the other hand the department stores have "lay-by record cards" which, as well as providing for the recording of payments, have the terms of the contract written on them. The department stores are fairly consistent in the terms of their agreements, most providing that:

First, in the case of fashion goods, at least 20% deposit be paid, the purchase to be completed within three months.

Secondly, on all other goods, at least 10% deposit be paid, the purchase to be completed within six months.

Thirdly, in all cases further instalments have to be paid at least once a month.

Fourthly, in the case of default by the purchaser, the firms varied in their attitudes. Two agreements stated that all money paid would be forfeited, another stated that only the deposit would be forfeited, and the fourth that deposits and instalments would be forfeited only

12. This is not always as unreasonable as it may seem, depending on the amount paid and therefore forfeited. Women's fashion lines apparently change very rapidly, and a store could lose quite heavily on a garment set aside in "cold storage" for a lay-by purchaser for two months. However it is still inequitable if the vendor retains the purchaser's money in excess of his loss on the goods.

to the extent of any loss or expenses incurred by the store because of the purchaser's failure to complete the contract. It is to be noted that this last provision bears striking resemblance to those of the N.S.W. Act.[13]

Fifthly, one agreement mentioned risk. Under the terms of that agreement goods were to be held at the purchaser's risk.

Although the lay-by staff generally claimed a wide discretion to waive or vary terms, it can be seen that some consistency would be desirable as far as terms are concerned. This point will be considered below with the question of legislative reform.[14]

## III LEGAL ANALYSIS OF LAY-BY TRANSACTIONS

### 1. Problems Arising:

The first problem arising in a lay-by transaction is that of passing of property. The intention of the parties will rarely appear on the face of the contract, and the provisions of the Sale of Goods Act tend to cloud the issue rather than clarify it. In the end, it appears that property does not pass under a lay-by contract until payment is completed.[15]

Associated with the property question is that of risk in lay-by goods. Who bears the risk in lay-by goods? Will such goods be covered by the vendor's normal insurance, or, by that of the purchaser?[16]

A more frequent problem is that of the purchaser's position where the lay-by seller goes bankrupt. The position here would generally seem to be that the purchaser ranks only as an unsecured creditor, and that he stands to lose a considerable amount of his money.[17] Associated with this is the problem of the vendor defaulting, not through bankruptcy, but because of dishonesty. Lay-by offers considerable scope for the "con man", for the purported vendor is able to take possession of the purchaser's money, and does not have to produce any goods until the transaction is completed. By this time he has had a good chance to abscond, leaving the purchaser with little remedy.

The last major problem area concerns the harsh terms and conditions often found in lay-by contracts. There is a special problem where the purchaser defaults, because, as has been shown, this often results in forfeiture of the deposit and all instalments paid by the

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13. See p. 25.
14. See pp. 25, 28 and 29.
15. See pp. 19–20.
16. See p. 20 et seq.
17. See p. 22 et seq.

purchaser. As such default may be caused by events quite beyond the purchaser's control, such as illness, such a condition may be far from equitable. This point, like the others mentioned above, will be treated in the following sections of the paper.

## 2. Passing of Property:

The two writers who do mention the passing of property in a lay-by agreement treat it as well settled that, in the case of specific goods, property passes at the time of the agreement, unless the parties have a contrary intention.[18] In the case of unascertained goods these writers consider that property passes when the goods have been ascertained.

It is submitted, however, that the position is not altogether that clear. Section 19 of the Sale of Goods Act reads:—

> (1) Where there is a contract for the sale of specific or ascertained goods, the property in them is transferred to the buyer at such time as the parties to the contract intend it to be transferred.
>
> (2) For the purpose of ascertaining the intention of the parties, regard shall be had to the terms of the contract, the conduct of the parties, and the circumstances of the case.

The section says, in effect, that property passes when it is intended to pass. But the intention of the parties is far from clear in most cases. It would be rare for either of the parties involved to understand the concept of property passing, and it is unusual for the contract to expressly state when property passes. This means that rules 1 and 5 of Section 20 of the Sale of Goods Act must be applied. Section 20 attempts to clarify the position by setting down a number of rules to ascertain the intention of the parties. Rule 1 reads:—

> Where there is an unconditional contract for the sale of specific goods, in a deliverable state, the property in the goods passes to the buyer when the contract is made, and it is immaterial whether the time of payment or the time of delivery, or both, is postponed.

In a lay-by sale involving specific goods, such goods would normally be in a "deliverable state", and, at first glance, it would appear that property passes when the agreement is made. But it seems questionable whether a lay-by sale is an "unconditional contract" within the meaning of rule 1.

There is considerable contention over the meaning of "unconditional contract" in rule 1. Of the two alternatives, one is preferred by the writers, and the other seems supported by the cases. The first

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18. Yorston & Fortesque, op. cit., p. 235; Sutton, op. cit., p. 23.

possibility is that "unconditional contract" means a contract not subject to a condition precedent or subsequent. This seems a reasonable meaning, as throughout the rest of the Act the term is used in this sense. Thus section 3(3) says that a contract of sale may be absolute or conditional, which clearly means subject to a condition precedent, or else there would be no point in the contrast. As well as this, rules 2, 3 and 4 of section 20 all deal with contracts subject to a condition precedent, so it would be reasonable to infer that rule 1, by contrast, deals with contracts which are not subject to such conditions. However, section 13(3) of the Act complicates the position. This section deprives the purchaser of his right to reject goods for the breach of a condition if the contract is for specific goods, the property in which has passed to the buyer.[19] Therefore, if the above meaning of "unconditional contract" is accepted, property will pass in virtually all contracts involving the sale of specific goods, and the right to reject will be lost in these cases.

It is probably for the above reason that the courts appear to have suported the other meaning of "unconditional contract". Under this view, the words mean a contract not containing any conditions in the sense of vital terms. In *Varley* v. *Whipp*[20] there was a contract of sale for a reaping machine which the purchaser had never seen. The machine was described as being virtually new, but when it was delivered it did not conform with that description, and the purchaser tried to repudiate the contract. In an action for the price the court held that this was a sale by description under section 15 of the Sale of Goods Act. There was, therefore, an implied condition that the goods should correspond with the description. As there had been no acceptance of the machine by the purchaser within the meaning of section 37 of the Act, property had not passed to the purchaser, and the plaintiff was not entitled to recover. It can be seen that in *Varley* v. *Whipp* the right to reject did survive the making of the contract, and that therefore property had not passed under section 20 rule 1. This was made clear by Channell J. when he said that he did not think that this was "an *unconditional* contract for the sale of specific goods".[21] Similarly, in *Ollet* v. *Jordan*[22] it was held that a contract of sale which was subject to an implied condition of fitness for purpose was not an "unconditional" sale.

It would seem from these cases that property only passes under section 20 rule 1 where a contract is "unconditional" in the sense of having no essential stipulations, or conditions. This would lead to an apparently absurd result however. There are few contracts which do not have at least some conditions, for example, the implied conditions

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19. The Misrepresentation Act 1967 (U.K.) is not in force in New Zealand.
20. [1900] 1 Q.B. 513.
21. Supra p. 517, emphasis supplied.
22. 1918 2 K.B. 41. Note also, supporting dicta in *Leaf* v. *International Galleries* [1950] 2 K.B. 86, and in *Long* v. *Lloyd* [1958] 1 W.L.R. 753.

of the Sale of Goods Act. It is therefore difficult to imagine a situation in which property would pass under section 20 rule 1.

A condition precedent is normally regarded as a condition which must be fulfilled before the contract becomes binding on one or both of the parties. For example, where a contract is subject to the approval of a third party, this approval would be a condition precedent of the contract. In *Bentworth Finance Ltd.* v. *Lubert*[23] the non-fulfilment of the condition precedent was taken to prevent the formation of the contract. It is submitted, however, that the preferable view is the non-fulfilment of the condition precedent only suspends the obligations of one or both of the parties under the contract.[24]

The question in the lay-by situation is whether the purchaser's obligation to pay is a condition precedent of the contract. It is submitted that it is not. It is clear that there is a binding contract on the parties before the fulfilment of this condition by the purchaser.[25] It is, of course, also clear that the vendor's obligation to deliver the goods is suspended until the purchaser has paid the price. But section 20 rule 1 says it is immaterial that both the time of payment and the time of delivery are postponed.[26] Thus, where delivery is postponed until payment, this does not amount to a contract subject to a condition precedent. As Romer, L. J. said, *obiter dictum*, in *Re Anchor Line (Henderson Bros.) Ltd.*[27],

> "It follows, in the view of the legislature, that where, under a contract for a sale of specific goods in a deliverable state, the time of payment or the time of delivery or both be postponed, the contract is not a conditional contract. It further follows that in such a contract, if the postponement of payment of the purchase price and the delivery of the goods can properly be described—as indeed in one sense they can properly be described—as a postponement of the completion of the purchase, the property will pass on the entering into the contract, although in that sense completion of the purchase price be deferred."

So far as section 20 rule 1 is concerned, then, it is unclear when property will pass in a lay-by sale of specific goods. This is because of the uncertainties surrounding the words "unconditional contract". Unfortunately, when property will pass in a lay-by sale of unascertained goods is also unclear.

Section 18 of the Sale of Goods Act says that in a contract of sale of unascertained goods, no property will pass until the goods are ascertained. Section 20 rule 5(1) then says:—

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23. [1968] 1 Q.B. 680.
24. *Aberfoyle Plantations Ltd.* v. *Cheng* [1960] A.C. 115.
25. Thus, if the purchaser does not complete the payment of the price he will be in breach.
26. See p. 16.
27. [1937] Ch. 1, 9.

> Where there is a contract for the sale of unascertained or future goods by description and goods in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods thereupon passes to the buyer. Such assent may be expressed or implied, and may be given either before or after the appropriation is made.

Like rule 1, rule 5(1) would seem of reasonably clear application, were it not for the doubt surrounding the word "unconditional". In this case it is used in the sense of an "unconditional appropriation". In *Carlos Federspiel & Co. S.A.* v. *Charles Twigg & Co. Ltd.*,[28] Pearson J. said:—

> "To constitute an appropriation of the goods to the contract, the parties must have had, or be reasonably supposed to have had, an intention to attach the contract irrevocably to those goods, so that those goods and no others are the subject of the sale and become the property of the buyer."

In a lay-by sale this appears to be the case. Once the vendor has appropriated the goods to the contract he will be in breach if he removes them, without there having been any prior breach by the purchaser. It is difficult to see this as other than an "unconditional appropriation", although in *Stein, Forbes & Co. Ltd.* v. *County Tailoring Co. Ltd.*[29], Atkin J. seemed to think otherwise. In that case, which involved a c.i.f. contract, Atkin J. expressed the opinion that usually an appropriation will not be unconditional if the seller only means to let the buyer have the goods on payment. In the lay-by situation, though, the preferable view might be that it is not the appropriation which is conditional, but rather the delivery. This would mean that in a lay-by sale of unascertained goods, property would pass under section 20 rule 5(1) when the goods were appropriated to the contract.

In conclusion, it must be stated that section 20 rules 1 and 5(1) do not provide any clear cut answer as to the transfer of property in lay-by agreements. Their application to the lay-by situation seems unclear. It would seem, though, that section 21 of the Act may provide a better clue. The section reads:—

> (1) Where there is a contract for the sale of specific goods, or where goods are subsequently appropriated to the contract, the seller may, by the terms of the contract or appropriation, reserve the right of disposal of the goods until certain conditions are fulfilled.

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28. [1957] 1 Lloyd's Rep. 240, 255.
29. (1916) 86 L.J.K.B. 448.

(2) In such case, notwithstanding the delivery of the goods to the buyer, or to a carrier, or other bailee for the purpose of transmission to the buyer, the property in the goods does not pass to the buyer until the conditions imposed by the seller are fulfilled.

In a lay-by sale of specific goods, the vendor has clearly sold or agreed to sell those specific goods to the purchaser in question. As has been pointed out, if he does not sell those specific goods to the purchaser, he would be in breach of contract, provided that the purchaser has adhered to his part of the bargain. But in a lay-by sale it is agreed that the vendor will not hand over physical possession of the goods until he has received the full purchase price. If this means that the vendor has reserved his right to dispose of the goods, then under section 21(2) the property does not pass to the purchaser.

A good example of this is *In Re an Arbitration between Shipton Anderson & Co. and Harrison & Co. Ltd.*[30] The owner of a specific parcel of wheat held in a warehouse sold it upon the terms "payment cash within seven days against transfer order". Before the goods were delivered to the buyer they were requisitioned by the Government under wartime powers it then had. One of the questions to be decided by the Court was whether property in the goods had in fact passed to the buyer before their delivery and therefore before the requisition. The Court held that it had not. In the words of Lush J.:—

> "The vendors stipulated that until payment was made the goods should remain in their possession, and that retention of the jus disponendi prevented the property passing."[31]

In that case then, the vendor reserved the right to dispose of the goods within the meaning of section 21(1), by stipulating that he should retain possession until payment. As this is also the lay-by situation, then it would seem that section 21 of the Sale of Goods Act prevents property passing in a lay-by sale until payment has been completed. This will be the case even in a sale of specific goods, unless the parties express a different intention. This point is of special importance as far as the risk in lay-by goods is concerned, and also where the vendor goes bankrupt.

### 3. Risk in the case of Loss or Damage to Lay-by Goods:

Risk is, *prima facie,* associated with property under section 22 of the Sale of Goods Act:—

(1) Unless otherwise agreed, the goods remain at the seller's risk until the property therein is transferred to the buyer; but when the property therein is transferred to the buyer the

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30. [1915] 3 K.B. 676.
31. Supra. p. 684.

goods are at the buyer's risk, whether delivery has been made or not:

Provided that where delivery has been delayed through the fault of either buyer or seller, the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault.

It would seem reasonable that the vendor should cover lay-by goods en masse under his own insurance rather than expect each purchaser to arrange separate cover. However, lay-by goods might not always be covered under the vendor's normal insurance policy.

Clearly, where the lay-by goods remain the vendor's property they will come within the purview of a normal Comprehensive Policy. But if the property has passed to the purchaser, this will probably not be the case, and the vendor will have to take out a separate cover on the goods.

It appears that the vendor has an insurable interest in lay-by goods, even if they are not his property. He has a lien over the goods until he has received payment. As a lien, by its nature, extends to the whole and every part of goods, however small a sum is involved, then any loss or damage to the goods would necessarily diminish the value of the security. A person with a lien over goods thus has an insurable interest in them.[32]

A vendor might not have to take out a separate cover on lay-by goods which are not his property, if he has an "O.T.C. Clause" in his insurance policy. Such a clause refers to goods held by the insured "in trust or on commission", and is found in many commercial policies.

Lay-by goods are clearly not held "on commission", but they might be classed as goods held "in trust". The words "held in trust" are to be read in a general commercial sense, rather than a strictly legal way. They "mean goods with which the assured was entrusted; not goods in trust in the technical sense."[33]

So much for insurance taken out by the vendor. But many lay-by purchasers will have a Householder's Comprehensive Insurance Policy. It might be questioned whether such a policy would cover lay-by goods, the property in which has already passed to the purchaser.

If a Householder's Comprehensive Policy has an "All Risks" extension this would cover some lay-by goods which are the property of the policy-holder. The proviso to this is that the goods would have to be of the type specified in the extension (e.g. household goods, home appliances). It is submitted, however, that the Comprehensive

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32. *Ebsworth* v. *Alliance Marine* (1873) L.R. 8 C.P. 596.
33. *Waters* v. *Monarch Fire and Life Assurance Co.* (1856) 5 El. & Bl. 870; 119 E.R. 705; per Lord Campbell, at 880, 709.

Policy, on its own, would not cover lay-by goods even if the property of the policy-holder.

The Householder's Comprehensive Policy normally covers goods belonging to the assured either (a) contained in the insured's residence, or (b) temporarily removed therefrom elsewhere within New Zealand. Obviously lay-by goods will not fall within the first category, as they are not in the insured's residence, and the question is whether they are "temporarily removed therefrom". Under its normal meaning the word "removed" refers to things that are changed in place, and would thus refer to goods which have been in the insured's residence and which, for some reason, have been taken away. Goods which have never been in his residence could hardly be said to be "removed" therefrom, and thus would not come within the purview of the clause.

In conclusion, there seems little reason why the lay-by vendor should not specifically insure lay-by goods which are in his possession. Indeed, this will be one of the recommendations of this paper.[34]

**4. Purchaser's Position in the case of Seller's Bankruptcy:**

Where the purchaser does not have property in the lay-by goods, the vendor's only interest in the goods is a lien to the extent of the money owing. But in the past, even a purchaser with property in the lay-by goods would not necessarily have been secure if the vendor went bankrupt. This was because of section 61(c) (the "order and disposition clause") of the Bankruptcy Act 1908. With the advent of the Insolvency Act 1967[35] this danger seems removed, and the lay-by purchaser with property in the goods would seem to rank as a secured creditor.

But it has been pointed out that lay-by purchasers will rarely have property in the goods.[36] Such purchasers have no security at all if the vendor goes bankrupt. They rank as unsecured creditors, and are likely to lose most, if not all, of the money paid for the goods. Such a situation is well illustrated by the failure of the Northern Linen Company in 1965.[37] That company had been formed in 1960 with a nominal capital of £2,000, and had borrowed £7,500 on the security of debentures charging all its assets. It employed travelling salesmen who visited houses, offices, and factories, obtaining book orders on the basis of samples. Agreements provided for a 20% deposit, and then for a number of periodic instalments. With such a small working capital the company was not in possession of the lay-by goods

34. See p. 29.
35. No. 54, 1967. As at 31st August 1970 this Act had not come into force, but it is expected to do so early in 1971.
36. See pp. 19–20.
37. Prior to this there had been two other failures of note. In 1960, a company called Dominion Supplies Ltd. failed with losses of $36,000, a good deal of which was owed lay-by customers. This was followed in 1962 by the failure of a mail-order company (not strictly lay-by) with losses of $34,000.

at the time of the agreement. These lay-by agreements were thus of the second type referred to above—agreements for the sale of unascertained goods.[38]

When it failed, Northern Linen left liabilities of over $90,000, and assets of just under $20,000. Lay-by customers, who numbered nearly three thousand, were owed approximately $52,000, trade creditors $20,000, a bank $2,000, and the debenture holders $15,000. It was estimated that the unsatisfied lay-by customers would receive between 10c and 15c in the dollar. This failure was followed by representations from various organisations who advocated the adoption of the New South Wales legislation in New Zealand.

The failure of the Northern Linen Company seems to have been due to lack of capital, lack of experience, and lack of adequate management. However, this is not always the case. Lay-by transactions, like mail order sales, provide perfect scope for sharp operators with less than honest intentions. The erstwhile vendor gets possession of the purchaser's money but has to give nothing in return until payments are completed. For the purchaser, this is often too late. Concern has recently been expressed about a particular operator who has progressively set up lay-by businesses, and then gone bankrupt, in one area of New Zealand. This operator would set up a business selling goods on lay-by, live in style on the purchase money, and then go bankrupt, and move on to another town, repeating the whole operation.[39] It is hard for the police to take action in such a case, because of the difficulty of proving fraud. Probably the most effective safeguards against such cases are found in the provisions of the New South Wales Act.[40]

## 5. Harsh Terms and Conditions in Lay-by Contracts:

As has been mentioned, terms and conditions are often especially harsh in the case of default by the purchaser (i.e. where he fails to complete instalments). Often this results in forfeiture of both the deposits and all the instalments paid by him, depending upon the actual terms of the contract. Probably such a forfeiture does not amount to a penalty, although "the essence of a penalty is a payment of money stipulated as *in terrorem* of the offending party; the essence of liquidated damages is a genuine convenanted, pre-estimate of damage".[41] Whether a sum is a penalty or liquidated damages is a question of construction to be decided upon the facts of each case, although the words of Tindal C.J. in *Kemble* v. *Farren*[42] might be of some use to the lay-by situation:—

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38. See p. 13.
39. "Consumer" 35, at page 132.
40. See pp. 25, 26 and 27.
41. *Dunlop Pneumatic Tyre Co., Ltd.* v. *New Garage and Motor Co., Ltd.* [1915] A.C. 79, 86, per Lord Dunedin.
42. (1829) 6 Bing. 141, 148; 130 E.R. 1234, 1237.

> "That a very large sum should become immediately payable, in consequence of the non-payment of a very small sum, and that the former should not be considered a penalty, appears to be a contradiction in terms".

If a sum is a penalty, then it will be subject to the equitable jurisdiction of the court. But whether it is a penalty or not must be judged as at the time of the agreement, and not at the time of the breach. At the time of making a lay-by agreement it is impossible to say what sum will be forfeited, for the amount forfeited will depend upon the time of breach.

In any case, it seems accepted that forfeiture of a deposit because of default does not amount to a penalty.[43] Thus, the lay-by purchaser could forfeit 50% of the actual purchase price, by reason of losing the deposit alone. Clearly this is another worthwhile area for lay-by reform.

### 6. Shortcomings in the Common Law regarding Lay-by Contracts:

These shortcomings are mainly in the areas of passing of property, risk in the goods, bankruptcy or other default by the vendor, and the harsh terms and conditions found in many lay-by contracts. They have now been discussed. In most cases the law seems uncertain, and in need of reform. But even where the law is certain it may still need reform. For example, it seems unfair that the unsuspecting lay-by purchaser should have no protection in the case of the vendor's bankruptcy or insolvency. For these reasons the next section of this paper will be devoted to legislative reform in the lay-by field.

## III REFORM

Both the N.S.W. Act, and the New Zealand Lay-by Sales Report have already been mentioned, albeit briefly. As any future reform is likely to be based on either the Act or the Report, both will now be dealt with in some detail.

### 1. The New South Wales Lay-By Sales Act 1943:

#### (a) An outline of the Act:

Although at first sight the Act appears a fairly complex piece of legislation, in actual fact its provisions are far from onerous. As will be apparent from the following discussion, most of the requirements of the Act are already followed by reputable traders in New Zealand, and its adoption here would simply mean that the not-so-reputable traders would have to fall into line. Since its inception in New South Wales in 1943 the Act has worked smoothly, and has not had any noticeably restricting effect on lay-by sales in that state.

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43. *Howe* v. *Smith* (1884) 27 Ch.D. 89.

The Act is essentially concerned with protecting the purchaser from the vendor's default and from the harsh terms and conditions of agreements. It does not deal with risk in goods or insurance. Contracting out of the Act is prohibited.[44]

(b) **Default by Vendor (through bankruptcy or dishonesty):**

The N.S.W. Act requires the vendor of lay-by goods to have the goods in his possession at the time the agreement is made, subject to certain qualifications (section 3(1)). The first qualification is that a purchaser may pay up to 20% of the purchase price before the goods have been received by the vendor (and inspected and approved by the purchaser), provided that the vendor pays this money into a trust account at a savings bank for the benefit of the purchaser (section 3(2)). The second qualification is that in the case of certain classes of goods approved by the State Governor the vendor may take out a fidelity bond in lieu of having these goods in his possession at the time of the agreement (section 3(5)). The third qualification applies to a contract where the purchaser makes a selection of the lay-by goods at a time subsequent to the date of the contract, whether or not at the time of the contract he indicates a choice or preference in relation to the goods or the type or class of goods to be selected by him.[45] In such a case, all the moneys received by the vendor pursuant to the contract are to be paid into a trust account for the benefit of the purchaser (section 17). None of these trust moneys are available for the payment of any of the vendor's other creditors, and thus cannot be attached or taken in execution by them (sections 3(3)(a) and 17(3)(a)).

The Act also lays down other requirements which are to the benefit of the purchaser. Every vendor must keep a register of lay-by transactions, in which he must enter certain particulars of the sale (section 4). He must also set the goods aside when they are appropriated to the contract, the goods in each sale to be identifiable by reference to the serial number of that sale (section 6). The purchaser and the police have the right to inspect the register and the goods to ensure compliance (section 5(2)).

The provisions of the N.S.W. Act thus give the lay-by purchaser considerable protection. The purchaser has the security of either the lay-by goods,[46] or of his money, and is thus completely protected should the vendor go bankrupt or insolvent.

The Act also gives protection against the dishonest vendor. It is, of course, always difficult to effectively legislate against such a person, because if he is prepared to defraud his customers, he will probably

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44. Section 18.
45. For example, the "Christmas Club" type of transaction. See p. 13.
46. Although the Act does not specifically say what interest the purchaser has in the lay-by goods, it is assumed that they are held in trust for him.

be prepared to ignore the provisions of any restricting act. However, the Act does impose considerable penalties where its provisions are not complied with. As well as this, the right of inspection by either the police or the purchaser gives the police an effective way of controlling the activities of dishonest or suspect vendors. As such, the provisions of the Act would seem to provide an effective deterrent to most potential offenders, and it is submitted that they would be a desirable part of any legislation regulating lay-by sales in New Zealand.

(c) **Harsh Terms and Conditions:**

The Act requires that at the time of the lay-by sale the vendor must deliver to the purchaser a written sales docket endorsed with the recorded number of the lay-by sale. This docket must itemise the goods, their description, and their price. As well as this, a notice in the prescribed form containing a summary of the provisions of the Act must be handed to the purchaser. Parol agreements varying the terms set down in the Act are void as against the purchaser (section 5).

It has been pointed out that the harshest terms in lay-by agreements are often those governing the forfeiture of the purchaser's payments where he fails to complete the contract. Under the N.S.W. Act the vendor is not entitled to any sum in excess of the cost to him of the determined sale, whichever party determines the sale. If the total consideration provided by the purchaser, and the value of the lay-by goods at the time the sale is determined, are in excess of the purchase price of the goods plus an amount sufficient to recoup the vendor for selling costs in respect of the lay-by sale, then such excess can be recovered by the purchaser (section 10(1) (a) ). On the other hand, where the amount paid by the purchaser is not sufficient to cover the vendor's losses, the vendor can recover the difference from the purchaser. He is not, however, entitled to any additional sum, whether as a penalty or compensation or otherwise in consequence of the determination of the lay-by sale (section 10(1) (b) ). For the purposes of the Act, the value of the goods when the lay-by sale is determined is deemed to be the same as their value when the sale was made, unless the contrary is proven (sections 10(2) and 10(3) ).

## 2. The New Zealand Lay-by Sales Report:

In looking at lay-by sales in New Zealand and the need for reform, the Contracts and Commercial Law Reform Committee gave particular consideration to the provisions of the N.S.W. Act. In several important points, however, the Committee's recommendations depart from the Act.

The New Zealand Lay-by Sales Report deals with the three areas of default by vendor through bankruptcy, harsh terms and conditions of lay-by agreements, and risk and insurance in lay-by goods.

(a) **Default by the Vendor:**

The Committee considered the provisions of the N.S.W. Act "far too onerous and detailed for New Zealand requirements".[47] It is respectfully submitted that this conclusion is unwarranted. Information made available to the writer from both the Retail Traders' Association of New South Wales, and the New South Wales Consumer Affairs Council indicates that lay-by sales have continued to account for roughly the same proportion of retail turnover since the N.S.W. Act came into operation. It would thus seem that traders in New South Wales have not found the requirements of the Act unduly onerous, and there is no reason why this should be so in New Zealand. This is further substantiated by the fact that many reputable traders in New Zealand already operate their lay-by systems in a similar manner to that required by the N.S.W. Act

However confusion may have arisen from an apparently wrong interpretation which the Contracts and Commercial Law Reform Committee gave to the N.S.W. Act. From their summary of the Act one could be excused for thinking that the lay-by vendor must have the lay-by goods in his possession and appropriated to the contract (section 3), *and as well as this,* that he must put all the money received from the purchaser into a trust account (section 17). Were this so, then the provisions of the N.S.W. Act would indeed be onerous. Because of the requirement that the goods be set aside, the vendor would lose use of the working capital tied up in the goods, and he would lose the chance of selling those goods to another purchaser. Because of the requirement that all the purchaser's money be paid into a trust account until the completion of the sale, the vendor would lose the use of the purchaser's money to compensate him for the loss of his own working capital. However it is clear from the N.S.W. Act that the vendor must do one or the other, not both. Section 17 is only an alternative to section 3. The two are *not* complementary.

Instead of accepting the provisions of the N.S.W. Act in this area, the New Zealand Report recommends basically that the lay-by purchaser be given priority when the vendor goes bankrupt. The drawback here, of course, is that there is little value in having priority in bankruptcy, if there is still not enough money to go around the creditors with that priority.[48] There is similarly little value in having priority if the vendor has absconded with the money and cannot be found.

The New Zealand Report argues that the requirements of the N.S.W. Act offer no real security against the dishonest trader, who will simply ignore them. But the N.S.W. Act does provide a means of policing traders, and this should prove particularly valuable in the

47. Page 8 para. 11.
48. For example, this would have been the case in the Northern Linen failure.

case of the dishonest trader. Such a trader will not be able to defraud people for long if he has the police pounding at the door demanding to see the goods he professes to sell. The Report further considers that the lay-by customers' priority in bankruptcy will make it difficult for the less stable trader to obtain business financing, as not many lending institutions would support him, with their security removed. But it would appear that the less scrupulous traders are not interested in loan financing anyway, preferring to finance themselves with the purchaser's payments.

It is therefore submitted that the provisions of the N.S.W. Act offer the purchaser a far better security in this area than do the recommendations of the New Zealand Report. But the ultimate in security could be achieved by a partial combination of the two. The N.S.W. Act gives the purchaser security as long as the vendor adheres to its requirements. The substantial penal provisions encourage him to do so. But should a bankrupt vendor not have complied with the provisions of the Act, it would seem reasonable to give the purchaser priority in bankruptcy. This appears to tie up any loose ends.

(b) **Harsh Terms and Conditions:**

In this area, the recommendations of the New Zealand Report are basically akin to the provisions of the N.S.W. Act. Where the contract is determined both the Report and the Act disapprove of the vendor retaining the purchaser's payments in excess of the amount required to compensate the vendor for his losses. There are slight differences however.

In the first place, the Report considers that the *prima facie* evaluation of the lay-by goods on determination as being the contract price at the time of agreement may be unduly harsh on the vendor. The Report recommends that such an evaluation should apply only if the sale is determined within one month.

In the second place the Report recommends that the vendor be entitled to 20% of the cash price of the goods as a conventional figure to recoup him for his "selling costs". Considering that the vendor is being compensated for any loss in the value of the goods, it might be wondered whether this provision is not too burdensome on the purchaser. The vendor has, after all, had the interest-free use of the purchaser's money and this might be considered sufficient to compensate him for his selling costs.

The 20% allowance to cover selling costs might lead to some unusual results. Supposing that a purchaser wishes to buy an article worth $200 on lay-by. As is commonly required he pays a 10% deposit—$20. He later cancels the contract without making any further payments, perhaps within a period of a few days. Under the Report's recommendations he will forfeit 20% of the *total* cash price of the article to recoup the vendor for his selling costs—$40. As well as losing his deposit the purchaser thus faces a bill for an extra $20

from the vendor, who may not even have set the article aside.[49] The Report's recommendation in this respect could thus turn out less favourable than the existing practice of many retailers. It would further seem in direct conflict with the basic principle that the vendor should not retain payments made by the purchaser in excess of the vendor's losses.

The third difference is, it is submitted, an illusory one. The New Zealand Report considers that section 8 of the N.S.W. Act gives the vendor a special right to determine a lay-by sale. It is recommended that no similar right be given a vendor in New Zealand. But section 8 only sets down the procedure to be followed where the vendor in writing determines a lay-by sale. Section 9 then sets down the procedure to be followed where the purchaser in writing determines a lay-by sale. Section 8 thus covers the situation where the purchaser defaults under the lay-by contract, but does not determine in writing. In such a case if the vendor wishes to determine the contract because of the default, he must do so in writing under section 8. Section 8 does not therefore give the vendor a special right to determine the lay-by sale. It gives the purchaser added protection where the vendor determines under his common law rights, and does not detract from the value of the N.S.W. Act.

The New Zealand Report does not make a recommendation similar to section 5 of the N.S.W. Act. Section 5 requires that certain written documents, including those informing the purchaser of his statutory rights, be given to the purchaser at the time of the lay-by agreement.[50]

(c) **Risk and Insurance:**

The New Zealand Report recommends that the vendor should carry the risk in the lay-by goods as long as the goods are in his possession, notwithstanding that property has passed to the buyer. Considering the discussion above,[51] this would indeed seem a reasonable and convenient solution.

## IV CONCLUSION

Lay-by selling is a well accepted form of credit transaction. However it should now be clear that it is potentially hazardous for the unsuspecting and unlucky purchaser. In most instances the amounts involved will be too small to litigate over, which probably explains the absence of case law in this field. But the person who buys on lay-by is often the person who can least afford such a small loss. For example,

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49. Presumably the vendor's "selling costs" are the clerical costs involved in processing a lay-by account. Where the vendor has not even set the lay-by goods aside, these would seem to be negligible.
50. See p. 26.
51. See pp. 20–22.

in the Northern Linen failure, most of the customers were young girls who were saving for their trousseaux.

The Northern Linen failure was followed by vociferous demands for legislative reform. We certainly have the material for legislation. We have the New South Wales Act, which appears to have worked long and well under conditions very similar to our own. We have our recent New Zealand report, with its suggested amendments to the Australian act. It is to be hoped that lay-by reform in this country will follow soon.

D. J. MacKay