

THE QUEBEC REGIME ON “MONETARY CLAIMS” AND THE UCC TREATMENT OF DEPOSIT ACCOUNTS

Posted on December 23, 2021

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On January 1, 2016, the province of Québec adopted a new type of movable hypothec with delivery (commonly called a “**pledge**”) on monetary claims, in order to respond more effectively to the needs of the Canadian market in terms of taking security on amounts of money. Québec thereby became a “precursor” in Canada in this regard, as the other common law jurisdictions in the country do not have a security mechanism of this type.

The Québec regime and the American regime: similar yet different

The rules applicable to a pledge on monetary claims (articles 2713.1 and following of the *Civil Code of Québec* (the “**CCQ**”) were largely inspired by those set out in Section 9 of the *Uniform Commercial Code* in the United States (the “**UCC**”). Consequently, the two legal regimes share the following similarities:

- the concept of “control” of a monetary claim and the enforceability against third parties, and
- the rules on conflicting priorities of rank among various secured creditors.

However, the two regimes differ in the following regards:

- the concept of a monetary claim is “broader” in Québec law, and
- the priority of rank of a pledge over any other movable hypothec, which is specific to Québec law.

The “broad concept” of monetary claims in Québec law

In Québec, a movable hypothec with delivery on a monetary claim may secure “any claim requiring the debtor to reimburse, return or restore an amount of money or make any other payment in respect of an amount of money”^[1]. This covers not only money in a deposit account with a financial institution, but any amount of money transferred to a third party (not necessarily a financial institution) pursuant to a contractual relationship wherein the principal obligation is secured by that amount of money. By way of example, this could be (i) an amount of money deposited by A (the tenant) with third-party C to guarantee payment of rent under a lease between A and B (the landlord), or (ii) an amount of money deposited in the bank account of the corporation D at financial institution E with which D has entered into a loan agreement whereunder the principal obligation

is secured by that amount of money.

In the United States, the concept of a monetary claim is much more limited, as Section 9 of the UCC applies only to “*deposit accounts*”, which is defined as “*a demand, time, savings, passbook, or similar account maintained with a bank*”^[2].

The Québec regime thus offers more flexibility than its American counterpart, allowing lenders to be more creative when taking security on monetary claims. It also has specific rules on the law applicable to the validity and publicity of monetary claims on the credit balance of a financial account or an amount of money remitted to secure the performance of an obligation towards the creditor. The operative principle here is the parties’ freedom to choose the applicable law in the legal contract governing the claim^[3], in the knowledge that absent a choice of law, the CCQ imposes the applicable law by default^[4]. The creditor will thus always have a compelling interest to choose Québec law as the applicable law in order to benefit from the advantages outlined above.

The concept of “control” of a monetary claim: a similarity of the two legal regimes.

A pledge can only exist (i) if there is a monetary claim due by the debtor of the principal obligation towards the creditor, and (ii) the creditor obtains delivery thereof by gaining control over the claim^[5]. Such control allows the security to be enforceable against third parties.

Control can be acquired in two ways^[6] depending on whether or not the monetary claim is held by the creditor:

(1) either the monetary claim of the grantor of the pledge is maintained with the creditor. In other words, the creditor is now the “debtor” of the monetary claim towards the grantor of the pledge and acquires control thereof by obtaining the grantor’s consent that the monetary claim will guarantee the grantor’s obligations towards the creditor^[7]. It should be noted that for evidentiary purposes, it is strongly advised to obtain the grantor’s consent in writing, even though the CCQ does not expressly require this.

An example of this situation would be a loan agreement between bank A (the creditor) and borrower B (the grantor of the pledge). Under this agreement the borrower must fulfill a principal obligation towards bank A, namely repayment of the loan, which obligation is secured by the amount of money in borrower B’s deposit account with bank A. In this situation, bank A acquires control of the monetary claim by obtaining the grantor’s consent that the monetary claim will guarantee the performance of its obligation towards bank A.

In practice, the grantor’s consent can take various forms but is most often found in a setoff clause in the loan agreement. It should also be noted that the enforceability the pledge against third parties

automatically arises when the creditor gains control of the claim^[8], without having to publish the right in the Register of Personal and Movable Real Rights (the “**RPMRR**”). The lack of a publication requirement for a pledge represents a considerable advantage for the creditor, as it does not have to register the security in order to set it up against third parties, which is not the case with all movable hypothecs without delivery.

(2) or the monetary claim of the grantor of the pledge is not held by the creditor, but by a third party. The latter is thus now the “debtor” of a monetary obligation towards the grantor of the pledge. In this instance, the creditor acquires control of the monetary claim by either (i) concluding a control agreement with the third party, provided that (a) the monetary claim is on a credit balance in a financial account maintained with the third party, or (b) the claim is on an amount of money paid by the grantor to guarantee the performance of an obligation towards the creditor^[9], or (ii) becoming the holder of the bank account of the grantor of the pledge^[10].

Returning to our example in paragraph (1) above of a loan agreement between bank A (the creditor) and borrower B (the grantor of the pledge), suppose that B holds the amount of money covered by the monetary claims in its bank account maintained with third-party C, and that one of the conditions of the loan is that this amount guarantees repayment of the loan, such that A must now conclude a control agreement with C in order to gain control over the monies in the account. It should be noted however that under the CCQ third-party C is not required to conclude such a control agreement with A^[11] and that the financial account must have a credit balance when the security is granted^[12]. Consequently, a control agreement cannot be entered into in respect of future monetary claims.

The UCC regime is also based, like the Québec regime, on the concept of control, such that the secured creditor acquires control of a monetary claim either (i) automatically, if the monetary claim pertains to a deposit account with the secured creditor where the latter is a bank^[13], or (ii) through a control agreement with a third party if the monies covered by the monetary claims are in a deposit account held by the debtor with the third party^[14], or (iii) where the secured creditor becomes the holder of the debtor’s deposit account with the third party^[15]. Similar to the rules under the CCQ, the right to enforce the monetary claims against third parties results from the secured creditor’s control over the claim: “*a security interest in a deposit account may be perfected only by control*”^[16].

The priority of rank conferred by a pledge over any other movable hypothec – a unique feature of the Québec regime

The UCC regime gives priority of rank to the creditor once the latter acquires control of the deposit account. This security interest thus outranks any other “conflicting security interest” of a secured creditor who does not

have control of the deposit account^[17]. The Québec regime also gives priority ranking to the creditor, but in a slightly different way, since the pledge “*ranks ahead of any other movable hypothec encumbering that claim, from the time that control is obtained, regardless of when that other hypothec is published*”^[18]. Thus, according to this provision, a movable hypothec without delivery covering monetary claims will rank after a pledge of those same monetary claims, regardless of the date on which the movable hypothec without delivery was registered.

By way of example, if A granted a movable hypothec without delivery on the universality of its property to B, the hypothec would thus cover the monetary claims of A. B will then publish its hypothec so it can be enforced against third parties, and this right to so enforce the hypothec will arise on the date it is published. Now suppose that after several months, A decides to obtain a loan from financial institution C, who requires A to open a bank account with it in which an amount to guarantee the loan is deposited. C of course also requires A to grant it security, namely a pledge of that deposited amount. Now, since that amount is held with C and A has consented that the amount guarantees the performance of A’s obligations towards C, by virtue of paragraph 1 of article 2713.8 of the CCQ the movable hypothec without delivery previously published by B will rank after the pledge. This example illustrates the considerable advantage of a pledge over other types of security available to creditors, as a pledge will always outrank every other type of security on a monetary claim.

Rules governing conflicting priorities of secured creditors: a shared similarity of the two legal regimes

It is often the case that a deposit account will be controlled by different creditors. In such situations the rules regarding conflicting priorities will come into play. In this regard, the Québec regime establishes a hierarchy whereby the security interest granted to a creditor who becomes the holder of a deposit account with a credit balance will outrank a pledge granted to a creditor on the monetary claims of the grantor of the pledge held against the latter creditor^[19]. In the same way, a pledge obtained by a creditor on the monetary claims of the grantor of the pledge held against that creditor “*ranks ahead of all other hypothecs with delivery effected by control encumbering that claim*”^[20]. Finally, in the case of a monetary claim held by several creditors through control agreements concluded with the same third party, rank is determined according to when the third party agreed to comply with the instructions of each creditor^[21].

The UCC regime has analogous provisions for conflicting priorities of secured creditors^[22], such that the two regimes are similar in this regard.

Conclusion

The Québec regime governing movable hypothecs with delivery on certain monetary claims has considerable advantages for creditors. For the “broad concept” of a monetary claim gives rise to a wide range of applications of this type of security, as it covers both money in a deposit account and any amount of money transferred to a

third party. In addition, this type of security has few formal requirements and does not need to be published in the RPMRR in order to be enforced against third parties. It should be noted however that in practice it is preferable to publish a pledge in the RPMRR in order to avoid potential litigation on priority of ranking. Finally, the priority of rank of a pledge, as recounted above, affords peace of mind to the creditor regarding the order of collocation, as it will have a first ranking hypothec on the pledged monetary claim ahead of any other creditor.

[1][ps2id id='1' target=''] Article 2713.1 CCQ. It should be noted that the following are excluded from the definition: a claim represented by a negotiable instrument, a claim that is a security or a security entitlement within the meaning of the *Act respecting the transfer of securities and the establishment of security entitlements*, and a claim resulting from the delivery of certain and determinate currency whose repayment, in accordance with parties' manifest intention, must be made by restitution of the same currency.

[2][ps2id id='2' target=''] Section 9-102 (29) UCC

[3][ps2id id='3' target=''] Article 3106.1 CCQ

[4][ps2id id='4' target=''] Article 3106.1, paras. 1 and 2 CCQ

[5][ps2id id='5' target=''] Article 2713.1 CCQ

[6][ps2id id='6' target=''] Articles 2713.2, 2713.3 and 2713.4 CCQ

[7][ps2id id='7' target=''] Article 2713.3 CCQ

[8][ps2id id='8' target=''] Article 2713.8, para. 1 CCQ

[9][ps2id id='9' target=''] Article 2713.4, para. 1 1^o) and 2^o) CCQ

[10][ps2id id='10' target=''] Article 2713.4, para. 2 CCQ

[11][ps2id id='11' target=''] Article 2713.5 CCQ

[12][ps2id id='12' target=''] Article 2713.4 CCQ

[13][ps2id id='13' target=''] Section 9-104 (a) (1) UCC

[14][ps2id id='14' target=''] Section 9-104 (a) (2) UCC

[15][ps2id id='15' target=''] Section 9-104 (a) (3) UCC

[16][ps2id id='16' target=''] Section 9-312 (b) (1) and 9-314 UCC

[17][ps2id id='17' target=''] Section 9-327 (1) UCC

[18][ps2id id='18' target=''] Article 2713.8, para. 1 CCQ

[19][ps2id id='19' target=''] Article 2713.8, para. 3 CCQ

[20][ps2id id='20' target=''] Article 2713.8, para. 3 CCQ

[21][ps2id id='21' target=''] Article 2713.8, para. 2 CCQ

[22][ps2id id='22' target=''] Section 9-327 UCC

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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