The Law Commission

Working Paper No. 109

Transfer of Land
Passing of Risk from Vendor to Purchaser

HER MAJESTY'S STATIONERY OFFICE

The Law Commission was set up by section 1 of the Law Commissions Act 1965 for the purpose of promoting the reform of the law.

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This working paper, completed on 11 July 1988, is circulated for comment and criticism only. It does not represent the final views of the Law Commission. The Law Commission would be grateful for comments on this working paper before 30 December 1988. All correspondence should be addressed to:

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CONTENTS

SUMMARY

In this working paper, the Law Commission examine as part of our programme for the simplification of conveyancing, the rule that the risk of damage to or destruction of the property prior to the completion of the contract of sale passes to the purchaser from the date of the contract. This gives rise to duplication of insurance in that both purchaser and vendor maintain insurance between contract and conveyance. We provisionally recommend that the vendor should be obliged to convey the property in the same condition as it was in at the date of the contract, subject to any contractual provision to the contrary. We would prefer this to be achieved by a change of law, but in the meantime a condition of sale to the same effect could be adopted in practice.

The Law Commission are extremely grateful to Mr. Mark Thompson LL.B., LL.M., Lecturer in Law at Leicester University, for his considerable work, by way of research and writing, in the preparation of this working paper.

All the proposals in this paper are merely provisional and its purpose is to obtain views on them, not only from practitioners and other legal experts, but also from the public.

THE LAW COMMISSION

ITEM IX OF THE FIRST PROGRAMME
TRANSFER OF LAND
PASSING OF RISK FROM VENDOR TO PURCHASER

PART I

PROBLEMS IN THE PRESENT LAW

Introduction

1.1 In item IX of the First Programme, the Law Commission undertook to examine those areas of property law where reform would lead to the simplification of conveyancing. As part of that programme, we are now examining the law that governs the passing of the risk in conveyancing contracts. At present, the prevailing rule appears to be that, after exchange of contracts, the risk of damage to the property passes to the purchaser. This stems from the principle that, from that date, the purchaser is regarded in equity as the owner of the property.

1.2 The existence of this equitable principle appears to cause a great deal of complexity, in that the concept of the trust is not the most suitable means by which the rights and obligations of parties to a contract are regulated. Accordingly, the law is more difficult to state than it need be. These problems, which we identify in Part I of this paper, themselves indicate the need for some clarification in the law. More fundamentally, however, we consider in this paper whether it is appropriate that the general law should throw the risk of damage to the property onto the purchaser prior to completion.

1.3 The rule of law that the risk passes to the purchaser was perhaps most clearly stated by Sir George Jessel M.R. In Lysaght v. Edwards[1] he said:

> If anything happens to the estate between the time of sale and the time of completion of the purchase it is at the risk of the purchaser. If it is a house that is sold, and the house is burnt down, the purchaser loses the house. He must insure it himself if he wants to provide against such an accident. If it is a garden, and a river overflows its banks without any fault of the vendor, the garden will be ruined, but the loss will be the purchaser's. In the same way there is a correlative liability on the part of the vendor in possession. He is not entitled to treat the estate as his own. If he wilfully damages or injures it, he is liable to the purchaser; and more than that, he is liable if he does not take reasonable care of it.

1.4 In this dictum, Sir George Jessel clearly points out two of the perceived consequences of a contract for the sale of land. First, the risk of destruction of or damage to the property rests with the purchaser who, to safeguard his own position, must insure and, secondly, the vendor is under an obligation to take reasonable care of the property. Of these propositions, it is the first which, to a layman at least, might appear somewhat surprising. One might expect that the law would require the vendor to convey that which he has contracted to sell, which is not just a particular property but a property in a particular condition. A purchaser taking this view might well, unless advised to the contrary, enter into the contract without effecting insurance, thereby exposing himself to the risk of catastrophic financial loss, should the property be

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1. (1876) 2 Ch. D. 499, 507. The opposite view expressed in Stent v. Bailis (1724) 2 P. Wms. 217, 220 per Sir Joseph Jekyll M.R. has attracted no judicial support.

destroyed prior to completion.[2] If, however, he follows the safe practice of insuring the property from the date of the contract, then, as will be seen, this does not mean that there is no longer any need for the vendor to maintain his own policy. The result is that both parties to the contract insure the same property against the same risk.

1.5 In our view, this position is obviously unsatisfactory. The rule in Lysaght v. Edwards results either in the purchaser being put at risk of a financial disaster or in unnecessary expense being incurred. Of the two, the former seems to us to be the more serious, and our principal concern is to ensure that a purchaser is not exposed to this risk, at least without full warning in advance. In addition to this, we feel that the law is uncertain in its operation in various respects, and there also exist arguments that the accuracy of the law as stated by Sir George Jessel is itself open to criticism.[3]

1.6 We are therefore putting forward for consultation proposals for reform. In Part I of this paper we examine the impact of the trust which arises on the creation of a specifically enforceable contract of sale on the rights and obligations of vendor and purchaser. The main consequence in practice is the passing of risk which can, usually, be guarded against by insurance. For the uninsured purchaser to be adequately safeguarded, it must be possible for him in all cases to rely on the vendor's policy (assuming there to be one). In Part II of this paper we examine the law

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2. New South Wales Law Reform Commission, Passing of Risk Between Vendor and Purchaser of Land, p. 18.

3. See M.P. Thompson, "Must a Purchaser Buy a Charred Ruin?" [1984] Conv. 43.

relating to insurance to see if the law can be changed to this end. Finally, in Part III of this paper we consider a number of more fundamental options for reform of conveyancing law, indicating our own preferences. We would emphasise, however, that we have not formed any final views, and we hope that there will be a wide-ranging discussion of our proposals.

Effect of contracts for sale

1.7 From the middle of the seventeenth century the effect of a contract for the sale of land has been said to be to pass the equitable title to the purchaser.[4] The reason for this is that, unlike most contracts of sale, specific performance is routinely awarded of a contract for the sale of land. This is on the basis that damages are never considered to be adequate compensation to a purchaser for non-performance of such a contract.[5] The application of the maxim, equity looks on that as done which ought to be done, then leads to the conclusion that the property belongs in equity to the purchaser.[6]

1.8 This maxim operates widely in land law. For example, specifically enforceable contracts to create leases or easements have the effect of creating equitable tenancies

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4. Lady Foliamb's Case (1651) cited in Daire v. Beversham (1661) Nels. 76.

5. See G. Jones and W. Goodhart, Specific Performance, (1986), pp.18-22.

6. See Atcherley v. Vernon (1723) 10 Mod. 518, 527 per Lord Macclesfield L.C.; Re Cary-Elwes' Contract [1906] 2 Ch. 143, 149 per Swinfen Eady J.

or equitable easements.[7] In these cases, however, there is a significant difference in the effect of the maxim. In the case of both leases and easements, the equitable interest is different in nature from the interest possessed by the holder of the legal estate. In the case of a contract of sale, however, the effect of the maxim is to pass the equitable fee simple. In that event, because there is a separation of the legal and equitable estates, a trust is said to arise. This trust relationship carries with it various incidents not present in other areas, where equitable interests can be created without involving the law of trusts in any way.

1.9 The trust that is created by the existence of a contract of sale is, however, a most unusual one, because there is normally a gap between the entry into an enforceable contract of sale and the payment of the purchase price. In that interim period, therefore, the vendor clearly retains a personal interest in the property:[8] this is an unusual position for a trustee, in situations where co-ownership is not involved.

1.10 The unusual nature of the vendor's trusteeship was recognised by the House of Lords in Shaw v. Foster.[9] Lord Cairns put the matter this way in a case where the contract had been completed:

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7. Walsh v. Lonsdale (1882) 21 Ch. D. 9; McManus v. Cooke (1887) 35 Ch. D. 681.

8. Re Birmingham [1959] Ch. 523.

9. (1872) L.R. 5 H.L. 321.

> The vendor was a trustee of the property for the purchaser; the purchaser was the real beneficial owner in the eye of a Court of Equity of the property, subject only to this observation, that the vendor, whom I have called the trustee, was not a mere dormant trustee, he was a trustee having a personal and substantial interest in the property, a right to protect that interest, and an active right to assert that interest if anything should be done in derogation of it. The relationship, therefore, of trustee and cestui que trust subsisted, but subsisted subject to the paramount right of the vendor and trustee to protect his own interest as vendor of the property.[10]

1.11 The fact that the vendor has a valuable interest of his own in the property has led to some difficulty both in describing the respective rights and duties that arise and also in ascertaining from what time it is correct, and indeed helpful, to describe the vendor as a trustee.[11] These difficulties are related to a second issue. The vendor's own interest in the property stems not simply from his right to receive the purchase money. The contract may not for a number of reasons, ultimately be performed. In this event, he will resume the position he was in, prior to entry into the contract, of being full legal and beneficial owner.

1.12 These considerations have led to judicial disagreement as to when the trust may properly be said to arise. The principal conflict has been over whether it is

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10. Ibid., at p. 338.

11. For the fullest treatment of these issues, see D.W.M. Waters, The Constructive Trust, (1964) pp. 74-141. See also Walter G. Hart, "The Inconsistencies of the Doctrine of Equitable Conversion", (1908) 24 L.Q.R. 403; Simon Gardner "Equity, Estate Contracts and the Judicature Acts: Walsh v. Lonsdale Revisited", (1987) 7 O.J.L.S. 60.

correct to say that the trust arises immediately a contract for sale is entered into, or whether it arises at some later date: a dispute of some importance, if such crucial consequences as the passing of the risk depend upon it. The nature of these disagreements will be examined below. First, however, it is convenient to consider the consequences that are said to flow from the passing of ownership in equity.

Vendor as trustee

1.13 The inherent contradiction in the vendor's position pending completion is reflected in the duties imposed upon him as a result of his status as trustee. Normally, it is a firm rule of equity that a trustee cannot profit from his trust.[12] Save where the vendor has been paid the full purchase price, when he can be seen to be a bare trustee,[13] this general rule of equity is by no means generally applied in this context.

1.14 It is true that if the property rises in value between contract and conveyance, the purchaser is entitled to that gain without any adjustment in the purchase price.[14] For example, if the purchase is of a reversionary estate and a life drops in the interim, then the purchaser has the benefit of the increased value of what he has contracted to

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12. Boardman v. Phipps [1967] 2 A.C. 46.

13. Bridges v. Mees [1957] Ch. 475, 485 per Harman J. See para. 1.47 below.

14. But cp. English v. Dedham Vale Properties Ltd. [1978] 1 W.L.R. 93 where the purchaser had, prior to the contract, passed himself off as the vendor's agent for the purpose of an application for planning permission.

buy.[15] Perhaps more likely in modern times would be local authority action causing the land to become more valuable; again the purchaser would derive the benefit.[16] Conversely, however, if the value of the land drops in that period, he suffers the loss.[17]

1.15 These propositions owe little to the passing of title in equity. The same results could quite easily be explained on the basis that the purchaser has made what turns out to be a good or bad bargain. Certainly in the case of executory contracts generally, a change in conditions which favours one party does not entail any right to re-negotiate terms.[18] Where one might expect the trust to play a role, however, it does not.

1.16 Ordinarily, a trustee is not entitled to benefit from his trust. Yet to reflect the fact that, until he has been paid in full, the vendor has a valuable interest of his own, the vendor is, prior to completion, entitled to certain benefits derived from the land. Good illustrations of this are supplied by the fact that it is the vendor and not the purchaser who can insist upon possession of the land prior to completion[19] and who is entitled to the rents and

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15. Harford v. Purrier (1816) 1 Madd. 532, 539. For the opposite situation, see White v. Nutts (1702) 1 P. Wms. 61.

16. Paine v. Meller (1801) 6 Ves. 349, 352. See Dart's Vendors and Purchasers 8th ed., (1929), pp. 268-269.

17. Poole v. Shergold (1786) 1 Cox 273.

18. See Farnsworth, Contracts, p. 5.

19. Phillips v. Silvester (1872) 8 Ch. App. 173.

profits emanating from it.[20]

1.17 What might be termed collateral benefits which are payable to the vendor are not paid to the purchaser. In Re Lyne-Stephens and Scott-Miller's Contract[21] it was held that damages recovered by the vendor from his tenant for breach of a covenant to repair were not recoverable by the purchaser. Similarly, there was no liability to account in Re Hamilton-Snowball's Conveyance.[22] Mr. Hamilton-Snowball contracted to purchase certain premises occupied by him that were at that time requisitioned. He entered into a contract to sell the premises on the same day that he contracted to buy them. After they were conveyed to him, the premises were de-requisitioned. It was held that he was entitled to keep the money which became payable on de-requisitioning and did not have to pay the money to the purchaser.

1.18 In both these cases, the fact that the vendor was regarded as a trustee had no impact on the result. The benefits he received were regarded as collateral to the contract of sale and purchase and he was therefore entitled to retain the money. In the same vein, but considerably more significant, is the position with regard to insurance money.

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20. Cuddon v. Tite (1858) 1 Giff. 395.

21. [1920] 1 Ch. 472; Re Edie and Brown's Contract (1888) 58 L.T. 307.

22. [1959] Ch. 308.

1.19 In Rayner v. Preston[23] contracts for the sale of a house had been exchanged when the house, which was insured by the vendor, was damaged by fire before completion. The vendor's insurance company paid out on the policy and the purchaser completed at the contract price. In an action brought by the purchaser to recover the insurance money from the vendor, it was argued that because he was a trustee, he should be liable to account for this money. This argument was adopted by James L.J., who dissented, but was rejected by the other members of the Court of Appeal. Brett L.J. considered that it was inaccurate to describe the vendor as a trustee at all and therefore the purchaser could not claim on a contract of insurance to which he was not privy. Cotton L.J., on the other hand, accepted that the vendor was a trustee of the land he had contracted to sell, but not of the insurance policy.

1.20 The disagreement between the three members of the Court of Appeal highlights the inherent uncertainty of the legal position pending completion. Brett L.J.'s view is very much a solitary one. The approach of James L.J. is consistent with the normal obligations imposed upon a trustee or fiduciary but, as the trust has always been regarded as unusual in this context, Cotton L.J.'s judgment is more in line with the general lack of liability on the part of a vendor to account. The case provides a good illustration that the trust concept provides little assistance in resolving disputes between vendor and purchaser. Moreover in subsequent proceedings brought by insurers against the vendor, the vendor's insurers were held to be entitled to recover a sum equivalent to the amount paid out under the policy by way of subrogation and because in the circumstances as they had actually occurred the

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23. (1881) 18 Ch. D. 1.

vendor could not keep both the insurance money and the full purchase price.[24]

1.21 In contrast, a novel but logical liability was imposed upon the vendor in Lake v. Bayliss.[25] In this case, the vendor had, in breach of contract, conveyed land to a third party. The purchaser under the first contract was held to be entitled to recover the purchase money paid to the vendor by the remedy of tracing. In reaching this conclusion, Walton J. expressed the view that, as the vendor was a trustee, he may, under certain circumstances, be obliged to pass on to the purchaser any higher offers to buy the property received after the contract of sale was formed, in order to allow the purchaser to consider re-selling at that higher price. While this seems a logical application of trust principles, it may come as something of a surprise to vendors.

Vendor's duty of care

1.22 Another aspect of reliance on the trust concept is the imposition of duties on the vendor in regard to his obligation to look after the property. The duty of care imposed upon the vendor was clearly stated and explained in Wilson v. Clapham.[26] Sir Thomas Plumer M.R. said:

> The care of the estate must of necessity be left to the vendor; he becomes a trustee for the purchaser, and what hardship is there in expecting

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24. Castellain v. Preston (1883) 11 Q.B.D. 380. The whole question of insurance is considered in Part II.

25. [1974] 1 W.L.R. 1073. This decision is more fully considered below: see paras. 1.59-1.60.

26. (1819) 1 Jac. & W. 36, 38.

> him to take the same care of it as he would if it were his own? He must take the measures that are adopted by every prudent landlord.

The ambit of the vendor's duty must be examined, since it obviously qualifies the proposition that the risk of damage or destruction passes to the purchaser.

1.23 Because the vendor is regarded as a trustee, he is clearly liable to the purchaser for physical damage to the property that he inflicts himself. Examples of this are when a substantial amount of rubbish is abandoned on the property,[27] or where fixtures are removed.[28] Such instances can be seen as providing clear illustrations of breaches of duty;[29] what is rather more problematic is the position when the vendor's action causes financial loss unconnected with physical damage. This will usually only occur when a lease is being sold. In such a sale, the vendor must ensure that he does not breach covenants prior to completion.[30] For example, if there is a covenant to insure the property, he must not let the policy lapse before assigning the lease.[31] If it is the freehold that is

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27. Cumberland Consolidated Holdings Ltd. v. Ireland [1946] K.B. 264. Cf. Hynes v. Vaughan (1985) 50 P. & C. R. 444.

28. Phillips v. Lamdin [1949] 2 K.B. 33. See also Ware v. Verderber (1978) 247 E.G. 1081.

29. They could equally be seen as examples of the vendor being in breach of a contractual obligation to convey what was agreed, as to which see para. 1.52 below.

30. If he does so, in addition to being in breach of the duty under discussion here, he may also be in breach of the covenants for title implied by the Law of Property Act 1925, s.76(1)(B).

31. Dowson v. Solomon (1859) 1 Drew. & Sm. 1. Where a freehold property is being sold, it is unlikely that the vendor will have any obligation to insure, see below para. 2.36.

being sold subject to a tenancy, then the vendor will be liable in damages to the purchaser if he permits the tenant to use the property in a way different from that permitted by the lease.[32]

1.24 A different problem with regard to leases arises when, on a sale subject to a lease, the lease expires prior to completion.[33] In Egmont v. Smith,[34] the vendor relet land on an agricultural tenancy prior to conveying it to the purchaser and was held to be entitled to do so. In Abdulla v. Shah,[35] on the other hand, the vendor of rent-restricted property relet the property, without consulting the purchaser. He was held liable to the purchaser for the difference in value between the land with and without the protected tenant.

1.25 Underlying Abdulla v. Shah there is the need for the vendor to inform the purchaser prior to making such decisions as whether or not to relet the property, and obtain his consent.[36] This is particularly true in today's society where various types of tenant enjoy

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32. Prosper Homes Ltd. v. Hambros Bank Executor and Trustee Co. Ltd. (1979) 39 P. & C.R. 395.

33. See V.G. Wellings, "The Vendor as Trustee", (1959) 23 Conv. (N.S.) 173.

34. (1877) 6 Ch. D. 469.

35. [1959] A.C. 124. Under s. 54 of the Indian Transfer of Property Act 1882, the purchaser does not acquire any interest in the property as a result of the contract. The obligation on the vendor to take reasonable care of the property derived from s. 55(1)(e) of the Act.

36. In Egmont v. Smith (1877) 6 Ch. D. 469, 475, Sir George Jessel M.R. expressed the view that the purchaser should be consulted.

considerable statutory protection. The true position was stated in another case as being that:

> as between vendor and purchaser generally the powers of the vendor to act as owner of the property, and (inter alia) to change tenants or holdings, are suspended pending completion of the purchase.[37]

1.26 In accordance with this principle, the vendor should not withdraw an application for planning permission already lodged. If he does so, he will have to compensate the purchaser for the additional expense involved in applying anew.[38] Similarly, if a business is being run at a loss from the property, the vendor should only continue to run it if he informs the purchaser of that intention.[39]

1.27 In addition to the duty not to do acts which damage or reduce the value of the land contracted to be sold, the vendor is also obliged to exercise reasonable care to ensure that these consequences do not occur. While this principle is easy to state, its application can pose problems. It is quite clear that a vendor can be liable in respect of damage done by third parties. This liability stems from a failure to exercise adequate supervision of the property. On this basis the vendor has been held liable to the purchaser for damage caused by tenants before they vacated the property prior to completion of the transaction.[40]

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37. Raffety v. Schofield [1897] 1 Ch. 937, 945 per Romer J.

38. Sinclair-Hill v. Sothcott (1973) 226 E.G. 1399.

39. Golden Bread Co. Ltd. v. Hemmings [1922] 1 Ch. 162.

40. Ferguson v. Tadman (1827) 1 Sim. 530; Royal Bristol Permanent B.S. v. Bomash (1887) 35 Ch. D. 390; Jensen v. Jeffery [1957] N.Z.L.R. 159.

1.28 As well as incurring liability for acts of lawful occupiers, the vendor has also been held responsible for damage inflicted by trespassers. The basis of this liability is, again, failure to take adequate precautions to prevent damage from happening. In Clarke v. Ramuz,[41] after contracts had been exchanged a trespasser removed large quantities of top soil. The vendor was liable to pay compensation to the purchaser, it being held that he had failed to exercise proper supervision of the property. Similarly, in Davron Estates Ltd. v. Turnshire Ltd.[42] a vendor was held liable for damage done by squatters. When obtaining possession, he should, apparently, have taken steps to prevent this from occurring.

1.29 In both these cases, the vendor was held to be at fault in not preventing the damage which occurred. The onus appears to be on the purchaser to establish this. If the property is damaged by vandals, or by the negligence of a third party, it will not always be the case that fault on the part of the vendor can be established. Then it would seem that the purchaser must bear the loss.[43] In addition, as will be seen, it is not clear that the purchaser will have a claim against the person who actually causes the damage, assuming that that person can be identified.[44] If the damage is significant, prolonged disputes pertaining to liability can be anticipated.

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41. [1891] 2 Q.B. 456.

42. (1982) 133 N.L.J. 937.

43. Cedar Transport Group Ltd. v. First Wyvern Property Trustees Co. Ltd. (1980) 258 E.G. 1077; Re Sweeny's Estate (1890) 25 L.R. Ir. 252. See also Smith v. Littlewoods Organisation Ltd. [1987] A.C. 241.

44. See para. 1.35 below.

1.30 Although it seems that the onus is on the purchaser to establish that the vendor has failed to exercise reasonable care, a note of caution should be entered as to this. It could be argued that, as the vendor retains control of the property, the onus is on him, in the event of damage, to show that the damage was not his fault. In the leading case of Scott v. The London and St. Katherine Docks Co.[45] the plaintiff was injured when bags of sugar fell from a warehouse window, the warehouse being owned by the defendant. It was held that as accidents of this type do not normally occur, there was a presumption that the defendant, who had control of the building, had been negligent. The maxim res ipsa loquitur applied.

1.31 This reasoning would appear to be equally applicable in the conveyancing context. As the vendor normally retains possession of the house pending completion, it might be thought that he should be required to show that any property damage was not his fault. This argument was not accepted, however, in the analogous case of Sochacki v. Sas,[46] where Lord Goddard C.J. declined to imply negligence on the part of a lodger for a fire, when he had left the room empty with an unguarded fire burning in a grate. He specifically rejected the argument that the maxim res ipsa loquitur should be applied, although Scott v. The London and St. Katherine Docks Co. was not cited.

1.32 Sochacki v. Sas has been criticised.[47] In part this criticism stems from an excessively lenient view of the

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45. (1865) 3 H. & C. 596.

46. [1947] 1 All E.R. 344.

47. "Fire", [1978] Conv. 183.

facts having been taken in favour of the lodger. More generally, however, the argument that the onus of disproving negligence should be on the person having control of the property seems persuasive. It is nevertheless evident that this important matter is unclear.

1.33 If the vendor's liability is based on breach of a duty of care, there will inevitably be disputes as to whether in any particular case a breach has occurred. Two cases relating to burst water pipes illustrate this problem.[48] In Lucie-Smith v. Gorman[49] the vendor moved out of the house after exchange of contracts. The house was left vacant for three weeks in February with the heating turned off. After the pipes burst he was held liable to the purchaser for the damage which ensued. In contrast to this, in Wycombe Health Authority v. Barnett,[50] the pipes burst when a tenant had left the house unoccupied, again with the heating turned off, but on this occasion for only two days. The duty of a tenant to a landlord is similar to that of a vendor to a purchaser. Despite the temperature at the time being in the region of -6 degrees or -7 degrees C., the Court of Appeal held that the tenant was not liable to the landlord for the damage. It had not been shown that she had failed to take reasonable care of the house.

1.34 On the assumption that the risk of damage does indeed pass to the purchaser, he is not at risk solely with regard to the property he has contracted to buy. In

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48. In neither case is the question of onus of proof discussed.

49. [1981] C.L.Y. 2866.

50. (1982) 264 E.G. 619. Cf. Warren v. Keen [1954] 1. Q.B. 15, 20 per Denning L.J.

Robertson v. Skelton,[51] after a considerable delay in completion occasioned by the purchaser's default, part of the property collapsed and damaged adjoining property. The purchaser was liable for the damage. If such damage occurs whilst the purchaser is uninsured, he will clearly seek to shift the liability elsewhere by establishing that the vendor had failed to exercise reasonable care of the property. This raises the difficulties referred to above.[52] The vendor may be able successfully to rebut the allegation that he failed to exercise proper care of the property by laying the blame on another party.

1.35 As an example, one can instance a situation where the house was re-wired shortly before being put on the market but the work was done negligently with the result that a fire started between contract and completion badly damaging the house. It would seem that the purchaser would, in these circumstances, be unable to sue the electrician in tort in his own right. This is because in Leigh and Sillavan Ltd. v. Aliakmon Shipping Co. Ltd.[53] the House of Lords made it quite clear that a person who owns only a beneficial interest in property cannot sue in negligence for damage to it caused by a third party without joining the legal owner as co-plaintiff or as co-defendant. The argument to the contrary was regarded as unsupportable. Neither is it clear that he could make the vendor bring an action on his behalf.[54] In Canada, when a similar situation occurred, it was held that the vendor and

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51. (1849) 12 Beav. 260.

52. See paras. 1.22-1.33 above.

53. [1986] 2 A.C. 785, 812 per Lord Brandon of Oakbrook.

54. See R.M. Goode, "Ownership and Obligation in Commercial Transactions", (1987) 103 L.Q.R. 433, 455-458.

purchaser acting together could sue the negligent workman[55] and this solution could presumably also be arrived at in England. This nevertheless seems inconvenient as the purchaser would have to complete the contract and then retain contact with the vendor in order to pursue the action.

Repairs and outgoings

1.36 The question often arises as to whether a vendor is under any obligation to effect necessary repairs to the property pending completion and, if so, whether he is entitled to be indemnified by the purchaser for their cost. The primary position appears to be that if the vendor retains possession of the property, he is bound to keep it in a reasonable state of repair, so that a purchaser may take the thing that he has contracted to buy.[56]

1.37 As to whether the vendor can recover the money spent on necessary repairs, the position is not entirely clear. The normal position insofar as trustees are concerned is that they are entitled to be compensated for out-of-pocket expenses reasonably incurred.[57] Because the vendor is regarded as a trustee, one might expect the position to be the same. This would be particularly so where the need for repairs has arisen without fault on the vendor's part, since it would seem to be consistent with the

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55. Buchanan and James v. Oliver Plumbing and Heating Ltd. (1959) 18 D.L.R. (2d) 575.

56. Royal Bristol Permanent B.S. v. Bomash (1887) 35 Ch. D. 390, 396 per Kekewich J.

57. Re Beddoe [1893] 1 Ch. 547. See Snell's Principles of Equity 28th ed., (1982), pp. 255-257.

notion that the risk passes to the purchaser, that he be liable to reimburse the vendor.

1.38 Although there are some judicial indications that repairing expenses can be recovered from the purchaser,[58] the trend of authority is to the contrary. In the cases where the issue has arisen, the determination of the dispute appears to have turned on the question of when the vendor had shown a good title and thus the purchaser could, under the contract, have gone into possession.[59] Thus in Binks v. Lord Rokeby[60] Lord Eldon held that responsibility for deterioration fell on the purchaser after title had been made and he was entitled to possession but that, prior to that date, it fell on the vendor. On the other hand, in Lord v. Stephens[61] the view was simply taken that the purchaser was not liable for the cost of repairs with regard to deterioration even though not apparently caused by the vendor's default. The basis of this may be that a vendor is liable to the purchaser for permissive waste which would mean that the vendor cannot let the property fall into disrepair.[62]

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58. Phillips v. Silvester (1872) 8 Ch. App. 173, 176 per Lord Selborne L.C.; Bolton Partners v. Lambert (1888) 41 Ch. D. 295, 302 per Kekewich J., affirmed without reference to this point (1889) 41 Ch. D. 302.

59. This is considered below, paras. 1.55-1.56.

60. (1818) 2 Swan. 222; Minchin v. Nance (1841) 4 Beav. 332. A delay in completion of 13 years occurred in this case.

61. (1835) 1 Y. & C. Ex. 222.

62. Regent's Canal Co. v. Ware (1857) 23 Beav. 575, 588 per Sir John Romilly M.R.

1.39 A different explanation both for the uncertainty and the willingness to impose liability on the vendor may be in the reluctance, already evidenced, to push the trust analogy too far. In Re Watford Corporation's and A.S. Ware's Contract,[63] the vendor sought to recover from the purchaser, who was in occupation, payments which he had had to make under the War Damage Act 1941.[64] In rejecting this claim, Simonds J. demonstrated a complete lack of sympathy for the vendor's argument based on trust principles. He said:

> It is commonly said ... that in the interval between contract and conveyance the property sold belongs in equity to the purchaser. So it does, and the vendor is, therefore, during that time constructively a trustee for him, but this statement must not be pressed so far as to give to the vendor all the rights of indemnity to which a trustee in the full sense is entitled from his trust estate, for the vendor has his own personal and substantial interest in the property, which he is entitled to protect, and it is, in my judgment, impossible to concede to him, in respect of payments made by him, whether voluntarily or, as this payment was made, compulsorily, the right of indemnity which an ordinary trustee can claim. This is a payment which might in certain circumstances enure for the vendors' own benefit, as, for example, if the purchaser made default in completion and the contract was rescinded.[65]

1.40 This passage explicitly recognises the unusual nature of the trusteeship. The trustee has a valuable interest in the property pending completion and may ultimately derive the benefit from the work done, if the

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63. [1943] Ch. 82.

64. Interestingly, s. 46(3) of the Act provided that any money payable to V was to be held on trust for P if the damage occurred when there was a contract of sale.

65. Ibid., at p. 85.

contract is not actually completed.[66] Moreover, it will be recalled that, pending completion, it is the vendor who is entitled to the rents and profits deriving from the land or, alternatively, to possession of it.[67] Because he derives the benefit from the land prior to completion, it seems only fair that he should be liable for the outgoings.[68] The position would seem to be that the vendor should keep the property in good repair after exchange of contracts. If repairs are needed before completion, the vendor must bear the cost of them but, if actual completion is delayed as a result of the purchaser's default, repairs effected after the contractual completion date are the responsibility of the purchaser.[69] Not for the first time, however, the law relating to this interim period between contract and completion is not as clear as one might expect. It is also apparent that the imposition of a trust does little to clarify the position.

Damage and destruction

1.41 In the passage cited earlier from Lysaght v. Edwards,[70] it was made clear that the traditional view taken in England is that, if the subject matter of the contract is damaged or destroyed between contract and conveyance, then the purchaser must nevertheless complete

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66. See also Ecclesiastical Commissioners v. Pinney [1899] 2 Ch. 729.

67. See para. 1.16 above.

68. Phillips v. Silvester (1872) 8 Ch. App. 173.

69. See also Robertson v. Skelton (1849) 12 Beav. 260, 266 (damage to the property occurred months after the purchaser should have taken possession).

70. See para. 1.3 above.

the contract. Subject to the vendor having taken proper care of the property, the risk is said to pass to the purchaser. Although it has been said that the purchaser must bear the risk of total destruction of the buildings prior to completion,[71] there is little direct authority in point. In addition, it is not entirely clear at what point in time the risk passes. This uncertainty stems from the judicial disagreements as to the nature of the trust involved which have been discussed above.[72]

1.42 If there is a bare trust in existence and, without fault on the part of the trustee, the trust property is destroyed, then it is the beneficiary who suffers the loss. Insofar as contracts for the sale of land are concerned, however, the trust, at least when the contract is wholly executory, is by no means the same as a bare trust. As has been seen, the incidents of the trust are not at all identical to those that normally follow from the existence of a trust relationship. Accordingly the trust itself has been described in a number of quite different ways.

1.43 As was pointed out earlier,[73] the reason why any sort of trust arises at all is that specific performance is readily available when the subject matter of the contract is land. However, there are difficulties with this approach. At the time the parties enter into the contract, they are potentially entitled to specific performance. As the maxim proceeds on the basis that the contract actually should be performed, the more usual view is that greater regard should

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71. See paras. 1.3-1.4 above.

72. See paras. 1.7-1.21 above.

73. See para. 1.7 above.

be had to the question of whether specific performance actually would be ordered than to whether, in theory, it might be. Related also to this is the issue of when the contract ought actually to be performed.

1.44 With regard to the second point, there is judicial support for the view that the purchaser should not be regarded as the beneficial owner until the date of completion or, perhaps even more restrictively, until the purchase money has actually been paid. If the former view, which derives some support from Kettlewell v. Watson,[74] is followed, then the time when the property is destroyed becomes vital. Unfortunately, the issue did not arise in Paine v. Meller[75] when after the contractual date for completion had passed, the house was destroyed by fire and the purchaser was held to be bound to complete.

1.45 The view that the purchaser only acquires a beneficial title from the date of completion has attracted little judicial support. Dicta advancing the view that it is only helpful to see the purchaser as beneficial owner from the time when he has paid the purchase price are, however, rather more numerous and this view derives support from the approach of the House of Lords in Rose v. Watson.[76] In that case, it was held that a purchaser obtained a lien over land contracted to be sold corresponding to the amount of the purchase price, payable

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74. (1884) 26 Ch. D. 501, 507. But see Re Birmingham [1959] Ch. 523.

75. (1801) 6 Ves. 349. See Gordon Walker, "Insurance and the Sale of Land", [1981] Aust. Bus. L. Rev. 148, 155.

76. (1864) 10 H.L.Cas. 672; Re Pagani [1892] 1 Ch. 236.

in instalments, that had been paid. The position as to the beneficial ownership of the land was explained in the following terms by Lord Westbury:

> When the owner of an estate contracts with a purchaser for the immediate sale of it, the ownership of the estate is, in equity, transferred by that contract. Where the contract undoubtedly is an executory contract, in this sense, namely, that the ownership of the estate is transferred, subject to the payment of the purchase-money, every portion of the purchase-money paid in pursuance of that contract is a part performance and execution of the contract, and, to the extent of the purchase-money so paid, does, in equity, finally transfer to the purchaser the ownership of a corresponding portion of the estate.[77]

1.46 This analysis has been expressly adopted in Ireland, where Kenny J. specifically rejected the view that the vendor became a trustee upon signing the contract, but insisted that it is only correct to say that the beneficial interest in the land passes to the purchaser from the time when he has paid the purchase price.[78]

1.47 The view that the beneficial interest in the land passes to the purchaser when he pays the purchase price derives from earlier judicial attempts to analyse the nature of the trust which has been said to be created by the contract itself. In Wall v. Bright,[79] Sir Thomas Plumer M.R. found great difficulty in seeing the position of a vendor under an executory contract for the sale of land as

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77. Ibid., at p. 678. See also, to similar effect, at p. 683 per Lord Cranworth.

78. Tempany v. Hynes [1976] I.R. 101, 114. Cf. Killner v. France [1946] 2 All E.R. 83 where the contract provided that the risk was to remain with the vendor until completion.

79. (1820) 1 Jac. & W. 494.

analogous to that of a trustee. Being conscious that this analogy had frequently been made, however, he described the vendor as being a trustee "sub modo", the meaning of this being that the vendor was potentially a trustee, only becoming one when the purchase money was paid and he became bound to convey the land.[80] Similarly but without apparent difficulty, Harman J. regarded a vendor of land as becoming a trustee of the legal estate on entering into the contract and a bare trustee when all instalments of the purchase price had been paid.[81]

1.48 There is another reason for doubting whether it is correct to say that the risk of destruction of the property always passes to the purchaser. The basis upon which the purchaser has been described as the beneficial owner of the land is that specific performance would be ordered of the contract and that equity then looks on that which ought to be done as already having been done. If specific performance is not available, then it can be argued that it is incorrect to view the purchaser as the owner in equity.

1.49 A number of dicta provide support for this view. One of the clearest statements to this effect is that of Lord Parker of Waddington. In Howard v. Miller[82] he said:

> It is sometimes said that under a contract for the sale of an interest in land the vendor becomes a trustee for the purchaser of the interest contracted to be sold subject to a lien for the

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80. Ibid. at pp. 501, 503. See also Dowson v. Solomon (1859) 1 Drew. & Sm. 1, 9 per Sir Richard Kindersley V.-C.

81. Bridges v. Mees [1957] Ch. 475, 485.

82. [1915] A.C. 318.

> purchase-money; but however useful such a statement may be as illustrating a general principle of equity, it is only true if and so far as a Court of Equity would under all the circumstances of the case grant specific performance of the contract.[83]

1.50 Lord Parker repeated this view, again in giving the advice of the Privy Council, in Central Trust and Safe Deposit Co. v. Snider[84] He expressly made the point that if, for any reason, equity would not decree specific performance, then the vendor either never was or has ceased to be a trustee at all.

1.51 The significance of this reasoning is that it undermines the proposition that it is because the purchaser is the owner of the property in equity, that the risk of its suffering damage or destruction passes to him.[85] First it could be argued that, in the exercise of its equitable discretion, a court would not decree specific performance of a contract to sell a house when that house has been destroyed. Such an order would cause hardship,[86] it not being crucial that the hardship occurred after entry into the contract.[87] This argument has prevailed in the United

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83. Ibid., at p.326.

84. [1916] 1 A.C. 266, 272.

85. Haynes v. Haynes (1861) 1 Drew. & Sm. 426, 451-452; Cornwall v. Henson [1899] 2 Ch. 710, 714 (rvsd. on the facts [1900] 2 Ch. 298); Plews v. Samuel [1904] 1 Ch. 464, 468; Edwards v. West (1878) 7 Ch. D. 858, 862; Ridout v. Fowler [1904] 1 Ch. 658, 662 (affmd. [1904] 2 Ch. 93); Simmons v. Pennington & Son [1955] 1 W.L.R. 183.

86. Patel v. Ali [1984] Ch. 283.

87. Walsh v. Lonsdale (1882) 21 Ch. D. 9.

States where specific performance was refused of a contract for the sale of land when a rezoning ordinance prevented the contemplated use of the property, thereby causing a very substantial reduction in its value.[88]

1.52 A second argument to the same effect is that the vendor is in breach of one of his contractual obligations if the property is destroyed. There is usually an obligation in conveyancing contracts, implied if not express, that the vendor will give vacant possession upon completion. This has been held to mean that the property must be conveyed in a state in which the purchaser can occupy it.[89] If a house is being sold and prior to completion it is destroyed, perhaps by fire or by an explosion, then the vendor cannot give vacant possession of the property in that sense. Consequently specific performance would not be awarded and so, it could be argued, the risk should not pass to the purchaser.[90]

1.53 A similar argument prevailed in Cook v. Taylor.[91] After contracts had been exchanged, the house was requisitioned. As it was no longer possible for the vendor to give vacant possession, Simonds J. refused to order specific performance, and ordered the return of the purchaser's deposit. However, the judge distinguished between the actual case and the situation where a house was

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88. Clay v. Landreth (1948) 175 A.L.R. 1047 (Virginia).

89. Cumberland Consolidated Holdings Ltd. v. Ireland [1946] K.B. 264.

90. B.P. Thompson, "Must a Purchaser Buy a Charred Ruin?" [1984] Conv. 43, 50.

91. [1942] Ch. 349.

destroyed by fire or flood. In that event, the view was expressed that the purchaser was bound to complete. Presumably the basis of this distinction is that in the latter situation the vendor can still give vacant possession of the land itself.

1.54 Different interpretations of the decisions and dicta cited may lead to serious doubts as to the validity of the rule stated in Lysaght v. Edwards, that the risk of damage or destruction of the property between contract and conveyance passes to the purchaser. That rule has, however, been frequently repeated and, indeed, was by no means novel in that case. It is also true that the rule can be justified theoretically by yet another explanation.

1.55 In contrast to the authorities that insist that specific performance must remain available, there is also a line of authority where this requirement is not insisted upon.[92] These cases insist merely upon the contract being valid if the beneficial ownership is to pass to the purchaser. Validity is generally taken to mean that the vendor has a good title or one that the purchaser has agreed to accept. The interpretation placed on the expression "valid contract" in Lysaght v. Edwards[93] was that there was nothing in the contract itself to cause it to be set aside. This would encompass such matters as the vendor having a good title and also, presumably, that there was no significant misdescription or misrepresentation.

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92. See Philip H. Pettit, "Conversion Under a Contract for the Sale of Land", (1960) 24 Conv. (N.S.) 47; Simon Gardner, "Equity, Estate Contracts and the Judicature Acts: Walsh v. Lonsdale Revisited", (1987) 7 O.J.L.S. 60.

93. (1876) 2 Ch. D. 499, 507.

1.56 It might be thought that if the vendor showing a good title was the pre-condition for the purchaser to become the beneficial owner, then that date would be the moment when the risk passes. This is not so, however. Instead, the effect of the vendor showing a good title is retrospective: the purchaser is treated as the beneficial owner from the date of the contract.[94] On this basis, therefore, if a house is destroyed the day after contracts have been exchanged, then, provided that the vendor can show a good title to the land in accordance with the contract, the loss falls on the purchaser.[95]

1.57 Further, there are cases where beneficial ownership has been held to have passed despite specific performance seemingly being unavailable. In Gordon Hill Trust Ltd. v. Segall[96] D contracted to buy property, at the time being used as a school, from V. D then contracted to re-sell the property to P. The contract between V and D provided that completion would not take place unless V secured alternative accommodation for use as a school. If this did not occur within two years, D was to have a right to rescind. V never did secure alternative accommodation and hence that contract was not completed. The action arose when P sued D for deceit: it being alleged that he had fraudulently represented he was the owner of the property.

1.58 Because D had acted in good faith, this action was in any event doomed. The Court of Appeal, however, also

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94. Lysaght v. Edwards (1876) 2 Ch. D. 499, 510 and at p. 518. See A.J. Oakley, Constructive Trusts 2nd ed., pp. 148-155.

95. Fletcher v. Manton (1940) 64 C.L.R. 37.

96. [1941] 2 All E.R. 379.

took the view that what had been represented was in fact true. This was because D was considered to have had an equitable title to the property by reason of his contract with V, despite specific performance not being available to enforce that contract.[97] Thus the case provides support for the view that the passing of beneficial ownership does not depend on the continued availability of specific performance but, instead, derives from the existence of an initially valid contract.

1.59 Lake v. Bayliss[98] was a similar decision. In return for an agreement to abandon two writs issued against him, the defendant agreed to convey land to the plaintiff. In breach of contract, he then conveyed the land for value to a third party. It was held that the plaintiff could recover the purchase money in the hands of the vendor by virtue of the proprietary remedy of tracing: the money in the defendant's hands represented the land which was owned in equity by the plaintiff.

1.60 The decision is not entirely satisfactory as it was not made clear whether the original contract was protected in the appropriate manner by registration. If not, then specific performance would have ceased to be available and, on one view, the result should have been that the defendant was not regarded as ever having been a trustee of the property contracted to be sold. Nevertheless, the absence of any importance being attached to the registration point does indicate that the continued availability of specific

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97. Ibid., at p. 388 per Luxmoore L.J.

98. [1974] 1 W.L.R. 1073.

performance was not regarded as necessary for the purchaser to be treated as equitable owner of the land.

Frustration

1.61 An additional uncertainty is the extent to which the doctrine of frustration will operate to relieve the purchaser from having to complete a contract when there has been substantial damage to its subject matter. So far as we know, there is no English case where a contract for the sale of land has been held to be frustrated. One case where such an argument might be thought to have been feasible was Cass v. Rudele[99] where the land to be sold appeared to have been destroyed by earthquake prior to completion. The case may, however, have been misreported[100] and consequently little can be read into it.

1.62 The matter has been discussed on several occasions by English courts without a firm conclusion having been reached. Some judicial statements have denied the applicability of the doctrine to contracts for the sale of land,[101] whilst others have accepted that it does apply, without actually applying it to the facts of the case.[102]

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99. (1692) 2 Vern. 280.

100. See Samuel Williston, "The Risk of Loss After an Executory Contract of Sale in the Common Law", (1895) 9 Harv. L.R. 106, 111 n.2.

101. Hillingdon Estates Co. v. Stonefield Estates Ltd. [1952] Ch. 627, 631 per Vaisey J.

102. Amalgamated Investment and Property Co. Ltd. v. John Walker & Sons Ltd. [1977] 1 W.L.R. 164, 173 per Buckley L.J.; Universal Corporation v. Five Ways Properties Ltd. [1978] 3 All E.R. 1131, 1135 per Walton J.; [1979] 1 All E.R. 552, 554 per Buckley L.J.

Much of the uncertainty stemmed from the maxim of equity looking on that as done which ought to be done: because in equity an estate had already passed to the purchaser, it was thought that frustration could not apply. However, since the House of Lords' decision in National Carriers Ltd. v. Panalpina (Northern) Ltd.,[103] this objection may now be seen as untenable.

1.63 In Panalpina, it was accepted that, in principle, a legal lease could be frustrated, although, on the facts where access to a warehouse was impossible for twenty months in the context of a ten year lease, it was held that the doctrine did not apply. The House was at pains to emphasise that the doctrine would only apply rarely to frustrate a lease. It was nevertheless accepted that the general principle of frustration applies. The principle is that:

> frustration occurs whenever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract.[104]

1.64 Counsel for the landlord had contended that frustration could not apply to leases because the contract was executed, drawing an analogy with sales of land. It was clear that sale of land was being used to refer to a completed contract and the analogy was rejected as false. Lord Simon of Glaisdale accepted that a fully executed

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103. [1981] A.C. 675.

104. Davis Contractors Ltd. v. Fareham U.D.C. [1956] A.C. 696, 729 per Lord Radcliffe, cited at [1981] A.C. 675, 688.

contract could not be frustrated but held that a lease, which imposes on-going mutual obligations, did not fall into this category.[105] It would seem to follow that a contract of sale, where the purchaser has not paid the purchase price and no conveyance has been executed, can be frustrated.

1.65 Accepting that a contract for the sale of land can in principle be frustrated, what event would cause the doctrine to be applied? In Panalpina, the examples given concerned the total destruction of the whole property, for example, a lease of a house on a cliff-top where, by erosion or natural catastrophe, the land had fallen into the sea, or the lease of a first floor flat when the whole building had been destroyed by fire. The Privy Council, on appeal from Hong Kong, has indeed held that a contract to buy a flat in a building which was destroyed by a landslip prior to completion was frustrated. In that case, hundreds of tons of earth also disappeared.[106] The issue remains whether a contract for the sale of a house will be frustrated if the house is destroyed by fire or some other disaster.

1.66 In the examples given in the House of Lords, all that would remain for the tenant would be a lease of airspace: obviously a wholly different proposition from a lease of a building. If the land itself is not destroyed but the building upon it is, then it could be argued that the land can still be conveyed, leaving it to the purchaser

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105. Ibid., p. 705.

106. Wong Lai Ying v. Chinachem Investment Co. Ltd. (1979) 13 B.L.R. 81. Owing to the number of deaths caused by this disaster, considerable delay in offering permission to rebuild was inevitable.

to reinstate the building: an option not available in the examples given in Panalpina.

1.67 Although appreciating the force of this argument, we feel that it may not be conclusive. In Canada, it has been accepted for some time that contracts for the sale of land can be frustrated. In Capital Quality Homes Ltd. v. Colwyn Construction Ltd.[107] the contract provided for twenty-six deeds of conveyance of twenty-six building lots to be executed, the purchaser, to the vendor's knowledge, intending to build homes on each plot and sell them separately. Owing to legislation enacted after contracts had been exchanged, this subdivision of the building plot became impossible and the Ontario Court of Appeal held the contract to have been frustrated.

1.68 In reaching this conclusion, reliance was placed on Cahan v. Fraser,[108] where a flood caused an inspection of a property to become impossible. This was held to frustrate the option to purchase it, and the money paid for an extension of the period in which the option could be exercised was ordered to be returned. Applying this decision, it was held that the basis of frustration was that a supervening event had occurred, beyond the control of the parties, which resulted in a significant change in the original obligation assumed by them under the contract. In these circumstances it was said to be illogical and unreasonable to contend that the fundamental object of the contract could still be effected simply because the equitable interest had passed to the purchaser.

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107. (1975) 61 D.L.R.(3d) 385.

108. [1951] 4 D.L.R. 112.

1.69 This reasoning was approved, albeit not applied on the facts, in Victoria Wood Development Corp. Inc. v. Ondrey,[109] and seems apt to describe the position when a house is destroyed between contract and conveyance. Some support for this view can be derived from the facts of the leading case of Taylor v. Caldwell,[110] where a contract to hire (not lease) a music hall for four separate days was held to have been frustrated after the hall had been destroyed by fire. Nevertheless, in the absence of direct authority, the position is unclear. It can also be added that the argument in favour of the application of frustration becomes weaker if the property is merely damaged, albeit substantially, prior to completion. In short, although there is clearly scope for a purchaser to argue where a house has been badly damaged or destroyed after exchange of contracts, that the contract for its purchase has been frustrated, this argument is as yet untested.

The case for reform

1.70 As has been seen, it is a long accepted principle of English law that the creation of an enforceable contract of sale has the effect of making the purchaser the beneficial owner of the land. This principle has a considerable effect on the rights and duties of the contracting parties. The principal consequence is that the risk of the property being damaged or destroyed passes to the purchaser. Other matters affected are the vendor's duties with regard to the maintenance and management of the

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109. (1978) 22 O.R. (2d) 1 (CAN).

110. (1863) 3 B. & S. 826.

property and his liability to account for certain benefits derived from the land.

1.71 As has been seen, however, the law with regard to these areas is by no means clear. This may be because instead of asking what the vendor is or should be contractually obliged to convey, these matters have been worked out by the application of trust principles. Yet the trust that arises is on any view a most unusual one because the vendor, until paid in full, retains a valuable personal interest in the property. Because the trust is unusual, it is difficult to derive from normal trust principles what the obligations of the vendor and purchaser actually are. In particular, the most serious consequence - that the risk of destruction of or damage to the property passes to the purchaser - is itself open to argument. It is not necessary for us to express our view as to which of the rival arguments is likely to prevail. The existence of the uncertainty is, however, a good reason in itself why the law should be put on a statutory footing to ensure that these important matters are made clear.

1.72 It is clear that the purchaser is exposed to serious risk when he enters into a contract for the sale of land. Yet the existence of this risk may be quite unknown to an unadvised purchaser who may take the not unnatural view that his responsibility for the property will start when he becomes the legal owner of it. It is true that a purchaser who is entering a conveyancing transaction with the benefit of legal advice is likely to be advised to insure against this risk and, indeed, an adviser who failed to give such advice would almost certainly be liable in

negligence for loss caused by this failure.[111] Nevertheless, the unadvised purchaser may be unaware of the need for this safeguard.

1.73 A further problem that can arise for a purchaser is that there might be practical difficulties in ensuring that the property is insured from date of the contract. If land is being bought at auction, the successful bidder becomes committed to the purchase when the hammer falls. If insurance has not been arranged prior to the auction, which is quite possible as the bidders will not know in advance who will make the successful bid, there will necessarily be a short period of time when the purchaser is not insured and, therefore, at risk.[112]

1.74 Whereas the purchaser runs the risk of catastrophic loss if he enters into the contract without having arranged insurance, the vendor's position is far safer. Because he is the legal owner of the property, he will almost inevitably have insured the property and is unlikely to have cancelled his policy, simply because he has entered into a contract to sell the house. Indeed, if he has for some reason failed to insure the property, his position is much improved by entering into a contract for sale since, in so doing, he passes the risk to the purchaser.

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111. Carly v. Farrelly [1975] 1 N.Z.L.R. 356. If the purchaser is knowledgeable and experienced in these matters, the adviser may not be liable for a failure to tender such advice. See Carradine Properties Ltd. v. D.J. Freeman & Co. (1982) 126 S.J. 157.

112. J.E. Adams, "Property Damage between Contract and Completion", (1971) 68 L.S. Gaz. 224.

1.75 On the basis that the risk does pass to the purchaser, it is essential that the purchaser is adequately insured from the date of exchange of contracts.[113] This will mean taking out his own insurance, irrespective of whether or not the vendor has maintained his own policy. At common law it is clearly established that the purchaser cannot recover moneys paid to the vendor under his insurance policy, if the insured event occurs after exchange of contracts.[114] The vendor is not liable to account for this money. If he has recovered on his policy, he is nevertheless entitled to receive the purchase price from the purchaser. This means that he will have suffered no loss as a result of the property damage and, because an insurance contract is a contract of indemnity, he will be liable to repay to the insurance company the amount it paid out.[115] The result of this is that in many cases the vendor is needlessly spending money maintaining his insurance policy.

1.76 It would be a mistake to conclude from this that a vendor can safely allow his own insurance policy to lapse after exchange of contracts. Even on the analysis employed in Lysaght v. Edwards, the beneficial title only passes to the purchaser if the contract is valid. This means that the vendor is able to show a good title and also, it is suggested, that there is no substantial misdescription of

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113. The need for a purchaser to obtain a valuation specifically for insurance purposes and difficulties over the meaning of reinstatement were highlighted recently by Schiemann J. in Beaumont v. Humberts, noted in the Estates Gazette of 23 April 1988 at p. 91.

114. Rayner v. Preston (1881) 18 Ch. D. 1.

115. Castellain v. Preston (1883) 11 Q.B.D. 380; the position if the insurance money has been spent on repairing the property appears different: cp. Collingridge v. The Royal Exchange Assurance Corporation (1877) 3 Q.B.D. 173.

the property in the contract nor misrepresentation prior to it. If the property is damaged and one of these defects in the contract is present, then the vendor must bear the loss.[116] In addition if the arguments referred to above, that the risk does not pass to the purchaser, are valid, then it will be necessary for the vendor to be insured. He should, therefore, in all cases maintain his own insurance policy.

1.77 Under the law as stated in Lysaght v. Edwards, it is a counsel of prudence for both vendor and purchaser to insure the property between contract and completion. This seems to us to be an unnecessary duplication of expenditure.[117] If reform resulting from our proposals prevents this duplication, vendors and purchasers might benefit from a small reduction in their conveyancing costs.

1.78 To summarise our views, we find the law relating to the period between exchange of contracts and completion to be unsatisfactory. Not only is the law unnecessarily complex and uncertain, but more importantly it exposes the purchaser to the risk of major financial loss. As he is not usually in possession of the property, this loss will be caused by events outside his control. This we consider to be unjust[118] and is a consequence we are anxious to prevent. In addition, it is common for insurance premiums to

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116. Simmons v. Pennington & Son [1955] 1 W.L.R. 183.

117. See also Trevor M. Aldridge, "Shifting the Insurance Burden", (1974) 124 N.L.J. 966.

118. For a similar conclusion from a civil law viewpoint, see A.D.M. Forte, "Must a Purchaser Buy Charred Remains? - An Analysis of the Passing of Risk on Civilian Principles", (1984) 19 Irish Jurist (N.S.) 1.

be paid by two people to cover the same property, which we consider to be a waste of money. Accordingly we now turn to consider methods by which these consequences can be avoided. We first consider whether our principal aim of safeguarding the purchaser can be achieved by changes to the law of insurance. We then explore whether it would be preferable to recast the law governing the rights and obligations of the parties to a contract for the sale of land. We would, however, re-emphasise that all our views and proposals are provisional and we would be grateful for views upon them.

PART II
INSURANCE

2.1 The current law which assigns the risk of damage to the property pending completion, makes it vital for the purchaser to be protected by insurance. Unless he is adequately protected, he runs the risk of financial catastrophe should the property be badly damaged or destroyed. The practical consequence of this will often be that the purchaser takes out his own policy, thereby leading to a duplication of insurance. This is because at common law he cannot rely on the vendor's policy and it is unclear whether the existing statutory provisions would enable him to do so either.

2.2 The position at common law with regard to insurance is this. If an insured event occurs, the vendor, by virtue of his own personal interest in the property, may still claim on his own insurance policy.[1] Despite the fact that the vendor is for some purposes regarded as a trustee, he is not liable to account to the purchaser for this money.[2] Rather it appears that the purchaser must complete at the full contract price. Once the purchaser has done this, the vendor is in receipt of both the purchase price and the insurance money. To prevent the vendor from obtaining a profit as a result of the damage to the property, the insurance company can recover from him the amount they have paid to him (unless actually spent on repairs when the

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1. Collingridge v. The Royal Exchange Assurance Corporation (1877) 3 Q.B.D. 173; Castellain v. Preston (1883) 11 Q.B.D. 380, 385 per Brett L.J.

2. Rayner v. Preston (1881) 18 Ch. D. 1.

position appears undecided). An insurance contract is a contract of indemnity and, as the vendor has suffered no loss, the money paid out can be reclaimed. In addition to this, the insurer on paying out on an insurance contract is subrogated to the rights of the insured. This means that the insurer can pursue any remedy open to the insured to offset the loss. If the vendor has not been paid, the insurer can enforce the contract against the purchaser and obtain the purchase price.[3] In either event, therefore, the purchaser's position is vulnerable.

2.3 The position at common law leads to the following results. The vendor has paid the premiums on an insurance policy. Despite one of the insured events occurring, the insurance company may be able to recover any money paid out, in which case the proportion of the premiums relating to the period after exchange of contract is often thought of as in the nature of a windfall. Secondly, as the purchaser cannot claim the benefit of this policy, but must nevertheless pay the contract price in full, he must take out a policy from the time of exchange of contracts in order to protect his own interest. This leads to the duplication of insurance.

2.4 In common with most commentators, we regard this position as unsatisfactory.[4] In this Part of the working

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3. Castellain v. Preston (1883) 11 Q.B.D. 380.

4. D.I. Cassidy, "The Insurance of Land and Buildings the Subject of a Contract of Sale", (1971) 45 A.L.J. 30; Trevor M. Aldridge, "Shifting the Insurance Burden", (1974) 124 N.L.J. 966; J.E. Adams and T.M. Aldridge, "Insurance of Domestic Property between Contract and Completion", (1980) 77 L.S. Gaz. 376; Gordon Walker, "Insurance and the Sale of Land", [1981] Aust. Bus. L. Rev. 148; M.P. Thompson, "Must a Purchaser Buy a Charred Ruin?" [1984] Conv. 43, 50-52. Cf. E.J.D. Peverett, "Shifting the Insurance Burden: Another View", (1975) 125 N.L.J. 217.

paper, we examine the effect of the existing statutory provisions which affect this area. In addition, we will consider reforms enacted in other common law jurisdictions to ascertain whether a satisfactory solution to the existing problems can be effected by legislation dealing specifically with the law of insurance.

Statutory provisions regulating insurance law

2.5 There are two statutory provisions which are relevant to the situation where the property is damaged between contract and conveyance. The older of the two is the Fires Prevention (Metropolis) Act 1774. Under section 83 of this Act, insurers are authorised and required upon the request of any person interested in any house or building which may be burnt down, demolished or damaged by fire, to cause the insurance money to be laid out and expended, as far as the same will go, towards rebuilding, reinstating or repairing such house or building.

2.6 Although this statutory provision would appear to be wide enough to allow a purchaser under an uncompleted contract to require the insurers to expend the money on the reinstatement of the property, it is considered to be doubtful whether it is safe for a purchaser to rely upon it. Lord Watson raised the question in Westminster Fire Office v. Glasgow Provident Investment Society[5] whether the Act applies outside London. However, the now accepted view is that the Act is not limited in this way.[6] Doubt remains

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5. (1888) 13 App. Cas. 699, 716.

6. Ex parte Gorely (1864) 4 De G.J. & Sm. 477; Re Quicke's Trusts [1908] 1 Ch. 887; Sinnott v. Bowden [1912] 2 Ch. 414; see also MacGillivray and Parkington on Insurance Law, 7th ed., (1981), para. 1686.

however whether a person can claim under this section simply because he has an interest in the land, or whether he must also have an interest in the policy. The latter view was supported by the Earl of Selborne in the Westminster Fire Office case and would exclude a claim by a purchaser.[7] However, this restrictive view has itself been doubted.[8]

2.7 In Rayner v. Preston,[9] James L.J. in his dissenting judgment expressed the view that a purchaser under an uncompleted contract of sale would be able to require the property to be reinstated. However this view was doubted as inconsistent with the indemnity basis of insurance by Bowen L.J. in Castellain v. Preston.[10] As the vendor was in receipt of the purchase money, he had suffered no loss, and the Act ought to be of no avail to the purchaser. This doubt was not expressly considered in Royal Insurance Co. Ltd. v. Mylius[11] where, by a bare majority, the High Court of Australia held that the purchaser could require that the insurance money be used towards reinstatement of the property under a provision similar to the 1774 Act. That case had unusual features, however, in that the vendor had been paid in full before the fire occurred and also that the insurance was effected on behalf of a mortgagee who, because of the fire, had lost the security for the loan.[12] The case is therefore of only limited persuasive authority.

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7. (1888) 13 App. Cas. 699, 714.

8. Sinnott v. Bowden, above.

9. (1881) 18 Ch. D. 1, 15.

10. (1883) 11 Q.B.D. 380, 399-401.

11. (1926) 38 C.L.R. 477.

12. For the mortgagee's right to secure reinstatement, see Law of Property Act 1925, s.108.

2.8 Mylius was distinguished recently by the High Court of Australia in Kern Corporation Ltd. v. Walter Reid Trading Pty. Ltd.[13] In this case a purchaser of commercial property sought to rely on section 58 of the Property Law Act 1974 (Queensland) after the property had been destroyed by fire prior to completion. It was held that this section, which is modelled on the 1774 Act, did not entitle him to insist that the vendor's insurer pay out money towards reinstatement of the property. This was because the contract had been completed and consequently no money was payable to the vendor. If, however, the money had been paid prior to completion, the insurer could, by exercising his right of subrogation, recover the purchase price from the purchaser. If this case is followed in England, then clearly the purchaser cannot rely for his protection on the Fires Prevention (Metropolis) Act 1774. To these doubts as to whether the purchaser can require the reinstatement of the property can be added the additional consideration that the Act only applies in the event of damage by fire. This limitation was imposed as the object of the Act was to prevent fraudulent claims resulting from arson: a factor in itself which may cause the Act to be construed narrowly.[14] Although fire is one of the more likely hazards affecting the property, the Act obviously does not provide comprehensive protection for the purchaser, even if he is able to rely upon it in the event of damage by fire. A further drawback of the section is that the policy may not provide sufficient cover to effect reinstatement. It is not surprising, therefore, that the section is apparently not relied upon in practice.[15]

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13. (1987) 61 A.L.J.R. 319.

14. Royal Insurance Co. Ltd. v. Mylius, above at pp.499-500 per Higgins (dissenting).

15. See also B. Conrick (1986) 1 Aust. Property Law Bulletin 28 discussing an unreported Australian decision which highlights the limitation of this section.

2.9 The remaining statutory provision which is relevant to the insurance position between vendor and purchaser is contained in the Law of Property Act 1925. This provides:

> 47-(1) Where after the date of any contract for sale or exchange of property, money becomes payable under any policy of insurance maintained by the vendor in respect of any damage to or destruction of property included in the contract, the money shall, on completion of the contract, be held or receivable by the vendor on behalf of the purchaser and paid by the vendor to the purchaser on completion of the sale or exchange, or so soon thereafter as the same shall be received by the vendor.
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> (2) This section applies only to contracts made after the commencement of this Act, and has effect subject to -
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> (a) any stipulation to the contrary contained in the contract,
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> (b) any requisite consents of the insurers,
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> (c) the payment by the purchaser of the proportionate part of the premium from the date of the contract.

2.10 The object of this section is clear: to make available to the purchaser the monies paid under the vendor's insurance policy. Unfortunately there are various difficulties attaching to the operation of this section which have the effect of making it inadvisable in practice for a purchaser to rely upon it.

2.11 The first, and most serious, difficulty relates to whether the insurer must pay at all if only the vendor has an existing policy on the property. In Ziel Nominees Pty. Ltd. v. VACC Insurance Co.[16] the purchaser contracted to

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16. (1975) 7 A.L.R. 667.

buy the vendor's land. The property was insured with the defendant insurance company. In January 1973, the land was severely damaged by fire and, shortly afterwards, the vendor claimed on the policy. In late February, the vendor signed an authority addressed to the insurance company to pay to the purchasers' solicitors all the money to which the vendor was entitled under the policy. That authority was handed over on completion the following day, when the purchase price was paid. The purchasers intended to continue with the policy, premiums thereunder having been adjusted between vendor and purchasers. Upon the refusal of the insurance company to pay the sum claimed to the purchasers, the purchasers sued, joining the vendor as a defendant.

2.12 The High Court of Australia unanimously held in favour of the insurance company. Assuming there to have been a valid assignment of the benefit of the policy, it was nevertheless held that the purchasers could not sue upon it. This was because the vendor had received the purchase price stipulated by the contract and consequently had suffered no loss as a result of the fire. Because no loss had been caused by the insured event, no insurance money was payable to him.

2.13 Although in this case the assignment of the benefit of the policy occurred after the fire, nothing turned on this fact. This was stated in terms by Barwick C.J. who said that when the assignment became effective "the vendor was not and could not at that time have become entitled to any moneys under the policy: and this for the simple and direct reason that he had not and could not suffer any loss by reason of the destruction or damage of the improvements on

the land which he had sold. In other words he had nothing to assign."[17]

2.14 In Ziel, no money was payable by the insurer, because the insured had already received the purchase money. Even where that is not the case, because of the doctrine of subrogation, the puchaser's position may not be improved. In the New Zealand case of Budhia v. Wellington City Corporation[18] a house contracted to be sold was partially destroyed by fire. The vendor undertook to pay the insurance money to the purchaser who had paid a proportionate part of the premiums. The insurance company paid out to the vendor, and then exercised its rights of subrogation and required the purchaser to pay the full purchase price to the vendor. This action succeeded with the result that the vendor suffered no loss so that the amount paid under the policy was refundable.

2.15 The same right of subrogation exists in England. In Phoenix Assurance Co. v. Spooner[19] the defendant had insured his land with the plaintiff company. During the currency of the policy, a corporation served a notice to treat under the Lands Clauses Consolidation Act 1845. Before anything had been done under the notice, the buildings on the land were destroyed by fire and the plaintiff paid out their full value under the insurance policy. The defendant and the corporation then agreed a price for the land which reflected the amount that the

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17. Ibid., at p.669.

18. [1976] 1 N.Z.L.R. 766.

19. [1905] 2 K.B. 753; Poole v. Adams (1864) 33 L.J. Ch. 639.

defendant had already received from the plaintiff, the corporation agreeing to indemnify the defendant against any claim by the plaintiff. Bigham J. held that the insurer, having paid out on the policy, was subrogated to the rights of the insured. These rights included a right to sell the property to the corporation at its full value prior to the fire. Accordingly, the plaintiff could recover the insurance money from the defendant who, under the indemnity, could recover that sum from the corporation.

2.16 It is true that in none of these cases did the courts have to consider either section 47 of the Law of Property Act 1925 or any equivalent provision. If the Ziel case had been followed, however, and the purchaser had paid the purchase price, then no money would have been payable to the vendor under the insurance policy. If the purchase price had not been paid, then after the insurance money had been paid, the insurer could have claimed the purchase price from the purchaser by exercising its right of subrogation.

2.17 Either of these constructions would render section 47 otiose. Because of this consideration it may well be that the English courts would construe the section in such a way as to avoid this result. It has been forcefully pointed out, however, that to achieve this result would require a willingness to construe the legislation liberally.[20] It is clear, therefore, that the section, as drafted, may not achieve the aim of ensuring that the purchaser can take advantage of the vendor's insurance policy.[21]

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20. New South Wales Law Reform Commission, op. cit., para. 3.4.

21. Chief Justice's Law Reform Committee (Victoria, 1979), Report on Insurance of Real Property, Appendix A, p. 2; see also R.E. Megarry and H.W.R. Wade, The Law of Real

2.18 It would, of course, be possible to amend section 47 so as to remove these doubts as to its efficacy. In Queensland, section 63(1) of the Property Law Act 1974 enacts a similar provision to that contained in section 47 of the Law of Property Act 1925. Section 63(2) further provides that money does not cease to become payable to the vendor merely because the risk has passed to the purchaser. It has been commented, however, that even this provision may not be adequate to achieve the desired effect, because the reason that the money is not payable to the vendor is not because the risk has passed to the purchaser but because he has suffered no loss.[22]

2.19 To make it clear that an argument based on Ziel cannot succeed, perhaps the best model on which to base any amendment is contained in the Sale of Land (Amendment) Act 1982 enacted in Victoria. This operates by inserting new sections into the Sale of Land Act 1962. The new section 35 provides that:

> 35(1) During the period between the making of a contract for the sale of land and the purchaser becoming entitled to possession or to the receipt of rents and profits pursuant to the terms of the contract, any policy of insurance maintained by the vendor in respect of any damage to or destruction of any part of the land agreed to be sold pursuant to the contract shall in respect of the said land, to the extent that the purchaser is not entitled to be indemnified under any other policy of insurance, enure for the benefit of the purchaser as well as

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Property 5th ed., (1984), p. 604; Cheshire and Burn's, Modern Law of Real Property 13th ed., (1982), p.124, n.17.

22. New South Wales Law Reform Commission, op. cit., paras. 3.9-3.10. In both Queensland and Victoria, the legislation also confers on the purchaser the right to recind in certain circumstances.

for the vendor and the purchaser shall be entitled to be indemnified by the insurer under any such insurance policy in the same manner and to the same extent as the vendor would have been if the land had not been subject to the contract.

(2) It shall not be a defence or answer to any claim by the purchaser against the insurer made under sub-section (1) hereof that the vendor otherwise would not be entitled to be indemnified by the insurer because the vendor has suffered no loss or has suffered diminished loss by reason of the fact that the vendor is entitled to be paid the purchase price or the balance thereof by the purchaser.

2.20 This part of the new section 35 of the Sale of Land Act 1962 is, we feel, sufficient to preclude any argument along the lines of that which succeeded in Ziel. Similarly, sub-section (2) also appears to rule out any claim to restitution by the insurer relying on the doctrine of subrogation. Amendment of section 47 of the Law of Property Act 1925 based on these provisions would remove some of the doubts as to the efficacy of the English legislation.

2.21 The problem highlighted in Ziel Nominees Pty. Ltd. v. VACC Insurance Co. is not, however, the only difficulty facing a purchaser who wishes to rely on section 47 to obtain insurance money payable to the vendor. Assuming that the insurance money is payable to the vendor despite him not having suffered any loss, or that it cannot be reclaimed by the insurer after the full price has been paid, there are other requirements to be satisfied before the purchaser can claim the money. These requirements are provided by section 47(2) and are set out in paragraph 2.9.

2.22 The first two requirements are that there is no contrary stipulation in the contract and that the insurer consents. The contract referred to in section 47(2) is presumably the contract of sale. General Condition 11(3) of

the Law Society's Conditions of Sale (1984 Revision) excludes entirely the operations of section 47 by substituting for it a contractual provision regulating the insurance position. Condition 11 will be considered shortly.[23] The National Conditions of Sale do not exclude section 47, and the condition that relates to insurance is considered further below.[24] The second qualification, that the insurer consents, is not thought to be a problem in practice. It is standard in insurance contracts for the policy effected by the vendor to extend to a purchaser under a contract of sale.

2.23 A clause, which is apparently in common use by the major insurers,[25] is as follows:

> If at the time of destruction or damage to any building hereby insured the Insured shall have contracted to sell his interest in such building and the purchase shall not have been but shall be thereafter completed, the purchaser on completion of the purchase, if and so far as the property is not otherwise insured by or on behalf of the purchaser against such destruction or damage, shall be entitled to the benefit of this Policy so far as it relates to such destruction or damage without prejudice to the rights and liabilities of the Insured or the Company under this policy up to the date of completion.

2.24 It seems clear that such a clause is sufficient to indicate a consent on the part of the insurer for section 47 to operate. There are, however, difficulties: the purchaser is not a party to the insurance contract and, unless he contributes a proportion of the premium, has supplied no

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23. See para. 2.34 below.

24. See para. 2.36 below.

25. E.J.D. Peverett, "Shifting the Insurance Burden: Another View", (1975) 125 N.L.J. 217, 218.

consideration for this clause in his favour. So far as we are aware, no insurer has yet resisted payment on the ground of absence of privity of contract, but this must remain a possibility.

2.25 The third requirement listed by section 47 before a purchaser can recover insurance money payable to the vendor is that he pay a proportionate part of the premium from the date of the contract. It is not clear whether the payment must begin as soon as the contract has been entered into, or if it is sufficient if the purchaser pays this sum upon completion.[26] Neither is it clear to whom the proportionate part of the premium should be paid; whether it is to the insurer or to the vendor. If it is necessary that the proportionate part be paid from the date of the contract, then section 47 will provide little protection for a purchaser as it is rare in practice for a purchaser to pay a proportionate part of the vendor's insurance premiums from this date.[27] Even if it is sufficient for the purchaser to pay a proportionate part at completion, however, it may nevertheless be unsafe for him to rely on the vendor's policy.

2.26 Even if the technical problems concerning section 47 are overcome, so that the purchaser may recover any monies payable to the vendor under his insurance policy, the further difficulty may arise that either no money is payable at all to the vendor, or the amount payable may be

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26. This is spelled out by National Conditions of Sale (20th ed.), No. 21(3) considered below at para. 2.37.

27. J.E. Adams and T.M. Aldridge, "Insurance of Domestic Property between Contract and Completion", (1980) 77 L.S. Gaz. 376.

insufficient to compensate for the loss. If the purchaser is entitled to take advantage of section 47, he can only claim what is payable to the vendor.[28] So if the vendor is uninsured or inadequately insured, the purchaser will be left with no protection.

2.27 There may be a number of reasons why no insurance money may be payable to the vendor upon the damage or destruction of his property. Most obviously, he may simply be uninsured, the most likely explanation of this perhaps being that his policy has lapsed through non-payment of premiums. Additionally, the vendor may be unable to claim where a condition in the policy has been breached with the result that the insurer can resist the claim. This situation could arise from non-disclosure of material matters when the policy was taken out, for example that the vendor has served a long prison sentence for robbery.[29] Again, if a house is left vacant for longer than a period specified in the policy, that policy may lapse unless an additional premium is paid.[30] In short, money may not be payable to the vendor for a number of reasons; a consequence which could be drastic for a purchaser who is seeking to avail himself of the protection offered by section 47.

2.28 The legislation enacted in Victoria seeks to deal with the problem of the insurance policy effected by the vendor being invalidated owing to some fault on the part of the vendor. Under section 35(9) of the Sale of Land Act

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28. See J. Birds, Modern Insurance Law, p.144.

29. Woolcott v. Sun Alliance and London Insurance Ltd. [1978] 1 W.L.R. 493.

30. See (1958) 55 L.S. Gaz. 775 where a warning is given with regard to this matter.

1962, an insurer shall not be entitled to deny liability to the purchaser because of a fault on the part of the vendor by reason of which the vendor would not be entitled to make a claim under the policy.

2.29 The aim of this provision, quite clearly, is to remove the need for duplication of insurance: to make it safe for a purchaser to rely on the policy maintained by the vendor. It would be quite possible to amend section 47 of the Law of Property Act 1925 along the lines of the legislation in Victoria. If such a course were considered to be desirable, we would welcome views as to whether the requirement that the purchaser should contribute a proportionate part of the insurance premium should be retained. A further matter which should be clarified is whether the vendor should be obliged to maintain his policy, and if so, what the consequences should be of a failure to do so. Under the Victoria legislation, it seems doubtful if a purchaser would be within section 35(9) of the Sale of Land Act 1962 where the vendor has simply let the insurance policy expire. In such circumstances, it might seem unreasonable to impose on insurance companies liability to pay out in respect of damage when an existing policy has simply been allowed to lapse.

2.30 Although amendment of the Law of Property Act 1925 along these lines would improve the position of the purchaser, it would not provide a complete solution to the problem. At present, it is a counsel of prudence for a purchaser to take out his own insurance policy upon entering into a contract to buy land, thereby probably duplicating the vendor's insurance. Although this may represent only a comparatively small amount of money to each individual concerned, when regard is had to the total number of transactions completed annually, the sums involved could be

quite significant. Avoiding the need for this would, we think, be desirable. This is not, however, our principal motivation. The need for duplication of insurance only arises because, at present, purchasers feel it necessary to take out their own policies to avoid the danger of a large financial loss should the property be damaged prior to completion. Unless by altering the law relating to insurance, this risk can be averted, then some purchasers will be unprotected and the need for the duplication of insurance will continue.

2.31 The Victoria legislation removes a good deal of the risk for a purchaser by enabling him to benefit from his vendor's policy despite the vendor himself being unable to claim owing to some fault on his part. This is similar in effect to a composite insurance policy whereby different interests in property are insured under one policy but non-disclosure or mis-statement by one insured will not prejudicially affect the claim of the other.[31] This will not enable a claim to be made, however, if the policy has lapsed, either because of non-payment of premiums or because of a condition in the policy such as one relating to the occupancy of the building. Accordingly, it would not be safe for all purchasers to rely on being able to recover under the vendor's policy.

2.32 An additional reason why, even after any reform of insurance law, it may nevertheless be prudent for the purchaser to take out his own insurance policy is that the vendor may be underinsured. It is only safe for a purchaser

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31. See General Accident Fire and Life Assurance Corp. Ltd. v. Midland Bank Ltd. [1940] 2 K.B. 388; Woolcott v. Sun Alliance and London Insurance Ltd. [1978] 1 W.L.R. 493.

to rely on the vendor's policy if the money payable would be sufficient to enable him to meet his financial obligations. If, as the law currently appears to be, he must complete the purchase despite the destruction of the buildings, he will be concerned to see that the money available to him will enable him to pay the vendor the agreed price and to have sufficient funds to rebuild the property. Even assuming that a building society would advance money after a house has been destroyed, a prospect which seems to us to be doubtful, that sum, together with any insurance money received under the vendor's policy may not be sufficient to meet his needs. The vendor may not have insured for a sufficient amount to take account of rising buiding costs.[32]

2.33 This point about underinsurance is well illustrated by the facts of a New Zealand case, Carly v. Farrelly.[33] A purchaser contracted to buy land and buildings from the vendor. As a term of the contract, it was agreed that the risk of damage passed to the purchaser who, despite this clause, had not insured. Before completion occurred, the buildings were destroyed by fire and the vendor received $7,300 from his insurer. The purchaser, who had paid the purchase price, failed in his action to recover this money from the vendor. It can be noted, however, that the purchase price, was $29,000. While it is true that some of this price would have reflected the value of the land without the buildings, it does appear that the property was significantly underinsured. Even if section 47 of the Law of Property Act 1925 were amended so as to ensure that a purchaser could always have recourse to money payable under an insurance policy maintained by the vendor, there would be

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32. Although many such policies are now index-linked.

33. [1975] 1 N.Z.L.R. 356.

no guarantee that that policy would provide adequate protection for him. Consequently, he would still be well advised to take out his own insurance policy.

Standard Conditions of Sale

2.34 Each of the sets of standard conditions of sale commonly used in practice contains conditions concerning insurance. Contracts which incorporate the 1984 revision of the Law Society's Conditions of Sale are not affected by section 47 of the Law of Property Act 1925. General Condition 11(1) provides that if the property is destroyed or damaged prior to actual completion and the proceeds of any insurance policy effected by or for the purchaser are reduced by reason of the existence of any policy effected by or for the vendor, the purchase price should be abated by the amount of such reduction.

2.35 This condition expressly excludes the operation of section 47 of the Law of Property Act 1925 which it replaces but does not, and is not intended to, avoid the need for the purchaser to take out his own insurance policy. Such a condition may be preferable to reliance upon section 47 but it does not meet the essential problems in this area. Further, it is difficult to see how the proceeds of any policy effected by the purchaser could in principle be reduced by reason of the existence of a policy effected by or for the vendor. Contribution clauses only apply to policies effected by or on behalf of the same party. If the purchaser is also added as an insured under the vendor's policy, there would be community of interest but the purchaser would not be prejudiced. If the vendor and purchaser have separate policies, whilst insurers may have rights of contribution inter se this would not affect the amount recoverable by the purchaser under his policy; though

if the loss were the fault of the vendor giving the purchaser a cause of action against him, the vendor's policy only would pay.[34]

2.36 The National Conditions of Sale (20th edtion) also make provision for insurance. Under General Condition 21(1), the vendor is not bound to maintain his insurance policy unless he is under an obligation to a third party to do so. This in practice will often cause the vendor to maintain the policy, because if the house is subject to a building society mortgage the building society will require an insurance policy to be maintained.[35] It is not uncommon, however, for houses to be sold after the mortgage has been redeemed, in which case the vendor will be under no contractual obligation to the purchaser to maintain his policy.

2.37 General Condition 21(3) enables the purchaser, at his expense, to require the vendor to obtain or consent to the endorsement of notice of the purchaser's interest on the policy and in such case, the vendor may require the purchaser to pay on completion a proportionate part of the premium from the date of the contract. This condition, if utilised, would appear to improve the purchaser's position from that which it would be if reliance were placed solely on section 47 of the Law of Property Act 1925. Even so, however, it would not provide total protection.

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34. See North British & Mercantile Insurance Co. v. London, Liverpool & Globe Insurance Co. (1877) 5 Ch. D. 569.

35. See H.W. Wilkinson, Standard Conditions of Sale of Land 3rd ed., (1982), p. 129.

2.38 If the purchaser's interest is endorsed on the vendor's policy, the purchaser would not be vulnerable to a claim by way of subrogation by the insurer. Thus the twin problems caused by Castellain v. Preston and Ziel Nominees Pty. Ltd. v. VACC Insurance Co. would be resolved. If, however, there is a joint policy which is voidable at the instance of the insurer, the purchaser would be in no better position than the vendor.[36] This difficulty could be avoided if the purchaser's interest were to be endorsed upon the policy in such a way that the insurers agree to insure each for his own interest. However this will not overcome any difficulties arising through underinsurance.

Conclusions

2.39 We consider therefore that this part of the law of insurance does not offer satisfactory protection to a purchaser: if he has not independently insured the property he has contracted to buy, it is by no means clear that he will be able to benefit from an insurance policy maintained by the vendor. This is because neither the Fires Prevention (Metropolis) Act 1774 nor the Law of Property Act 1925 is free from doubt in terms of efficacy.. If the doubts are well-founded, then various consequences flow. Most important, the purchaser may suffer a catastrophic loss, having to pay the full purchase price for a badly damaged but, so far as he is concerned, uninsured property.

2.40 To avoid this potential calamity, the purchaser, as the law currently stands, is well-advised to take out his own policy, thereby duplicating the vendor's insurance

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36. Central Bank of India Ltd. v. Guardian Assurance Co. Ltd. and Rustomji (1936) 54 Lloyd's Rep. 247.

policy. This seems to be a waste of money: a waste which will continue, unless the law is altered either to make it safe to rely on the vendor's policy or to leave the risk with the vendor.

2.41 Insofar as insurance law is concerned, some of the existing doubts could be resolved by legislation. In particular, the difficulty exposed by the Ziel case in Australia should be removed. To that end, we could recommend the enactment of legislation modelled on that in Victoria, whereby the purchaser would recover insurance monies payable to the vendor and that the monies would be payable despite the vendor either having received the purchase price or being entitled to receive it.

2.42 Such an amendment would remove one serious difficulty facing a purchaser. Others would, however, remain. These are that the policy may be invalid or have lapsed, or the property may be underinsured. Although legislation in Victoria provides that insurance money should be paid to a purchaser despite the policy being voidable owing to the vendor's fault, we have doubts as to the fairness of this approach. Even if this course were taken, however, the policy may have lapsed or provide insufficient cover. These factors alone are good reasons for the purchaser to continue the current practice of insuring himself.

2.43 Our main concern in reviewing this area is to prevent a purchaser suffering ruinous loss as a result of destruction of or damage to property prior to completion. Incidentally, we also regard it as advantageous to end the need for the wasteful practice of duplication of insurance. The risk of such loss could be reduced but not eliminated by

the amendment of section 47 of the Law of Property Act 1925 and for that reason we would provisionally recommend that this be done. To summarise, these amendments would enable the purchaser to recover from the insurer the amount that the vendor would have been entitled to receive had there been no contract of sale in existence. It should also be made clear that it is not a requirement that he has actually paid a proportionate part of the premiums as from the date of the contract.

2.44 These provisional proposals, if enacted, would, we feel, strengthen the purchaser's position. There would nevertheless remain a residual but real area of risk. Accordingly, we do not see these proposals as providing a comprehensive solution to the problems. We, therefore, canvass in Part III of this working paper more radical proposals for reform. We would be particularly interested, however, in receiving comments on the question of insurance.

PART III
PASSING OF THE RISK - OPTIONS FOR REFORM

3.1 In Part I of this working paper, we examined the law which governs the position of vendor and purchaser *pending completion of a contract for the sale of land.* Their respective rights and obligations are considerably affected by the maxim of equity, whereby the purchaser is regarded as the beneficial owner of the property from the date of the contract. The principal effect of this maxim is that the risk of damage to the property during this period passes to the purchaser.

3.2 Our provisional view is that the law is unsatisfactory. It is uncertain in scope, in that arguments can be put that the explanation of why the risk is said to pass to the purchaser is unconvincing. Secondly, the ambit of the vendor's duty to take care of the property is uncertain in its application. The resolution of this difficulty will be crucial for a purchaser who is uninsured. This issue may also be important if both parties are insured in that a dispute may ensue between the two insurance companies as to who should be liable to pay out for the damage.

3.3 We feel that these uncertainties are themselves undesirable and that it would in any event be desirable to eradicate them from the law. The vital question is whether the purchaser or the vendor should bear the risk of damage to the property pending completion. Our provisional view is that it should remain with the vendor. Our reasons for this view are as follows.

3.4 The law as it currently stands may be said to represent a serious trap for the purchaser. If he has not taken out insurance on the property from the date of exchange of contracts, he runs the risk of catastrophic loss should it be seriously damaged or destroyed. Because it is usual for the purchaser not to go into possession until completion, he is at risk with regard to matters outside his control. This we regard as unjust.

3.5 The vendor would not be unduly prejudiced if he were to bear the risk for this period. It is true, as we pointed out in Part II of this working paper, that the vendor's insurance policy may not provide adequate cover. This may be because the vendor is underinsured or, more seriously, the policy may be voidable at the instance of the insurer or may have lapsed. While such a person is clearly at risk, entry into a contract of sale does not increase that risk.

3.6 To sum up, we consider that changing the law would remove a potential hardship for the purchaser without significantly prejudicing the position of the vendor. In addition, it is also possible that some reduction in conveyancing costs might be achieved through the removal of the need for both parties to maintain insurance policies for this period. In reaching this conclusion, we are encouraged by the fact that a number of other common law jurisdictions have thought it necessary to reform the law in the direction which we are advocating.[1] We put forward for

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1. Conveyancing (Passing of Risk) Amendment Act 1986 (New South Wales); Sale of Land (Amendment) Act 1982 (Victoria). Recommendations for change to favour the purchaser have been made by the Law Reform Commission of Tasmania, Report No. 36 (1984), para. 2.14 and the New Zealand Contracts and Commercial Law Reform Committee, Aspects of Insurance Law (2), paras. 3.99-9.15.

consideration five options, each of which would go some way to meet our objectives.

Option No.1: Abolition of trust

3.7 The underlying reason why the risk of physical damage to the property is said to pass to the purchaser as a result of entry into a valid contract of sale is that the purchaser is regarded as acquiring beneficial ownership in the land from that date. The legal estate is held on trust for him by the vendor. The vendor is thus, as trustee, subject to a duty of care with regard to the property and the purchaser, as beneficial owner, is the person to bear the risk of the property being damaged or destroyed.

3.8 As has been seen, the trust which is created is a most unusual type of trust. The incidents of the trust are quite different from those that normally arise when a trust has been created. Our first option, therefore, is to alter the time when the equitable interest in land passes and thus the time at which a trust arises. If it were to be provided that the equitable ownership cannot pass separately from the legal ownership, no trust would arise. It could be provided that a trust should arise only when the purchase money has been paid, only when the purchaser goes into possession or only when both these events have occurred.

3.9 However, all these possibilities give rise to difficulties. It would be very difficult to provide that equitable ownership could not pass separately from legal ownership in the context of the sale of land. Payments in advance possibly by third parties must create equitable interests in the land. It is by no means clear that such a proposal would have the effect of changing the moment when

risk passes. Although the passing of risk is generally thought to be a result of the trust arising, it could be held to pass as a result of an implied term in the contract.[2]

3.10 Would it be preferable to provide that a trust can only arise once all or part of the purchase price has been paid? If a deposit has been paid on exchange of contracts, then this is a part payment of the purchase price. Rental purchase schemes also give rise to part payment of the purchase price. It seems to us that apportioning liability where only part of the price has been paid could give rise to unnecessary complexity. It would not prevent the need for both parties to insure. If the whole price has been paid, but the purchaser is not in possession, he still does not have the control over the property that seems to us to be desirable if he is to be at risk.

3.11 There is a more important objection to reforming the passing of risk by abolition of or change to the trust that now arises on exchange of contracts. The existence of the trust affects the relationship of vendor and purchaser quite apart from the passing of risk. It affects their rights and duties, and the nature of the property that they hold. Altering these is unnecessary if all that is wanted is to affect the passing of risk and it would be difficult to judge what the effects of such a change might be. For all these reasons we do not recommend this option.

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2. M.P. Thompson, "Must a Purchaser Buy a Charred Ruin?" [1984] Conv. 43, 50.

Option No.2: Risk to pass on completion

3.12 If altering the time at which equitable ownership can pass is likely to give rise to the problems outlined above, it may be better to separate the passing of risk from the passing of equitable ownership. Our second option is therefore that the risk should pass on completion of the transaction when the estate sold in substance passes to the purchaser.[3] This would bring the sale of land into line with the sale of goods.

3.13 When goods are sold, the risk passes when the property in the goods passes, subject to a contrary agreement.[4] In many contracts for the sale of goods property passes at the time of the contract,[5] but this can be altered by the parties and it seems that "very little is needed to give rise to the inference that the property in specific goods is to pass only on delivery or payment".[6] Thus the gap between contract and completion that arises on a sale of land can, and often does, arise on the sale of goods. We are not aware that the basic provision as to the

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3. With registered land the legal estate vests in the purchaser as at the date of application for registration: Land Registration Act 1925, ss.19, 22; Land Registration Rules 1925, rr.83, 85. If an equitable interest only is sold, the risk should similarly pass as at completion.

4. Sale of Goods Act 1979, s.20(1),"Unless otherwise agreed, the goods remain at the seller's risk until the property in them is transferred to the buyer, but when the property in them is transferred to the buyer the goods are at the buyer's risk whether delivery has been made or not."

5. Sale of Goods Act 1979, s.18.

6. R.V. Ward Ltd. v. Bignall [1967] 2 All E.R. 449, 453 per Diplock L.J.

passing of risk with sale of goods has given rise to any significant complaint.

3.14 If there were to be a statutory provision to the effect that risk passed on completion, this would have to be subject to a contrary agreement. It may be that such a provision would be ineffective because vendors would simply contract out of it as a matter of course. We would like to hear from those with experience of conveyancing whether this would be so. Even if it were, such a provision might still be worth while because it would require a deliberate effort to contract out of it and at least the purchaser would have drawn to his attention the fact that he was to be put at risk.

Option No.3: Vendor's contractual obligation

3.15 The previous option sets out a fairly simple approach to the passing of risk. In the third option we suggest a similar approach so far as the timing of the passing of risk is concerned but a more detailed provision for the vendor's obligations. What we propose is that the vendor should be obliged to convey the property to the purchaser in the physical condition it was in at the date of the contract. Possibly there should be an exception for fair wear and tear, and if this option is liked we would particularly welcome views on this point.

3.16 We should at this stage spell out the consequences of this option. First, it does not impose any duty on the vendor with regard to the property at the time when the contract is entered into. It will remain for the purchaser and his mortgagee to satisfy themselves as to the condition of the property before contracts are exchanged. If,

however, the property is damaged after exchange of contracts then, unless the property is restored to the condition it was in at the time of the contract, the vendor will be in breach of contract. The consequence of this will depend on the nature and extent of the damage which has actually occurred.

3.17 If the damage which occurs to the property is fairly minor, the vendor would be liable to compensate the purchaser for the cost of repairing the damage but the purchaser would be bound to complete the contract. If, however, the damage was serious, for example if a house was gutted by fire, then the purchaser should be entitled to terminate the contract and also claim damages; those damages to be assessed in accordance with normal contractual principles. The vendor is regarded as being in breach of contract because he is unable to convey that which he has contracted to convey.

3.18 In determining how substantial the damage is, the matter is clearly one of degree. We suggest that the appropriate test is that which operates currently in the case of misdescription of the property. The test applied in this event is that the vendor cannot compel the purchaser to complete if the misdescription is:

> so far affecting the subject-matter of the contract that it may reasonably be supposed, that, but for such misdescription, the purchaser might never have entered into the contract at all, in such case the contract is avoided altogether.[7]

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7. Flight v. Booth (1834) 1 Bing. N.C. 370, 377 per Tindal C.J.

3.19 This test seems appropriate in that misdescription may often relate to the physical state of the property as is the case where it has been damaged. We would emphasise, however, that the test should be objective and not related to the requirements of the individual purchaser.[8] In addition, we would point out that the effect of substantial damage is not to enable the purchaser simply to rescind the contract ab initio and merely recover his deposit. Rather its effect is that the purchaser may terminate the contract and claim damages.

The proposal in practice

3.20 In the case of minor damage, the position would be relatively straightforward. When the damage occurs, the vendor can either repair it or convey the property to the purchaser in its damaged condition. As this will entail a breach of contract, the purchaser would be entitled to an abatement of the purchase price to reflect that damage. In either case, the vendor would normally recover his financial loss from his insurer.

3.21 Two comments can be made as to this. First, in the context of the scope of the vendor's obligation to repair, it is probable that no higher duty is imposed on the vendor than is currently the case. At present, it seems that the vendor is obliged to maintain the property in good repair and that, at least until the date fixed for completion, he should effect any necessary repairs.[9] In cases falling short of total destruction, therefore, this proposal may not

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8. This is also the rule in the case of misdescription: Ridley v. Oster [1939] 1 All E.R. 618, 622 per Oliver J.

9. See paras. 1.36-1.40 above.

significantly alter the vendor's position. The second point is that in the preceding paragraph we refer to the vendor claiming on his insurance policy. It is possible, however, that the damage may be caused by an uninsurable event. For example, it is not possible fully to insure against subsidence. In addition, if a rise in the water table causes flooding, and damage ensues as a result,[10] such damage is not within normal insurance policies. The question arises as to whether the vendor should be liable for all damage and deterioration to the property, fair wear and tear excluded, or only for that damage which is a commonly insurable risk.

3.22 Our provisional view is that no distinction should be drawn between types of damage and that the vendor's obligation should not be qualified to extend only to commonly insurable risks. We are of this view for various reasons. First, it is consistent with our general approach to view the matter from the standpoint of asking what it is that the vendor should be obliged to convey, rather than simply focussing on what risks should pass in isolation. Secondly, the vendor has been at risk of these uninsured events occurring throughout the period of his ownership of the land. Entry into a contract of sale does not expose him to additional risk. Our general approach is that the risk of damage to the property should be carried by the vendor. Finally, we intend to propose that the parties be free to agree such contractual terms relating to the physical condition of the property as they see fit. If the parties wish to distinguish between different types of risk in the contract, they will be free to do so. Accordingly, while we recognise that our proposal could be modified in terms of

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10. Cf. Post Office v. Aquarius Properties Ltd. [1987] 1 All E.R. 1055.

effectively limiting the vendor's responsibility to insurable risks only, we are provisionally opposed to this course of action. We would be grateful for views on this issue.

Chain transactions

3.23 We are conscious that it is very common for a contract for the sale of land to be part of a chain of transactions. It is necessary, therefore, to consider how our proposal would operate in this circumstance. We take as a scenario, a situation where V has contracted to sell his house to P and at the same time has contracted to buy from A. P, meanwhile, has contracted to sell his house to B. These transactions are syncronised so that they are all to be completed on the same day but, between contract and conveyance, V's house is destroyed.

3.24 The effect of our proposal is as follows. P would be entitled to terminate his contract with V but, nevertheless, be required to convey his own house to B. At that point, he will have the equity value of his own house, having redeemed any outstanding mortgage, and also have finance arranged to buy another property. He will be in a position akin to that of a first time buyer and should be able to buy another house quickly. Assuming the vendor is adequately insured, he will be in receipt of insurance monies equivalent to his actual loss, which may be the market value less the value of the site or else, depending on the terms of the policy, the cost of reinstatement.[11] This will be used to redeem any outstanding mortgage on that

11. Leppard v. Excess Insurance Co. Ltd. [1979] 1 W.L.R. 512.

property, the balance going towards the purchase of A's house which he will still be bound to complete.

3.25 We think that, although there will be some disruption to the chain, this is probably inevitable if one of the houses to be sold is destroyed. If our proposal is adopted, however, we are of the view that the disruption on the scenario that we envisage will be relatively minor. We should, however, deal expressly with the increased liability of the vendor.

3.26 Under our proposal, the vendor is to be regarded as in breach of contract if he cannot convey the property in the physical condition it was in at the date of the contract. He may, therefore, be liable in damages to the purchaser. These damages would reflect any increase in house prices between the date of the contract and the date of the destruction of the property, which is the date when the contract is lost. Such damages, and other incidental expenses recoverable by the purchaser, would not appear to be recoverable by the vendor under his insurance policy. This may prompt the vendor's solicitor or other conveyancer to advise him to take out insurance against this potential legal liability from the date of the contract. If this occurred, then the saving in conveyancing costs achieved by removing the need for the purchaser to insure would, to a certain extent, be offset by the additonal premium paid by the vendor.

3.27 There are several responses that can be made to this. First, it is already the case that the vendor may be liable in damages to the purchaser if he is unable to fulfil his contractual obligations. It is not normal practice to insure against this liability and it is not obvious that

this practice would change by the addition of another potential head of liability. If, out of caution, additional insurance were taken out, the premium would be likely to be less than a purchaser currently has to pay, because the potential liability would be much less. We would envisage, therefore, a small net saving in conveyancing costs. Most important to us, however, is that our main reason for changing the law is to remove the trap which currently exists for purchasers rather than specifically to save money in the conveyancing process. That is simply an incidental benefit to our proposal. We are not, therefore, unduly troubled by the increased potential liability of the vendor. The answer to this may be the inclusion of a provision in insurance policies dealing with liability to purchasers in the event of destruction of the property. We would envisage that such increased cover could be obtained at a relatively minor cost.

Alternative dates for passing of the risk

3.28 If our provisional proposal is accepted, the vendor will fulfil his obligation if the property is in the same physical condition as it was in at the date of the contract, when the vendor executes a conveyance or transfer of the property.

3.29 The three other plausible occasions when it might be thought to be appropriate that the purchaser should bear the risk of damage to or destruction of the property are the date when the purchaser goes into possession, should that date precede completion, the contractual date fixed for completion and the date when the purchase price is paid. The legislation enacted in New South Wales provides that the risk of damage to the property should remain with the vendor until completion or, if so stipulated, until the purchaser

goes into possession, whichever is the earlier.[12] The reason for passing the risk to the purchaser from the date when he goes into possession is that from that date he has control of the property and, consequently, he should bear the risk of damage to it. We see the force of this argument, and would be prepared to consider following it if it received support on consultation.

3.30 Should it be thought desirable to do so, the risk could certainly be allocated to the purchaser from the date he went into possession or the date fixed for completion. A term to this effect could be implied by statute into the contract of sale. However, such a term would not necessarily be without difficulties. Even if the purchaser has gone into possession, it is not inevitable that the contract will ultimately be completed. Some misrepresentation may emerge, or the vendor's title may prove to be defective. Although at common law the taking of possession prior to completion may amount to an acceptance of the vendor's title, thereby precluding objection to it, this result does not inevitably follow. The Law Society's Conditions of Sale (1984 Revision) provide that if the purchaser is in occupation he must insure the property.[13] But both standard sets of conditions of sale contain conditions to the effect that occupation by the purchaser

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12. Conveyancing Act 1919, s.66K inserted into the Act by Conveyancing (Passing of Risk) Amendment Act 1986, Sched.1.

13. Condition 18(4)(c) - the obligation to insure only arises under the condition where the purchaser is in "occupation", not "possession", thereby excluding the situation where the purchaser is merely in receipt of rent or profits. Consideration would have to be give to whether the risk should pass when the purchaser goes into occupation rather than possession in the wider legal sense.

prior to completion does not amount to an acceptance of the vendor's title.[14] Consequently, even if the purchaser has gone into occupation, the vendor should maintain his own policy. Allocating the risk to the purchaser at this stage would reintroduce the problem of duplication of insurance which we are keen to avoid.

3.31 In addition to this, there is the consideration that it might not always be easy to determine whether possession has in fact been taken. It is common for a vendor to allow a purchaser a right of access prior to entry into the contract and this may also be given after exchange of contracts.[15] This is likely to occur if the vendor is not himself in occupation and the purchaser wishes to start decorating some or all of the rooms. Should the property be damaged at this time, it would be necessary to determine whether or not the purchaser had actually taken possession. Alternatively, the purchaser may have taken possession and since vacated the property, and it might not be thought desirable for the risk to oscillate between vendor and purchaser.

3.32 Another important question is the liability of the purchaser if he damages the property while in possession. Clearly if the general position is to be that the vendor remains liable while the purchaser is in possession, it will be essential that a vendor who lets a purchaser into possession, protects himself by contract against such

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14. National Conditions of Sale (20th ed.), No. 8(3); Law Society's Conditions (1984 Rev.), No. 18(3).

15. In Schindler v. Pigault (1975) 30 P. & C.R. 328, Megarry J. left open the question whether a purchaser had a right of reasonable access after exchange of contracts.

negligence. However, despite this difficulty and for the reasons above, our tentative view is that the risk should remain with the vendor until completion.

3.33 Passing the risk to the purchaser from the contractual date of completion also seems to us to be undesirable. It may be that the delay in completion is not the purchaser's fault and he may become entitled to terminate the contract. Again, it would seem advisable for the vendor to maintain his own insurance policy until completion actually occurs.

3.34 We have already discussed passing the risk to the purchaser once the purchase price has been paid, in the context of Option 1. The reasons we gave there, that there are difficulties where partial payment has been made, and that the purchaser still has no control over the property, apply to this proposal too. For these reasons, we think that the disadvantage of an implied term assigning the risk to the purchaser prior to actual completion outweigh any advantages. We would, however, be grateful for any views on this matter.

Leasehold property

3.35 Our discussion so far has centred on the sale of freehold land. A question which should be considered is whether our proposal with regard to the physical condition of the property should apply equally to contracts for the sale of leasehold property. In principle, we see no reason why it should not, particularly when it is the case that it is by no means uncommon for residential property to be sold by way of a long lease. In such a situation, the same considerations apply as is the case for the sale of freehold

property. In addition, we do not see any reason to distinguish between residential and commercial properties, since this would be to introduce an at times difficult distinction into another area of the law.

3.36 We would stress that our proposal would not alter the law with regard to the state of the property to be leased. Such matters as whether the property must be fit for human habitation or in a good state of repair will continue to be governed by the general law. All our proposal seeks to do is to place the vendor under a duty to maintain the property in the same condition it was in at the date of the contract to grant or assign a lease. Equally, once the lease has commenced, the respective obligations of the parties with regard to the physical condition will be governed by the lease itself, as modified by the general law.

3.37 One further matter which should be considered in the context of leasehold property is whether our proposal should apply when the vendor of an interest is not himself responsible for repair of the property. For example, if the contract is to assign a lease and the landlord is subject to an obligation to repair, either statutory or by covenant, the issue is whether the assignor should be liable to the assignee in respect of pre-assignment damage to the property. Again, we see no reason in principle why this should not be the case. If the property is damaged or destroyed, the assignor cannot assign what he has contracted to assign. The fact that the landlord may be under an obligation to the assignor should not, in our view, alter the obligation owed by the assignor to the assignee. We would, however, appreciate views on this matter.

Sub-sales

3.38 The final situation to consider is how our proposal would operate in the case of sub-sales: where A contracts to sell to B who, before completion of that contract, contracts to re-sell the property to C. The issue is how liability is apportioned should the property be damaged or destroyed prior to completion.

3.39 Our proposal as to the vendor's obligation would have the following effect. A would be unable to convey the property to B in the same condition as it was in at the date of the contract and would consequently be liable in damages to him. B, in turn, would be liable to C. If the damage was so serious that the A-B contract was terminated, the question would arise as to whether the damages payable to B would include any lost profit on the re-sale. The answer to that would depend on the normal rules governing remoteness of damage: whether A knew that B intended a re-sale.[16] This position seems unobjectionable to us and we do not propose, therefore, to suggest any modification to our proposal to deal with sub-sales.

Contracting out

3.40 An important question that now arises is whether the parties should be able, by express contractual term, to abrogate or modify the vendor's obligation outlined above, thereby reallocating the risk of damage to the purchaser.

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16. See The Rule in Bain v. Fothergill (1986), Working Paper No. 98, paras. 1.9-1.12.

3.41 A case can be made for preventing the parties from doing this. It could be argued that if the contract provided that the risk should pass to the purchaser, then he would need to insure the property. The vendor would in any event have to maintain his own policy, and the result of the reallocation of the risk would be that a duplication of insurance would occur; a wasteful practice which we are keen to eradicate.

3.42 This consideration we see as a practical reason why the parties might not normally wish to introduce such a term rather than as a reason of principle why they should be prohibited from doing so. The effect of our proposal is to stipulate what, as a matter of general law, the vendor's obligation should be with regard to the physical condition of the property. As with other obligations that the vendor has, however, we do not see why as a matter of principle the parties should not be free to contract in whatever terms they choose. This they may opt to do by either removing or limiting the vendor's liability to pay damages in the case of the destruction of the property. In the case of sub-sales it may be regarded more convenient by the parties for either the vendor or the sub-vendor not to be under the general obligation we propose. Although conscious that Schedule 1 to the Conveyancing (Passing of Risk) Amendment Act 1986 in New South Wales prohibits contracting out insofar as the sale of dwelling-houses is concerned, we propose that the parties should be at liberty to agree that the risk should pass to the purchaser from the date of the contract.

3.43 Another argument can be put in favour of allowing the parties to contract out of our proposal if they choose to do so. It is that one reason for advocating a change in the law is that a purchaser may not know that he bears the risk and neglect to insure the property. If the contract

expressly states that the risk passes to him, he will be alerted to the need to insure. If he then does not do so, it would seem that he is the author of his own misfortune. We would, however, emphasise that this is a provisional view and we would particularly welcome comments on this matter.

Frustration

3.44 As has been seen in Part I of this working paper, the application of the doctrine of frustration to contracts for the sale of land is uncertain.[17] If our proposal were implemented, much of this uncertainty would disappear. If the property were destroyed, the vendor would be unable to fulfil his contractual obligation and would simply be in breach of contract. If the parties have, by an express contractual term, varied the vendor's obligation, then they will necessarily have provided in the contract what the position is to be if the property is destroyed. The doctrine of frustration would then be inapplicable.

3.45 The only remaining scope for the doctrine would be where it is envisaged that the land is to be used for a particular commercial purpose and, for example, because of some governmental action, that purpose became impossible. We do not think it would be appropriate to seek to legislate in advance what circumstances would cause such a contract to be frustrated. Individual contracts will vary, as will the event which inhibits the purchaser's plans. We feel that this issue is best left to case law. We therefore make no proposals as to the law of frustration.

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17. See paras. 1.61-1.69 above.

Should legislation be retrospective?

3.46 A case can be made for enacting that this change in the law should operate retrospectively. This is that, because the vendor will in any event be insured, he will not be substantially prejudiced by our proposal. Conversely, making the legislation retrospective may relieve a few purchasers from the risk of catastrophic loss should they have entered into contracts to buy land without effecting insurance of it. We do not feel, however, that this case outweighs the usual presumption against retrospective legislation. Our proposal would make a fairly radical change in the law and would impose some additional liability on a vendor. To do so without giving him the chance either to insure or to negotiate a modification of that obligation with the purchaser would, in our view, be unfair. We propose, therefore, that this change in the law should take effect only from a date stipulated in the legislation.

Option No.4: A right of rescission

3.47 Our preferred option is to provide that, subject to any agreement to the contrary, the vendor should be under a duty to convey the property to the purchaser in the same condition as it was in at the time of the contract. The effect of this proposal is that the risk of damage to the property remains with the vendor until conveyance or our alternative possibility, the time when the purchaser takes possession. A second route by which this result could be achieved is to follow the model adopted in New South Wales which gives the purchaser a right to rescind should the property be seriously damaged prior to completion.

3.48 Section 3 of and Schedule 1 to the Conveyancing (Passing of Risk) Amendment Act 1986 operate to insert new

provisions into the Conveyancing Act 1919. Section 66K(1) provides that the risk in respect of damage to land shall not pass under a contract for the sale of land until either the completion of the sale or, if so stipulated, the purchaser enters, or is entitled to enter, into possession of the land whichever is the sooner. Section 66L(1) then gives the purchaser the right to rescind the contract if the property is substantially damaged before the risk has passed to him. This right must be exercised within twenty-eight days of the purchaser becoming aware of the damage. The effect of rescission is that all money paid by the purchaser under the contract shall be repaid to the purchaser and both parties shall be relieved of any liability under the contract, except for any liability arising out of a breach occurring before the date of rescission.[18] The Act then goes on to empower the court to award specific performance with an abatement of the purchase price in appropriate cases.[19]

3.49 We have already considered the question of whether the risk should pass to the purchaser from the time when he goes into possession and have concluded very tentatively that this would not be desirable.[20] If any legislation were to be modelled on the New South Wales Act, we would, therefore, exclude any reference to the purchaser going into possession.

3.50 Apart from the issue of when the risk should pass, we found difficulty with the right of rescission which the

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18. Conveyancing Act 1919, s.66L(4)(a), (b).

19. Ibid., s.66M(1).

20. See paras. 3.30-3.32 above.

Act confers. Under section 66L, it is not clear whether rescission means rescission ab initio or termination of the contract.[21] Our uncertainty as to this stems from the right of the purchaser to recover money paid under the contract. If this means he has a right to restitution of money paid to the vendor, then rescission is being used in the former sense. In that event, the parties are restored to the position they were in prior to entering the contract. Consequently we cannot see why the purchaser should recover damages for other breaches of the contract which occurred before the property was damaged. If, alternatively, the purchaser can recover all the money he has spent as a result of entering into the contract, to include such items as legal costs, then it would seem that the purchaser is actually terminating the contract and claiming damages. These damages are limited, however, in the same way that the rule in Bain v. Fothergill[22] operates so to do in cases of defects in title. We have already recommended that this rule should be abolished[23] and would be unhappy to see a similar restriction on damages introduced, albeit for a different reason.

3.51 In giving the purchaser the right to withdraw from the contract if the property is substantially damaged prior to completion, the issue seems to be whether he should also be entitled to damages. In principle we think that he should be. If the risk of damage does not pass to the purchaser until completion and the property is destroyed or

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21. See Johnson v. Agnew [1980] A.C. 367.

22. (1874) L.R. 7 H.L. 158.

23. Transfer of Land, The Rule in Bain v. Fothergill (1987), Law Com. No. 166.

damaged before that date, the vendor cannot convey what he is contractually obliged to do. This inability to fulfil his contractual obligation necessarily involves a breach of contract and we think that the purchaser should have available the whole range of contractual remedies which are available for any other breach of contract.

Option No.5: A practice suggestion

3.52 While our provisional view is that Option 2 would be a desirable reform to the law, we would also like to put forward a suggestion that does not require legislation. Although the law at present imposes a trust on the vendor and in so doing passes the risk to the purchaser, we believe there is no reason why the parties should not provide in their contract of sale that the risk shall not pass and, if they so wish, give the purchaser a chance to withdraw if the property is damaged. Naturally vendors may not wish to see such terms introduced. However, the purchaser may be able to negotiate for such terms as part of the overall contract, and may be willing to pay a slightly higher price in return for not having to insure on his own account.

3.53 Such clauses are common in Scotland where, as in England and Wales, the risk would otherwise pass to the purchaser. A typical one might state:

> The subjects including the whole garden ground will be maintained in their present condition, fair wear and tear excepted, and will remain at the seller's risk until the said date of entry. In the event of the subjects, or any part thereof, being substantially damaged or destroyed by fire or other cause prior to the said date of entry the purchaser will be entitled to resile from the bargain without

any claim or penalty being due to or by either side.[24]

3.54 If such a contractual term became common practice in this country, perhaps as a standard condition of sale, then most of the problems identified in this working paper would be resolved. At present, however, such clauses are apparently not used by English practitioners. Why not is unclear. However, it is still our provisional view that the law should be changed so that the risk remains with the vendor, unless the parties agree otherwise. In other words, we would reverse the present position as a matter of law not merely of practice. We are not yet persuaded that it would be satisfactory to leave the position unaltered. This would put the onus of changing current practice on the parties by including special conditions of sale reallocating the risk, whilst waiting for the draftsmen of the standard sets of conditions to amend these contracts. Not all purchasers, nor indeed all vendors, of land are represented by solicitors, or licensed conveyancers, capable of appreciating the advantages and disadvantages of any such amendment. Do-it-yourself conveyancers should be covered. We are, therefore, at present opposed to this suggestion as a long-term solution. However in the short-term practitioners could consider its immediate adoption as an interim measure.

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24. J.H. Sinclair, Handbook of conveyancing practice in Scotland, (1986), p.210.

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